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SPECIAL PURPOSE ENTITIES

THE TREATMENT OF SPECIAL PURPOSE ENTITIES IN THE NETHERLANDS

Note by Statistics Netherlands

Summary

Special purpose entities are daughter companies of foreign multinational enterprises that are set up in a specific country, often for fiscal reasons. Most of their financial and related income transactions are large and take place with companies in foreign countries. This paper will explain how special purpose entities can be treated in a nation's National Accounts. It will describe different types of special purpose entities identified in the Netherlands and will show how special purpose entities are treated statistically in the Netherlands. Many special purpose entities have their residence in the Netherlands: at the end of 2008 there were more than 12,000 special purpose entities recorded in the Netherlands.

I. INTRODUCTION

1. The Conference of European Statisticians decided at its 2007 plenary session that a Group of Experts on the Impact of Globalisation on National Accounts be created to review the main distortions in the compilation of national accounts caused by the growing globalisation of economies and to develop recommendations on how to deal with these distortions. The election of the Group of Experts was approved by the Executive Committee of the United Nations Economic Commission for Europe (UNECE) at its twentieth session (27 February 2008). The Group of Experts will work in cooperation with Eurostat and the Organisation for Economic Co-operation and Development (OECD). The present document contains an input for the preparation of the Recommendations.

2. Special purpose entities (SPEs) are daughter companies of foreign multinational enterprises that are set up in a specific country, often for fiscal reasons. Most of their financial and related income transactions are large and take place with companies in foreign countries. Many SPEs have their residence in the Netherlands: at the end of 2008 there were more than 12,000 SPEs recorded in the Netherlands. Although the economic relevance of SPEs is normally small, they may account for large financial flows. In the Netherlands, for example, they accounted for more than 1.6 billion euros in assets and liabilities on their closing balance sheets in 2007. This amount equals almost three times gross national product (GDP). Annex I shows some key figures of SPEs in the Dutch National Accounts.

3. Starting with the major revision of 2001, Statistics Netherlands included SPEs in Dutch national accounts. Introducing this specific group of companies in the national accounts made it necessary to think of answers to several conceptual questions regarding the treatment of SPEs, because there were no clear guidelines or definitions in international manuals. Similar questions are posed by and are on the research agenda of the Group of Experts on the Impact of Globalisation on National Accounts.

4. In order to cope with these questions a project group was set up in the Netherlands, consisting of representatives of both Statistics Netherlands (Centraal Bureau voor de Statistiek, CBS) and the Dutch Central Bank (De Nederlandsche Bank, DNB) that collects the data on SPEs. The group was assigned to formulate a decision tree by which SPEs could be detected. In this decision tree, all criteria concerning the definition of Dutch SPEs should be included.

5. In new international manuals SPEs have received much more attention and guidelines on how to cope with these entities are given. In section III new guidelines on SPEs in the System of National Accounts 2008 (SNA2008), the sixth edition of the IMF Balance of Payments and International Investment Position Manual (BPM) and the fourth edition of the OECD Benchmark Definition of Foreign Direct Investment (BD4) will be covered and will be compared with the Dutch approach on SPEs as of now.

6. On the Group of Experts research agenda, several questions are posted on the subject of SPEs. These are:

- (a) What criteria can be used to determine the residency of the relevant unit?

- (b) How can SPEs be defined and how to deal with complex groups of units owned by non-residents?
- (c) How should the relevant monetary flows be recorded; as service, capital formation, income or financial transaction?
- (d) How to group SPEs: financial and holding companies, royalty and license companies, factoring companies, etc.?
- (e) How to deal with SPEs created by government?

7. Question d will be covered first, in section II, because it gives a good impression of what types of companies we are dealing with. Government created SPEs will not be discussed in this paper, for the reason that Statistics Netherlands has not identified this specific group of SPEs in the Netherlands. Questions a through c will be dealt with in the rest of the paper, along with international guidelines and problems that arise in the methods used. The paper will conclude with some suggestions on future work and ideas on how to create better statistics on SPEs.

II. TYPES OF SPECIAL PURPOSE ENTITIES

8. The research agenda identifies three types of SPEs. In the Netherlands however, two newly defined groups were added. In this section the five different types of SPEs will be illustrated shortly.

9. The first category consists of financing and holding companies. Financing and holding companies channel funds in a worldwide group on behalf of a non-resident mother company. Large cross-border financial transactions are typical for this type of SPE. The asset side of the balance sheet almost completely consists of financial assets and accounts receivable relating to foreign entities. In the Netherlands the financing and holding companies form, by far, the largest group of SPEs.

10. Royalty and license companies make up the second category of SPEs. These businesses have been given ownership of intellectual property rights by their parent companies and collect income in the form of royalties as fees on licenses or act as a cashier of their parent company in the invoice of royalty and license fees (in which case the SPE usually only owns sublicenses). The flows of the royalty and license companies are recorded as exports of services. The revenues are passed on to the parent company.

11. The third group of SPEs are factoring companies, conducting the invoice of sales of the worldwide company on behalf of the (non-resident) parent company. Although the sales are not related to the domestic company, the payments are settled by the SPE.

12. As mentioned in the beginning of this paragraph, two extra types of SPEs were added in the Netherlands. The first type is the operational lease companies. These are daughter companies of foreign parent companies that lease out fixed assets to foreign customers through operational lease contracts. These companies show clear SPE characteristics.

13. Also, special purpose vehicles (SPVs) with foreign originator were added to the Dutch decision tree on SPEs. These SPVs are intended to securitize large quantities of banks' assets. The choice to specifically add the SPV part to the SPE decision tree was made because SPVs with a foreign originator form a relatively large homogenous group, and, although in most cases a Dutch legal entity is the immediate parent, the foreign originator usually still has a lot of influence in the SPV.

14. Now that the different types of SPEs are made clear, conceptual questions on how SPEs could and/or should be treated in national accounts will be treated in the next paragraph.

III. TREATMENT OF SPECIAL PURPOSE ENTITIES IN NATIONAL ACCOUNTS

15. This section will discuss new guidelines in SNA2008, as well as some key features of guidelines in other international manuals. By doing this, various questions on the Group of Experts' research agenda will be dealt with.

A. Definition of Special Purpose Entities

16. As stated in the introductory section, at the time of the introduction of SPEs in the Dutch National Accounts (Dutch Benchmark Revision 2001) international guidelines provided hardly any details on how to deal with these types of institutions. SNA2008 does hold guidelines on the treatment of SPEs in the paragraph 'Special cases' in chapter 4 on institutional units and sectors. The question on the Group of Experts' research agenda on how SPEs can be defined is answered in SNA2008 as follows:

“A number of institutional units may be described as special purpose entities (SPEs) or special purpose vehicles. There is no common definition of an SPE but some of the following characteristics may apply.

