

INTER-SECRETARIAT WORKING GROUP ON NATIONAL ACCOUNTS

Minutes of the Expert Group Meeting
On the Treatment of Mobile Phone Licences in the National Accounts
Washington, 5 April 2001

I. INTRODUCTION

1. The Expert Group Meeting was called by the ISWGNA in response to the request of the United Nations Statistical Commission (UNSC) expressed at its last meeting in March 2001, “that the ISWGNA make decision as quickly as possible on the national accounting treatment of mobile phone licences”. The ISWGNA invited interested countries and experts to attend the meeting. This was the second meeting convened by the ISWGNA to discuss specifically mobile phone licences within less than a year. The previous special meeting of the ISWGNA was held on 23 June 2000 in Washington.
2. The meeting was attended by Mr. Rafaelo Malizia of ISTAT (Italy), Mr. G. Eding of the CBS (Netherlands), Mr. Robin Lynch of the ONS (United Kingdom) and Mr. Brent Moulton of the BEA (United States). Representatives of the secretariats which are members of the ISWGNA - Eurostat, IMF, OECD, UNSD, UN/ECA, UN/ECE and the WB also attended.

II. ORGANISATION OF THE MEETING

3. Mr. Adriaan Bloem of the IMF who is currently chairing the ISWGNA chaired the Expert Group meeting. The meeting had available for discussion the following papers: position paper from the ISWGNA, draft paper from the UK on Use of the Electro-Magnetic Spectrum – Treatment of Payments and the recent update of the IMF Working Paper on Treatment of Mobile Phone Licences in the National Accounts. Participants also had in front of them documents, in the form of comments, submitted by INE (Spain), Mr. Brent Moulton, BEA (United States), ABS (Australia), Ms. Anne Harrison (OECD), Statistics Canada, Mr. Robin Lynch, ONS (United Kingdom), INSEE (France) and the World Bank. The representatives of the CBS (Netherlands) and INSTAT (Italy) made oral presentations.

III. SUMMARY OF PRESENTATIONS AND SUBSEQUENT DISCUSSION

A. Position of the ISWGNA

4. Mr. Paul McCarthy presented the position of the ISWGNA on the national accounting treatment of mobile phone licences, which is described in the report of the special meeting of the ISWGNA held in June 2000 in Washington. It was noted that the outcome of the special meeting was that the licences should be treated as intangible non-produced assets in their own right. Two important conclusions in support of making the decision were that: (i) the spectrum itself is a tangible non-produced assets and the SNA does not have to be changed to handle this, and (ii) transferability is a sufficient condition, but not a necessary condition, for identifying something as an asset: transferability was specifically mentioned in 1993 SNA in the context of identifying a market price.

5. It was also pointed out that the difference between the Eurostat and the ISWGNA treatments was that Eurostat set a threshold of a minimum 5 years life before the licences would be treated as an asset while the ISWGNA had stayed with the SNA criterion of one year.

6. Participants were informed that the treatment of the mobile phone licences was also discussed at the OECD national accounts meeting held in September 2000 in Paris. A paper presented by the UK Office for National Statistics (ONS) made a case for payments for the UK licences to be treated as a rent. Possible implications for other parts of the accounts were also considered. Following that session at the OECD meeting, the ISWGNA met again briefly to consider the issues raised during this discussion. There was a general agreement that nothing new had been added to the debate since the special ISWGNA meeting held in June and that the decision made at that time did not need to be changed. However, at the request of the ONS, the ISWGNA agreed to set up an EDG on the OECD national accounts web site in order to continue the debate on the issue.

B. Treatment proposed by the UK ONS

7. Mr. Robin Lynch presented the position of the UK Office for National Statistics. The ONS came to the provisional conclusion, after consulting the 1993 SNA and the ESA 95, that the spectrum was a tangible non-produced asset similar to land, and the payments should be classified as pre-payments for rent. This conclusion differs from the alternative proposal developed in the international debate since the issue arose in the beginning of 2000 to treat the payments as purchasing a license and show the payments reflecting the sale of an asset by the government to the companies.

8. However, it was pointed out that there is some common ground in the two treatments: (i) the electro-magnetic spectrum is a tangible non-produced non-financial asset; (ii) the licence to use the spectrum is a separate asset, an intangible one; and (iii) up-front payments to use the spectrum can under some conditions be classified as pre-payment of rent.

9. The UK position to treat the initial payments for the use of the spectrum as rent was developed by drawing an analogy with land and its treatment as described in paragraphs 7.128 and 10.129 of the 1993 SNA. The attention of the participants was drawn to paragraph 7.128 which states that “ ...rent is recorded on an accrual basis, i.e. rent is treated as accruing continuously to the landowner

throughout the period of the contract agreed between the landowner and the tenant. The rent recorded for a particular accounting period is, therefore, equal to the value of the accumulated rent payable over that period in time, as distinct from the amount due to be paid, or actually paid.”. Paragraph 10.129 was also mentioned several times. It says that “ the owner of sub-soil assets, who is often a government unit, may grant a concession or lease to another institutional unit entitling the latter to extract the asset over a specified period of time in return for a series of payments (usually described as royalties). This arrangement is similar to a landowner conceding to a tenant the right to exploit the land in return for the payments of rent, except that the subsoil assets are exhaustible. The payments are property incomes and recorded as rent. The holder of the concession or lease may be entitled, or permitted by the owner, to sell the concession or lease to a third party. Such a sale is recorded as the sale of an intangible non-produced asset”.