Such units often have no employees and no non-financial assets. They may have little physical presence beyond a “brass plate” confirming their place of registration. They are always related to another corporation, often as a subsidiary, and SPEs in particular are often resident in a territory other than the territory of residence of related corporations. In the absence of any physical dimension to an enterprise, its residence is determined according to the economic territory under whose laws the enterprise is incorporated or registered.” (paragraphs 4.55 - 4.56)

17. Annex 7 of the new OECD Benchmark definition of Foreign Direct Investment also provides guidelines on how to detect SPEs. These criteria are:

- (a) The enterprise is a legal entity,;
 - (i) formally registered with a national authority; and
 - (ii) subject to fiscal and other legal obligations of the economy in which it is resident.
- (b) The enterprise is ultimately controlled by a non-resident parent, direct or indirectly.;

(c) The enterprise has no or few employees, little or no production in the host economy and little or no physical presence.;

(d) Almost all assets and liabilities of the enterprise represent investments in or from other countries.;

(e) The core business of the enterprise consists of group financing or holding activities, that is – viewed from the perspective of the compiler in a given country – the channeling of funds from non-residents to other non-residents. However, in its daily activities, managing and directing plays only a minor role.

18. As stated in SNA2008, no common definition is available. The SNA also states that SPEs often have no non-financial assets. This, however, is not the case in the second group of SPEs in the previous section: the royalty and license companies, because these hold or manage intellectual property rights.

19. In the Netherlands, a decision tree was introduced on how to define SPEs (see annex II). In this tree distinction is made between the different SPE types. As such, the Dutch definition of SPEs is the outcome of the criteria that are set up and shows many similarities to the international guidelines, described above. In this section the different criteria are stated, to which a company has to comply in order to be recorded as an SPE. First of all, only resident entities, which are (in)directly controlled by foreign entities can obtain the SPE status. Therefore the first two criteria are:

(a) The institutional unit is a resident entity,;

(b) The institutional unit is (directly or indirectly) foreign-controlled for more than 50 percent.

20. When an entity complies with the first two criteria, it is ‘benchmarked’ against the criteria of the five different SPEs presented in section 2. For each group a different criterion can be used:

(a) For the financing and holding companies: do more than 90 percent of total assets (excluding trade credits) and more than 90 percent of liabilities relate to non-resident entities?

(b) For the royalty and license companies: do more than 90 percent of total returns consist of export of royalty and license fees?

(c) For factoring companies: do more than 90 percent of returns and costs consist of factoring from and to non-residents?

(d) For operational lease companies: is more than 90 percent of turnover reached cross-border and does more than 90 percent of liabilities relate to non residents?

(e) For the SPV with foreign originator (that are controlled by a resident foundation) the foreign control criterion mentioned above (criterion 2) does not have to be met, because in most

cases there is no direct or indirect foreign control. The criterion, if an SPV with foreign originator is identified, to qualify as SPE is almost the same as that of the financing and holding companies: do more than 90 percent of the assets and more than 90 percent of liabilities relate to non-resident entities?

21. If these criteria or questions can be answered positively, one could speak of an SPE. One last escape is introduced in the tree, to ensure no production unit is present within an SPE. If an entity's domestic turnover (of in the Netherlands produced services, no re-exports) exceeds 25 million or more, it is generally not classified as an SPE: Domestic turnover of the institutional unit does not exceed 25 million euro.

B. The residence issue

22. Although briefly covered in the previous part of this section, the residence criterion proves to be very important. With regard to the definition of residence, SNA2008 is in line with the 6th Balance of Payments manual. It reads: "An institutional unit is said to be resident within the economic territory of a country when it maintains a centre of predominant economic interest in that territory, that is, when it engages, or intends to engage, in economic activities or transactions on a significant scale either indefinitely or over a long period of time." (SNA 2008, paragraph 1.48)

23. In the case of SPEs the question of residency is not straightforward: what criteria can be used to determine the residency of the relevant unit? This residence question is a logical first question with regard to SPEs, because if the conclusion is drawn that a company under investigation is not a resident of a country, it of course should not be recorded as such in that country.

24. Finding a satisfactory answer to this question of residency proves to be rather difficult. Because of increasing globalisation, it is becoming increasingly difficult to determine whether an entity is resident or not. Nonetheless the question is very important, especially when looking at the large financial flows involved with the dealings of SPEs. Overlap between two countries needs to be prevented; otherwise data on it will either be counted double or not at all. This can frustrate international comparability as well as the compilation of supranational accounts.

25. Before the introduction of SPEs in Dutch national accounts at the time of the 2001 Benchmark revision the residence criterion formed an important reason to exclude SPEs from the national accounts. Three excerpts of SNA stated:

"The concept of residence used here is not based on nationality or legal criteria [...]. An institutional unit is [...] said to be a resident unit when it has a centre of economic interest in the economic territory of the country in question." (SNA2008, paragraph 1.48)

"An institutional unit has a centre of predominant economic interest in an economic territory when there exists, within the economic territory, some location, dwelling, place of production, or other premises on which or from which the unit engages and intends to continue engaging, either indefinitely or over a finite but long period of time, in economic activities and transactions on a significant scale." (SNA2008, paragraph 4.14)

“Corporations and quasi-corporations are said to have a centre of economic interest and to be resident units of a country (economic territory) when they are engaged in a significant amount of production of goods and services there, or own land or buildings located there. They must maintain at least one production establishment there which they plan to operate indefinitely or over a long period of time.” (SNA1993, paragraph14.22)

26. One would think, especially after reading the last excerpt, SPEs should not be regarded as institutional units. Some SPEs only exist as a postal box or brass plate at a trust office. However, when looking more closely to some of the passages, Statistics Netherlands found enough reasons to actually see the SPEs as resident in the country:

(a) The criteria for a ‘production establishment’ are not clear in SNA: “The establishment combines both the kind-of-activity dimension and the locality dimension. An establishment is an enterprise, or part of an enterprise, that is situated in a single location and in which only a single productive activity is carried out or in which the principal productive activity accounts for most of the value added.” (paragraph 5.14). So no limits in the size of the location exist, nor are there requirements for having people on the payroll.;

(b) It can be stated that SPEs have production. SPEs produce services by intermediating financial flows en by issuing licenses and such. Their production is apparent in the export of services and the costs made in the Netherlands.

27. Based on these argumentations it was decided SPEs can be Dutch institutional units, because they meet the narrow residence demands in SNA. Also, from a practical point of view, it is useful to regard SPEs as Dutch residents. This interpretation by Statistics Netherlands during its Revision of 2001, shows great similarities to the way SNA2008 deals with this issue. The strict condition that a production establishment must be maintained is let loose and now, paragraph 4.56 in SNA2008 reads: “In the absence of any physical dimension to an enterprise, its residence is determined according to the economic territory under whose laws the enterprise is incorporated or registered.”

28. The SPE project group in the Netherlands applied a rather practical criterion on residence in which a resident SPE should be an institutional entity registered at a Dutch Chamber of Commerce and conduct fiscal activities in the Netherlands. The Chamber of Commerce records all corporations with economic activity in the Netherlands and these entities should be described in Dutch national accounts. By adding the fiscal aspect it is assured a company will only be measured in one country, assuming an entity will normally be liable to tax in only one country (or at least pay taxes for a certain transaction in just one country).

C. Production by special purpose entities

29. SNA2008 states that (in most cases) SPEs have only one form of production:

“Entities of this type are commonly managed by employees of another corporation which may or may not be a related one. The unit pays fees for services rendered to it and in turn

changes its parent or other related corporation a fee to cover the costs. This is the only production the unit is involved in though it will often incur liabilities on behalf of its owner and will usually receive investment income and holding gains on the assets it holds.” (art. 4.57)

30. However, in the Netherlands two other types of production are defined. One is income from hiring services, the second more important one, is production of royalties and license fees. As described in the second section, one SPE category is formed by the licensing and royalty companies. These hold or manage intellectual property rights (non-financial assets) and collect income in the form of royalty and license fees. Data on the import and export of royalties and licenses is available from the Balance of Payments survey in the Netherlands and can therefore be used to define this type of production.

D. Looking through SPEs

31. The decision tree, described in annex II and section IIIa, can be used without any problems for the “uncomplicated” cases. However, a foreign company might set up more than one company in the Netherlands. It can build a whole cluster of companies, with a domestic mother being major shareholder in its domestic subsidiaries. This might lead to incorrect definition of SPEs.

32. To come to a correct definition of individual companies within clusters like this, DNB and CBS decided that, when a company cluster is found in the Netherlands, the definition of each individual subsidiary will start at the bottom of the cluster, with the entities that do not have domestic daughter companies themselves. After this, the holding companies directly above these entities are examined and so on until the ultimate mother in the Netherlands can be examined in the tree. There will not be any problems if all entities within the cluster can be defined the same. However, if some entities in the cluster have clear SPE characteristics and others do not, a problem can occur when defining the status of the mother in the Netherlands.

33. The decision tree has proved to work well, especially for the ‘simple’ cases. It was set up to cover most of the possible SPE companies. For some complicated cases, even when applying the above approach, the tree does not suffice and in those cases it is up to the project group to make a well thought through decision on the status of company in question.

34. So basically, problems occur if a(n) (ultimately) foreign controlled domestic entity has subsidiaries in the same country. For cases where no inland subsidiaries exist, the (simple) decision tree can be used without any difficulties. When looking at a company with multiple subsidiaries in the same country, all assets might appear to stay in the Netherlands. But what really happens is that funds are channeled abroad through its SPE daughter(s). To qualify such an entity as a regular production unit would be unfair and wrong. As mentioned earlier, international guidelines suggest looking through these types of entities. Box A will focus on the way foreign direct investment with regard to SPEs can be recorded.

Box A: SPEs and Foreign Direct Investment

From a slightly different perspective, the analysis of foreign direct investment figures can also be complicated by SPEs. The 4th OECD Benchmark Definition on foreign direct investment (FDI), in accordance with BPM, sixth edition, gives guidelines on how to deal with and report different foreign direct investment (FDI) flows. In the case of SPEs, correct FDI reporting becomes more difficult, because of the pass-through character of the SPEs. It states that because of the residence of these companies in a given country, FDI from and to that country should be recorded in FDI statistics of that specific country. However segregation between FDI statistics on SPEs and non-SPEs is wanted in FDI presentations, because SPEs are often only used for channeling of funds *via* the country. Otherwise the presentation of FDI will be distorted by the SPE figures.

To create a more “economically significant” picture of the geographical breakdown of FDI, SPEs form a major problem. Looking through SPEs until a non-SPE is reached involves a great deal of work: in theory a multinational enterprise can create tens or even more than one hundred SPEs in different countries and by channeling funds through all these SPEs before the funds actually reach their non-SPE counterpart, FDI statistics compilers have to look through all these SPEs in all those countries, if a correct allocation of this FDI is to be reported. In practice most companies will not have funds channeled through so many SPEs and the creation of origin and destination matrices¹ is a step towards a more correct allocation of FDI and a better view of the dealings of SPEs.

However, when looking through all SPEs until a non-SPE entity is reached (ultimate destination) one actually would deny the very existence of the SPEs, because they will not be reported in statistical accounts. DNB and CBS compose respectively Balance of Payments and Rest of the World-accounts including and excluding SPEs. In the accounts including the SPEs, the direct linkages between the Netherlands and the first non-resident counterpart company are used. Although it might be interesting and useful to know and register the ultimate destination of the transactions flowing through the SPEs, composing statistics on this seem more suitable for satellite accounts. In the core statistics direct flows should be reported, where a subdivision in statistics including and excluding SPEs is desirable to be able to compose comparable and useful data.

IV. THE RECORDING OF TRANSACTIONS AND ACCOMPANYING ISSUES

35. In the previous section methods that are used in the Netherlands for detecting and registering SPEs were discussed. This section will touch upon another question posted on the research agenda. It will look at how relevant transactions by SPEs are compiled and recorded in

¹ The OECD Benchmark Definition states it is desirable that compilers provide supplemental information on the specific linkages between the inward and outward positions of its SPEs. By creating Origin and Destination Matrices a country can show what the SPE positions with different countries are, thus creating more transparency with regard to the geographical breakdown of SPE financial flows.

the Netherlands. In addition, the main strengths and weaknesses of the sources and methods are discussed.

A. Compilation of special purpose entities in national accounts

36. The question on the research agenda relevant to this section reads: ‘How should the relevant transactions be recorded: as service, capital formation, income or financial transaction?’ Statistics Netherlands tries to record SPE activities as detailed as possible. With the data that is available it compiles a complete set of national accounts data, from production account to other non-financial transactions, including interest, dividends, reinvested earnings and capital formation, concluding with the (large) financial transactions in the financial account. Although the available data is currently quite limited (there are, for example, no data on transactions with resident entities) Statistics Netherlands is capable, using several assumptions, to compile the complete data set.