10. Several difficult issues with regard to the treatment of payments for use of the spectrum were mentioned. These include: (i) the possibility to classify a payment as rent when it is a lump sum; (ii) the use of an auction to determine the value of the payments; (iii) the treatment of the payments in the company accounts (e.g. companies reflect the licence payments in their capital and profit and loss accounts); (iv) transferability (the UK logic does not depend on the criterion whether the licence is transferable or not); (v) length of lease (the UK case does not depend on the length of the licence period); and (vi) difficulty in imputing payments over time (an argument against the rent treatment has been the difficulty of imputing payments for a future period far distant from the original payments).

11. In conclusion, it was stressed that the position of the UK ONS is that payments for licences to use the spectrum should be classified as rent where the ownership and permanent effective control of the underlying asset remains with the original owner. This implies the value remains in the original asset, and payments reflect the use of the asset by a second party.

12. It was also noted that the IMF paper is a useful step in assisting a fuller understanding of the issue, but significant areas remain where there is certain disagreement. Therefore, it was suggested that the debate must continue until there is a clearer consensus.

C. IMF Working Paper

13. Mr. Nils Mahle (IMF) presented the IMF Working Paper on Treatment of Mobile Phone Licences in the National Accounts. A re-drafted version of the paper, which was first available in June 2000 was posted on the EDG web-site a few days before the Expert Group meeting. It was stressed that the document should be regarded as a research in progress and the views expressed are those of the authors and do not necessarily represent those of the IMF or IMF policy.

14. The aim of the paper was to determine the correct treatment of the mobile phone licence payments under the current 1993 SNA. However, the current text of the SNA does not have any specific guidance on these payments. Therefore, their treatment needed to be decided on general principles and by analogy with other cases. The paper also aims at clarifying the SNA text and providing some guidance, criteria and indicators for handling the border cases.

15. The first issue discussed in the paper is the nature of the licences. They are defined as giving exclusive rights to provide mobile phone services or otherwise use specified parts of the electromagnetic spectrum. They are allocated by an auction, issued for an up-front payment, pre-agreed instalments, a share of future revenue or for free. They may, or may not, be: cancellable by the government; transferable; given for a fixed period. As some of the licences have been auctioned for substantial sums, rules need to be developed on how to treat them in the national accounts.

16. The paper concludes that there are usually two assets involved with mobile phone licences, namely the spectrum, which is owned by the government, and the licence, which is an intangible non-produced asset sold by the government to the licence-holder. The values of the two assets are linked complementarily. The spectrum is a tangible non-produced asset owned by government. The sale of the licence is the sale of an asset. Alternative treatments of recording the licence payments as sale of the spectrum itself, other taxes on production, productions of a service, or rent were considered and rejected. Recording of payments depends on how the risks and benefits of ownership over the right to use the spectrum during the licence period are allocated. In this respect it was noted that in most cases the government has retained ownership of the spectrum and the term of the licence is finite (often 15-30 years).

17. The issue of treatment the licence over the remainder of its life was mentioned. The paper considers methods of amortization of the licence over its life. Under the 1993 SNA, the amortization is shown in the other changes in volume of assets account and does not affect income and saving. The paper considers the issues associated whether amortization should be taken into account in income and saving measures. However, it was noted that the issue of amortization is outside the discussion of the Expert Group meeting.

18. In conclusion it was pointed out that the treatment proposed by the IMF does not affect 1993 SNA, because treatment of the spectrum as a non-produced tangible asset is within the definitions of the SNA as is the treatment of the licence as a non-produced intangible asset. The treatment is an application of existing principles to a new situation. The principles are also applicable to other intangible assets such as broadcasting licences, fishing rights and others. The main effects in the accounts are that treating the licences as the sale of an asset affects only net lending and borrowing and only at the time of the contract being written, while treatment as rent affects disposable income, saving, and net lending and borrowing over the life span of the contract.

D. Comments on the IMF Working Paper

19. In the United States, licences to use the radio spectrum do not automatically revert to the government at the end of the licence period; the licences can be renewed with payment of only a small administrative fee. Therefore, when in 1994 the classification of radio spectrum licences was considered, the rent treatment was rejected because a time period is inherent in the definition of rent, whereas use of the spectrum in the US is essentially permanent. The BEA believes that it correctly treats the receipts from the US radio spectrum auctions as the sale of a non-produced asset. However, it was noted that if a radio spectrum licence is for a fixed, long period of time, as is the case of the UK auction, the appropriate treatment appears less clear.

20. Mr. Brian Newson (Eurostat) member of the ISWGNA presented the written comments submitted by ABS (Australia), Statistics Canada, (INSEE) France and (INE) Spain.