37. The Central Bank (DNB) is the institution responsible for the collection of survey data on SPEs. DNB is also responsible for the compilation of the Balance of Payments (including and excluding SPEs). New Dutch SPEs are obliged to report themselves to DNB. The largest SPEs have to report monthly on their financial and non-financial transactions with non-residents. Once a year they also have to report balance sheet figures. Because only the larger SPEs are questioned on such a regular basis, the reporting SPEs are grossed up to make up for the non-reporting (smaller) SPEs. Biannually benchmarking takes place to make sure no SPEs are missed and the grossing up is of the right size.

B. Assumptions and vulnerabilities in the methods used

38. In compiling a complete set of national accounts data, several assumptions have to be made to come to a complete data set. This section will touch on some of these assumptions, in which vulnerabilities may lie. In annex III, a more detailed account is given on the composition of SPE figures in Dutch national accounts.

39. One of the assumptions made relates to the domestic output of royalties and license fees. The output value of royalty and license fees is determined as the domestic revenues from royalty and licenses and the exports of these services. These are royalty and license fees “produced” by the Dutch SPE itself, so not “re-exported fees”. To estimate the latter, it is assumed that all imported fees are directly exported to a mother company. Output by the SPE then consists of domestic sales plus total exports adjusted for “re-exports”. Any fluctuation in exports will normally also be reflected in fluctuations in imports. The assumption is made that incidental fluctuations in the gap between imports and exports are the result of acquisitions (or disposals) of royalties or (sub) licenses. When the gap between imports and export shows a sharp rise during one period, the assumption is made that this is caused by an acquisition of non-financial assets. These amounts will be recorded as (negative) gross capital formation. Whether this method is (still) appropriate is currently under investigation. Mostly it is a technical intervention to limit fluctuation in royalty and license production and thus value added by SPEs.

40. Another illustration of vulnerability is formed by estimations of domestic transactions. With regard to the costs of SPEs, Balance of Payments information on the imports of SPEs is

available. However, there is no data on the domestic costs (among which compensation of employees) made by SPEs. The same problem occurs in the primary income account and to a lesser extent in the financial account. No actual data on domestic transactions is available. Although presumably much smaller than transactions with foreign counterpart sectors, the lack of these data makes the estimation and interpretation of the economic behaviour of the SPEs in the resident country much more difficult.

41. Balance of Payments information on financial accounts is available, although not as detailed as for non-SPE corporations. Here also, virtually no data on domestic transactions exist. Only data on balance sheets, distinguished between resident and non-resident counterpart sectors, is available (but not in time for the first provisional annual estimate, six months after the end of the reporting year). The latter data give an indication on how domestic financial transactions have developed. For the rest CBS estimates domestic transactions, mostly by extrapolating domestic figures using the development in foreign transactions.

42. To get a better idea of how big transactions with domestic counterparts are, the SPE Project group in the Netherlands has started on a route towards an enlarged questionnaire for SPEs. In this questionnaire SPEs are asked to fill out a complete profit and loss account including domestic as well as foreign transactions. It is expected to be introduced in the questionnaire as of December 2009.

43. Another problem the project group in the Netherlands faced, was related to the delineation of the SPE population. SPEs only have to report to DNB. Non-financial corporations have to report to CBS and therefore it is very important the relevant populations of both institutions are aligned with each other. Last year CBS and DNB came together to compare their registers and where they found discrepancies, companies were studied more closely to come to an agreement on the status of the entity. The SPE decision tree, dealt with in the previous paragraph, proved to be very useful. Now, the populations of DNB and CBS are made consistent. This way, no companies are missed in questionnaires or counted double in different sectors.

V. CONCLUDING REMARKS

44. This paper shows how SPEs can be treated in a nation's National Accounts. It describes different types of SPEs identified in the Netherlands and shows how SPEs are treated statistically in the Netherlands. The Netherlands is host to many SPEs. For that reason Statistics Netherlands, in close cooperation with the statistical department of the Dutch Central Bank, has been monitoring the development of this sector closely for the last decade. As SPEs proved to have a significant impact on the Dutch cross-border transactions, they were included in Dutch economy during the Benchmark Revision of Dutch national accounts in 2001.

45. Because clear guidelines in international manuals were absent, criteria on the definition and treatment of SPEs had to be devised. To do this a project group was set up. In creating the new SPE criteria the project group was confronted with most of the issues currently addressed on the GROUP OF EXPERTS research agenda. An SPE decision tree was created by which the status of a company (non-SPE or SPE) could be tested adequately. Since its introduction the

Dutch SPE decision tree, although undergoing small changes when deemed necessary, has proved to work very well in the detection of SPEs.

46. Recent new international manuals pay more attention to SPEs. Guidelines on how to detect and define them are presented and show great similarities to the Dutch SPE approach. In different countries the definition of SPEs might still be slightly different, because the impact of SPEs is not as large. Because of the strong presence of SPEs in the Netherlands, the Dutch Central Bank (DNB) and Statistics Netherlands agreed to report statistics both including and excluding SPEs (Balance of Payments, Rest of World-account). It is strongly recommended to compose statistics, both including and excluding SPEs, because otherwise SPEs can inflate a nation's National Accounts and Balance of Payments drastically.

47. Because of limitations in the available source information, strong, and sometimes very strong, assumptions have to be made in the compilation of the relevant national accounts data. Domestic transactions are not yet covered in the questionnaires filled out by Dutch SPEs and assumptions on domestic flows have to be made. Progress is made however, to enhance the SPE questionnaire in future by asking, among others, more details about domestic transactions.

VI. QUESTIONS AND ISSUES

48. With regard to this paper and the treatment of Special Purpose Entities, Statistics Netherlands would like to pose the following questions to the other members of the Group of Experts:

- (a) Do members have suggestions for improvement of the methodology on the treatment of SPEs?
- (b) Can the described Dutch decision tree on SPEs also be used in other countries for the detection of SPEs?
- (c) How do members deal with the problems of limited data availability on SPEs?
- (d) Next to the described five types of SPEs, do members have indications for other types of SPEs in their countries?

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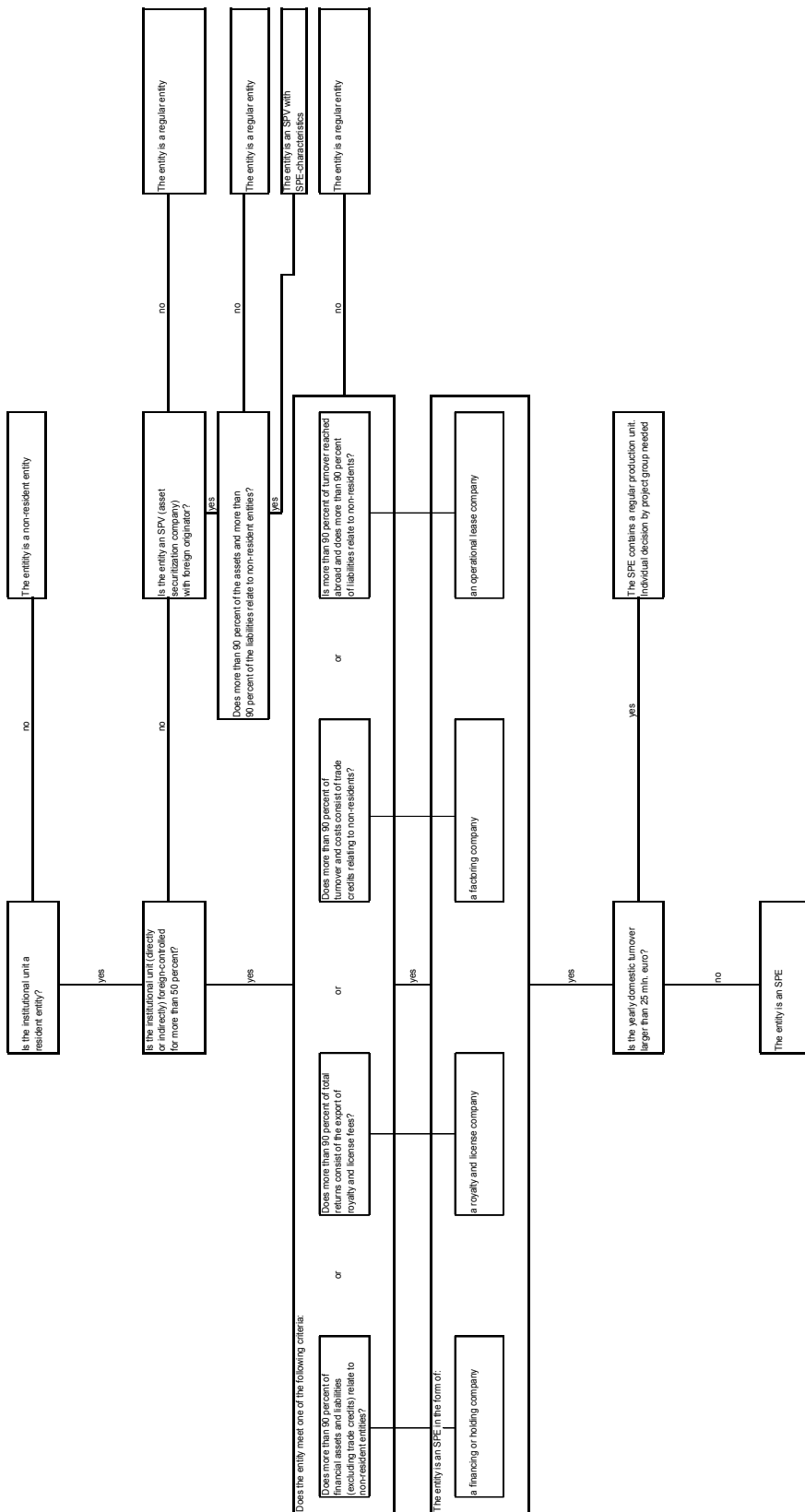
Annex I

Transactions of Special Purpose Entities in the Netherlands								
	2001	2002	2003	2004	2005	2006*	2007*	
	<i>mln euro</i>							
1. PRODUCTION ACCOUNT								
R	Output (basic prices)	4 804	4 659	4 451	5 320	6 138	5 902	6 403
U	Intermediate consumption (excl. deductible VAT)	6 514	5 856	5 758	6 074	6 974	6 766	6 602
	Value added (gross)	- 1 710	- 1 197	- 1 307	- 754	- 836	- 864	- 199
2.1 INCOME ACCOUNT (GENERATION OF INCOME)								
R	Value added (gross)	- 1 710	- 1 197	- 1 307	- 754	- 836	- 864	- 199
U	Compensation of employees	311	344	315	343	372	363	390
	Wages and salaries	252	269	244	262	287	284	307
	Employers' social contributions	59	75	71	81	85	79	83
	Consumption of fixed capital	987	933	939	930	888	885	852
	Operating surplus (net)	- 3 008	- 2 474	- 2 561	- 2 027	- 2 096	- 2 112	- 1 441
2.2 INCOME ACCOUNT (PRIMARY DISTRIBUTION)								
R	Operating surplus (net)	- 3 008	- 2 474	- 2 561	- 2 027	- 2 096	- 2 112	- 1 441
	Property income	81 362	52 840	45 256	60 768	65 717	69 556	62 610
	Interest	19 645	20 634	18 171	19 520	17 133	19 203	24 548
	Dividends	33 044	22 617	28 179	32 823	41 025	57 900	71 711
	Reinvested earnings on direct foreign investment	28 673	9 589	- 1 094	8 425	7 559	- 7 547	- 33 649
U	Property income	78 054	50 209	42 663	58 532	63 192	66 579	59 675
	Interest	18 335	20 557	18 887	19 671	17 264	21 568	25 858
	Dividends	17 698	9 682	20 275	21 043	54 041	26 252	46 439
	Reinvested earnings on direct foreign investment	42 021	19 970	3 501	17 818	- 8 113	18 759	- 12 622
	Primary income (net)	300	157	32	209	429	865	1 494
2.3 INCOME ACCOUNT (SECONDARY DISTRIBUTION)								
R	Primary income (net)	300	157	32	209	429	865	1 494
	Social contributions	2	2	2	2	2	2	2
U	Current taxes on income and wealth	1 287	1 090	971	1 139	1 317	1 750	2 346
	Social benefits (in cash)	2	2	2	2	2	2	2
	Disposable income (net)	- 987	- 933	- 939	- 930	- 888	- 885	- 852
2.4 INCOME ACCOUNT (USE OF INCOME)								
R	Disposable income (net)	- 987	- 933	- 939	- 930	- 888	- 885	- 852
U	Net saving and capital transfers	- 987	- 933	- 939	- 930	- 888	- 885	- 852
3.1 CAPITAL ACCOUNT (CAPITAL TRANSFERS)								
R	Saving (net)	- 987	- 933	- 939	- 930	- 888	- 885	- 852
U	Net saving and capital transfers	- 987	- 933	- 939	- 930	- 888	- 885	- 852
3.2 CAPITAL ACCOUNT (CAPITAL ACCUMULATION)								
R	Net saving and capital transfers	- 987	- 933	- 939	- 930	- 888	- 885	- 852
	Consumption of fixed capital	987	933	939	930	888	885	852
U	Capital formation (gross)	-	700	785	545	624	1 152	- 726
	Net lending/net borrowing	-	- 700	- 785	- 545	- 624	- 1 152	726

Annex I (continued)								
Transactions of Special Purpose Entities in the Netherlands								
	2001	2002	2003	2004	2005	2006*	2007*	
4. FINANCIAL BALANCE SHEET								
4.1 OPENING BALANCE SHEET								
A	Other deposits	18 476	21 735	21 198	25 535	27 448	32 622	32 509
	Long term bonds	28 834	27 539	25 320	24 322	25 136	28 053	21 230
	Short term loans	200 293	193 916	189 178	180 379	148 445	146 048	177 869
	Long term loans	223 095	243 864	237 087	259 772	272 659	285 083	290 279
	Shares and other equities	433 183	529 899	522 960	570 620	600 348	689 956	777 348
	Other accounts receivable and payable	18 046	26 405	28 165	23 843	22 725	21 226	23 276
	Total assets	921 927	1 043 358	1 023 908	1 084 471	1 096 761	1 202 988	1 322 511
L	Long term bonds	288 014	300 614	311 601	310 567	302 776	297 943	320 170
	Short term loans	79 650	101 209	99 343	107 433	96 089	116 491	127 784
	Long term loans	103 303	115 400	110 888	132 075	151 334	186 729	162 984
	Shares and other equities	457 005	526 157	499 226	523 515	498 440	568 729	673 716
	Other accounts receivable and payable	15 641	18 398	24 578	19 188	16 924	15 918	20 625
	Total liabilities	943 613	1 061 778	1 045 636	1 092 778	1 065 563	1 185 810	1 305 279
	Total net worth	- 21 686	- 18 420	- 21 728	- 8 307	31 198	17 178	17 232
4.2 FINANCIAL ACCOUNT								
A	Other deposits	5 994	- 419	4 283	1 115	4 389	604	24 063
	Long term bonds	5 625	19	55	1 511	2 223	- 5 771	6 578
	Short term loans	9 655	13 882	- 3 622	- 28 716	- 6 816	34 114	7 185
	Long term loans	36 785	14 719	27 650	15 594	8 913	14 627	220 241
	Shares and other equities	132 299	2 539	59 930	14 433	35 881	99 495	41 610
	Other accounts receivable and payable	6 687	1 408	- 4 068	- 1 086	- 1 649	1 353	- 209
	Change in assets	197 045	32 148	84 228	2 851	42 941	144 422	299 468
L	Long term bonds	32 297	20 132	25 428	- 5 611	- 10 511	23 696	32 180
	Short term loans	27 542	12 155	9 232	- 11 848	18 060	15 374	63 959
	Long term loans	18 737	5 438	24 609	23 452	30 932	- 18 433	145 501
	Shares and other equities	116 263	- 9 525	31 431	- 589	6 168	120 333	60 831
	Other accounts receivable and payable	2 206	4 648	- 5 687	- 2 008	- 1 084	4 604	- 3 729
	Change in liabilities	197 045	32 848	85 013	3 396	43 565	145 574	298 742
	Changes in financial net worth	-	- 700	- 785	- 545	- 624	- 1 152	726
	Net lending/net borrowing	-	- 700	- 785	- 545	- 624	- 1 152	726
	Statistical discrepancy	-	-	-	-	-	-	-
4.3 OTHER CHANGES								
A	Other deposits	- 2 735	- 118	54	798	785	- 717	- 779
	Long term bonds	- 6 920	- 2 238	- 1 053	- 697	694	- 1 052	- 22
	Short term loans	- 16 032	- 18 620	- 5 177	- 3 218	4 419	- 2 293	- 678
	Long term loans	- 16 016	- 21 496	- 4 965	- 2 707	3 511	- 9 431	- 6 686
	Shares and other equities	- 35 583	- 9 478	- 12 270	15 295	53 727	- 12 103	- 25 564
	Other accounts receivable and payable	1 672	352	- 254	- 32	150	697	536
	Total assets other changes	- 75 614	- 51 598	- 23 665	9 439	63 286	- 24 899	- 33 193
L	Long term bonds	- 19 697	- 9 145	- 26 462	- 2 180	5 678	- 1 469	- 9 546
	Short term loans	- 5 983	- 14 021	- 1 142	504	2 342	- 4 081	- 283
	Long term loans	- 6 640	- 9 950	- 3 422	- 4 193	4 463	- 5 312	- 7 397
	Shares and other equities	- 47 111	- 17 406	- 7 142	- 24 486	64 121	- 15 346	21 057
	Other accounts receivable and payable	551	1 532	297	- 256	78	103	1 035
	Total liabilities other changes	- 78 880	- 48 990	- 37 871	- 30 611	76 682	- 26 105	4 866
	Total other changes in net worth	3 266	- 2 608	14 206	40 050	- 13 396	1 206	- 38 059
4.4 CLOSING BALANCE SHEET								
A	Other deposits	21 735	21 198	25 535	27 448	32 622	32 509	55 793
	Long term bonds	27 539	25 320	24 322	25 136	28 053	21 230	27 786
	Short term loans	193 916	189 178	180 379	148 445	146 048	177 869	184 376
	Long term loans	243 864	237 087	259 772	272 659	285 083	290 279	503 834
	Shares and other equities	529 899	522 960	570 620	600 348	689 956	777 348	793 394
	Other accounts receivable and payable	26 405	28 165	23 843	22 725	21 226	23 276	23 603
	Total assets	1 043 358	1 023 908	1 084 471	1 096 761	1 202 988	1 322 511	1 588 786
L	Long term bonds	300 614	311 601	310 567	302 776	297 943	320 170	342 804
	Short term loans	101 209	99 343	107 433	96 089	116 491	127 784	191 460
	Long term loans	115 400	110 888	132 075	151 334	186 729	162 984	301 088
	Shares and other equities	526 157	499 226	523 515	498 440	568 729	673 716	755 604
	Other accounts receivable and payable	18 398	24 578	19 188	16 924	15 918	20 625	17 931
	Total liabilities	1 061 778	1 045 636	1 092 778	1 065 563	1 185 810	1 305 279	1 608 887
	Total net worth	- 18 420	- 21 728	- 8 307	31 198	17 178	17 232	- 20 101

Annex II

DECISION TREE ON SPEs



[ENGLISH ONLY]

Annex III**EXCERPT FROM PAPER BY ZWIJNENBURG, RECORDING OF SPECIAL PURPOSE ENTITIES IN THE DUTCH NATIONAL ACCOUNTS, 2006****ESTIMATION OF SPE-TRANSACTIONS IN NA****A. SPEs in the production account**

1. As explained in section IV, there is not much information on domestic transactions of SPEs. For the production account only data from BoP on trade in goods and services of SPEs are available. There is no information on domestic production or intermediate consumption of SPEs. The estimation of these variables is further complicated by the fact that most SPEs provide financial services to the company group for which no clear commission is paid. This implies that the production value for this type of SPEs should be compiled indirectly.

2. SPEs are engaged in two types of production. The SPEs that hold non-financial assets provide services on the basis of their royalties and licences. The SPEs that act as a financial vehicle or holding company on behalf of their foreign parent company provide financial services.

3. The production value of royalty and licence fees is determined as the domestic revenues from royalty and licences and the exports of these services for the account of the SPEs. Not all exports are regarded as production of the SPE, because part of the export originates from imports. For this type of flows, the SPE is merely a link in the transit of royalty and licence fees on behalf of their parent company. The parent company provides services on the basis of royalties and licences to the SPE, whereas the SPE (on the basis of sublicenses) passes these services on to the ultimate customers/users. This part of the imports and exports is regarded as re-exports in the

4. Dutch National Accounts². These re-exports do not form part of the production or intermediate consumption of SPEs. In addition, part of the imports and exports consist of domestic production and domestic sales. The domestic sales are compiled on the basis of the gap between the exports and imports of services. This gap can be seen as an indicator for the services

² In the following table the figures for re-exports of SPEs are presented for the years 2001 to 2005 (in mln euro).

	2001	2002	2003	2004	2005
Re-export of royalties and licence fees	4,901	4,624	4,418	4,485	3,615

that are provided by the SPE itself (and that do not originate from the imports of services). Therefore, it can be used to estimate the domestic production of the SPEs.

5. Under the assumption that domestic sales will develop in line with the imports and exports, the gap between imports and exports cannot show too much fluctuation; for the part of the transit trade, the gap between imports and exports (this is the part of services provided by the SPE that is not transferred to the parent company in the form of imports of royalty and licence fees, but is paid out to the parent company in the form of dividends) will be quite stable over time. Any fluctuation in exports will normally also be reflected in fluctuations in imports. Therefore, the assumption was made that incidental fluctuations in the gap between imports and exports are the result of acquisitions (or disposals) of royalties or (sub)licences. When the gap between imports and exports showed a sharp rise during one period, the assumption was made that this was caused by an acquisition of non-financial assets. Instead of recording these amounts as imports or exports of services, these amounts will be recorded as gross capital formation.

6. The calculation of the production value of the financial services provided by the SPE is somewhat more difficult. According to ESA95 (article 3.63) the production value of financial intermediaries should be measured as total property income received minus total interest paid, excluding the value of any income received from the investment of their own funds. However, because of the introduction of a new method for the compilation of FISIM, the measurement of production of financial services has changed. This is not applicable to SPEs though. Because international discussions came to the conclusion that FISIM should not be applied to investment funds and financial holdings, in the Dutch National Accounts SPEs were also excluded from FISIM. Because they only provide services to the worldwide company, they are comparable to holding companies. They are not market producers of these services and therefore FISIM is not applicable to SPEs. Because they are not market producers, it is difficult to make an accurate estimate of the market value of their production. As is the case with other non-market producers, such as investment funds and holdings, it was decided to use the sum of cost approach.

7. A third production category is rent. From DNB data for 1985-1992, it appeared that SPEs gain revenues from hiring services. For the years following 1992 a growth rate per year was established for the estimation of the output of the hiring services.

8. In table 1 the calculation of output of SPEs is shown.

Table 1. Output of SPEs (mln euro)

	2001	2002	2003	2004	2005
Domestic production of royalties and licence fees	534	503	555	594	615
Income from hiring services	80	92	96	101	106
Export of royalties and licence fees	645	652	778	871	1,069
Export of financial services	3,545	3,412	3,022	3,559	4,547
Total production	4,804	4,659	4,451	5,125	6,337

9. With regard to the costs of SPEs, information is available from BoP on the imports of SPEs. In addition, estimates have to be made for domestic costs. Information on domestic costs is available from source data of DNB for the period 1989-1992. On the basis of this information it was calculated that domestic costs equal 46 percent of the average amount of imports and exports of 'other services' according to BoP. This percentage was confirmed by recent data of DNB on some type of costs (such as office and management costs) and was used in the calculation of domestic costs for all years.

10. Table 2 shows the calculation of intermediate consumption of SPEs.

Table 2. Intermediate consumption of SPEs (mln euro)

	2001	2002	2003	2004	2005
Domestic intermediate consumption	446	414	442	664	1,164
Imports of financial services	5,236	4,650	4,093	4,374	5,674
Imports of other services	832	792	1,223	1,031	703
Total intermediate consumption	6,514	5,856	5,758	6,069	7,541

B. SPEs in the primary income account

11. Most of the data on the primary income account is derived from the information from BoP. Because SPEs have large cross-border assets and because they are foreign-controlled, in the primary income account there are large cross-border property income flows. Property income flows related to foreign direct investment in particular are substantial. These are interest income, dividends and reinvested earnings. Because data are lacking on domestic flows, estimations have to be made for domestic property income flows on the basis of domestic stock information.

12. In addition to property income flows, compensation of employees also has to be taken into account on the primary income account of SPEs. Because SPEs employ some staff (although for most SPEs this is very limited), estimates have to be made for the wages and social contributions paid by SPEs. Under the assumption that 9.000 SPEs have on average 0.75 employees (who earned 50,000 euro on average in 2002) the total compensation of employees in 2002 was an estimated 338 million euros. For the calculation of the time series an annual growth rate of 7 percent is used, based on the average growth rate of compensation of employees for the sectors S.11, S.12 and S.123/124 in the Dutch National Accounts in the same period.

13. In the estimation method for primary incomes of SPEs corrections were made to the item of reinvested earnings on direct foreign investment. Under the assumption that all SPEs are fully owned by non-resident parent companies, all earnings or losses from the SPE by definition have to be attributed to the RoW account. Part of the earnings or losses will be distributed to the parent company in the form of dividends, and the remaining part will be attributed to the parent company in the form of reinvested earnings. This implies that the reinvested earnings on the uses side is used as a residual.

14. The reinvested earnings on foreign direct investment on the uses side of the SPEs is calculated as follows. First, the profit/loss after taxes of the SPE has to be calculated. This is done by adding up all value added (+), compensation of employees (-/-), property income received (+), interest income paid (-/-) and taxes on income (-/-). Under the assumption that all profits/losses after taxes of the SPE are attributed to the foreign parent company (apart from a very small part of domestic dividend payments), this total profit/loss of the SPE should be equal to the sum of dividends declared (domestic and abroad) and reinvested earnings abroad. As the figure from BoP on dividends declared is assumed to be more robust than reinvested earnings, and as the estimate for domestic dividend payments is so small, the reinvested earnings paid are determined as a residual. In general, the calculation of reinvested earnings on the uses side of the primary income account of the SPE is measured as follows:

$$\begin{aligned}
 & \text{Reinvested earnings on direct foreign investment (use) =} \\
 & \text{Value-added} \\
 & \textit{minus} \quad \text{Compensation of employees} \\
 & \textit{plus} \quad \text{Balance of interest received and interest paid} \\
 & \textit{plus} \quad \text{Distributed income received} \\
 & \textit{plus} \quad \text{Reinvested earnings received} \\
 & \textit{minus} \quad \text{Taxes on income} \\
 & \textit{minus} \quad \text{Dividends declared (domestic and abroad)}
 \end{aligned}$$

15. Table 3 presents the results for the transactions on the primary income account derived from the information from BoP and the estimations made for domestic transactions.

Table 3. Primary income account for SPEs (mln euro)

	2001	2002	2003	2004	2005
<i>Resources</i>					
Interest	19,645	20,634	18,171	19,685	18,621
Distributed income of corporations	33,044	22,617	28,179	32,877	39,885
Reinvested earnings on direct foreign investment	28,673	9,589	-1,094	7,949	-1,726
<i>Uses</i>					
Compensation of employees	311	344	315	338	338
Interest	18,335	20,557	18,887	19,720	19,471
Distributed income of corporations	17,698	9,682	20,275	19,841	53,559
Reinvested earnings on direct foreign investment	42,021	19,970	3,501	18,526	-19,069

C. Other non-financial transactions of SPEs

16. In addition to the transactions already mentioned, SPEs engage in two other types of non-financial transactions, taxes on income and gross capital formation.

17. First of all SPEs, like all other corporations, pay taxes on the basis of their income. There are no data from SPEs on the payments of taxes for recent years. On the basis of information up till 1999 estimates have been made for the tax payments for the recent years.

18. Acquisitions less disposals of intangible fixed assets are the result of incidental gaps between imports and exports of royalties and licences. This has already been explained above (on the calculation of the transactions on the production account of SPEs).

19. Table 4 shows the estimates of taxes on income and on gross capital formation.

Table 4. Estimations of other non-financial transactions of SPEs (mln euro)

	2001	2002	2003	2004	2005
<i>Uses</i>					
Taxes on income	1,287	1,090	971	1,142	1,277
Gross capital formation	0	700	785	520	1,123

D. Net lending/net borrowing of SPEs

20. As all profits/losses of the SPE are attributed to the foreign parent company, the net lending/net borrowing of the SPE will, apart from its gross capital formation, equal zero. Under the assumption that all gross capital formation is financed by the foreign parent company via financial transactions (and is not covered by current receipts and expenditures), net lending/net borrowing equals gross capital formation. In table 5 the most important balancing items are presented for SPEs.

Table 5. Balancing items for SPEs (mln euro)

	2001	2002	2003	2004	2005
Value added (gross)	-1,710	-1,197	-1,307	-944	-1,204
Balance of primary incomes	2,997	2,287	2,278	2,086	2,481
Balance of other non-financial transactions	-1,287	-1,090	-971	-1,142	-1,277
Net lending/net borrowing	0	-700	-785	-520	-1,123

E. Financial accounts and balance sheets

21. For the financial accounts the main data source is also the BoP, which contains much data on cross-border transactions of SPEs. However, just as with the non-financial transactions, the information is not as extensive as on regular corporations. This implies that not all data from BoP can be directly linked to corresponding ESA95-transactions. For some items it was not quite clear which items they consisted of, while for others more information was needed to make a clear breakdown to account them to corresponding ESA95-items. For instance under the item inter-company loans, both short-term and long-term loans are recorded. For National Accounts

requirements this item has to be broken down into the two categories mentioned. The same goes for securities other than shares.

22. Table 7 shows the link between the source data from BoP and the corresponding ESA95-items.

Table 7. Linkage scheme between BoP-data on SPEs and ESA95-categories

Source description	ESA95-category
Deposits and bank balances	AF.2 Currency and deposits
Bank loans (liability)	AF.2 Currency and deposits
Bonds (notes and commercial paper)	AF.332 Long-term securities other than shares, excluding financial derivatives
Inter-company loans	AF.41 and AF.42 Short-term and long-term loans
Inter-company short term deposits	AF.41 Short-term loans
Other loans	AF.42 Long-term loans
Participations	AF.51 Shares and other equity, excluding mutual funds shares
Other	AF.7 Other accounts receivable/payable
Accounts payable/receivable – Banks	AF.2 Currency and deposits
Real estate	AF.51 Shares and other equity, excluding mutual funds shares
Reinvested earnings	AF.51 Shares and other equity, excluding mutual funds shares

23. The compilation of the financial accounts for SPEs the data from BoP and the international investment position are converted to ESA-categories in accordance with table 7. Then, the information on domestic positions is added and all items are linked a counterpart sector. Subsequently, the domestic participations and loans are partly consolidated., as some SPEs have participations in other domestic SPEs. Because these positions are reported by one as a liability and by the other as an asset, they have to be consolidated in compiling the sector results for the SPEs. Approximately 95 percent of the total domestic positions of SPEs are related to other domestic SPEs and are therefore corrected. Because it is known that a large part of the domestic loans are also inter-concern positions, these also have to be consolidated in the system of National Accounts. Taking into account the reported domestic positions of SPEs on the asset and liability side, it is determined that approximately 75 percent of the reported loans are inter-concern and should be consolidated.

24. Lastly, as only stock data are available on domestic positions of SPEs, the change in domestic positions has to be broken down into financial transactions and other changes. First, the other changes for the domestic items are estimated. This is done largely on the basis of the other changes with respect to cross-border positions. When these have been corrected for exchange rate changes, the other changes in domestic positions result. The transactions are then derived as a residual.

* * * * *