21. The Australian Bureau of Statistics (ABS) agrees with the conclusions of the IMF paper. The licences recently issued in Australia satisfy the SNA definition of intangible non-produced assets. They are issued for a 20 year period and are fully transferable. There is no restriction of their use. The ABS has also noted the conclusion in the IMF paper that payments received for some shorter-term, non-transferable uses of spectrum may be classified as rent. However, the ABS has no firm view on whether the boundary should be drawn at one year or at five year (as decided by Eurostat) licences.

22. The ABS is concerned about the alternative treatment of amortization/reappearance of assets as suggested in the IMF paper. In this respect, it would support a review of the 1993 SNA asset –liability boundary and treatment of rights and obligations conveyed by various contractual and licensing arrangements. However, it was stressed that a possible review should not dissuade the ISWGNA from determining the appropriate treatment of mobile phone licences based on the current content of the SNA.

23. Statistics Canada noted in the comments submitted to the Expert Group meeting, that IMF paper was quite thorough and had argued several alternatives. The first preference is for the rent treatment as it is quite easy to explain to the users in Canada. As a second best preference, Statistics Canada supports the IMF alternative treatment which incorporates amortization in the income account and changes all the sequence of accounts accordingly. Canada also supports the Eurostat proposal, mentioned in IMF paper, that five year criterion is used rather than one year to delineate sales of assets from rent. This is considered a good practical amendment.

24. In its comments, INSEE (France) supports the recording of mobile phone licences as the sale of an asset and not the rent treatment, which requires imputations of rent flows. However, it does not agree with recording the sale as a transaction of an intangible non-produced asset as proposed in the IMF paper. France would prefer to record it as the sale of the electromagnetic spectrum frequencies for the length of the contract. Participants were informed that a paper on this issue would be written soon. INSEE is interested in the questions raised in Annex 1 of the IMF paper about reviewing the 1993 SNA Asset-Liability Boundary. However, it opposes any immediate change in the SNA as the proposals outlined in Annex 1 need further elaboration.

25. As a general rule, INE (Spain) agrees with the conclusions in the IMF paper. It also agrees that two assets are involved with mobile phone licences, namely the spectrum which is a tangible non-produced asset and the licence which is an intangible non-produced asset. In Spain, because of current restrictions on the use of the electromagnetic spectrum, only a certain number of operators can exploit it. The licence is issued for 20 years term, which can be extended for another 10 years. The licence is cancellable and under specific conditions it can be transferred to another party. The payment is known when the licence is awarded and is made at the time the licence is issued.

26. Mr. Paul McCarthy (OECD) presented the written comments submitted by Ms. Anne Harrison (OECD). The comments covered the note submitted by Robin Lynch (UK) and the IMF paper.

27. With regard to the paper written by Robin Lynch it was noted that paragraph 7.128 of 1993 SNA had been interpreted larger than intended. It was noted that the main objective of this paragraph is that

if the rent is paid in one lump sum for a twelve month period, in principle it should be allocated on an accrual basis to the relevant twelve months. It was also noted that the paper does not enter sufficiently into the consequences of the pre-payment aspect of the UK proposal.

28. Concerning the IMF paper, the comments were directed at Section IV: Amortization of the value of the licences and reappearance of the value of the spectrum and the accompanying tables. In view of the author of the comments, the tables are incomplete because they do not show in the balance sheets the accounts receivable and payable, which are shown in the financial account under the rent option. Another comment concerns the flow accounts and whether they are fully worked through in the IMF examples. However, the IMF paper was commended for opening the possibility of treating the cost of using non-produced capital as a charge on income.

Comments by the representatives of Italy and the Netherlands

29. The representative of ISTAT informed the meeting that in Italy the spectrum is not considered an asset, as it does not exist in nature. In fact, the government gives the right to an operator to function in a certain field: the radio waves are produced by the operator. The licences are issued to allow the operator to install and manage a mobile telephone system in the country. In his view the 'permission' to use the field or the air represents the 'asset'. The air is not an economic asset as recognised by the 1993 SNA. The situation is similar to radio and TV broadcasting.

30. With regard to the licence it was suggested that to be treated as a 'sale' or 'purchase' of an intangible asset. It was also noted that the payment of taxes by the operator should be considered.

31. The representative of CBS (Netherlands) informed the meeting that Netherlands agrees with the conclusions of the IMF paper. He commended the paper as a very useful tool. In the Netherlands, the licence is treated as a sale of an asset.

32. After the various presentations, the Chairman of the meeting summarised the main points which were raised for discussion, namely:

- Nature of the spectrum: assets or not;
- What decides ownership: what criteria are used and how to deal with them?
- Parallels between contracts in using land and spectrum;
- Value of the spectrum or value of the contract;
- How does the length of time affects the issue of mobile phone licences?
- The impact on net worth of the society;
- Timing of the payment: does it matter whether the payment is made up-front or for more than a year?

33. In the ensuing discussion several participants pointed out that the spectrum is an asset. It was also noted that if there is not an underlying asset, then it is a payment of tax.

34. Cancellability was mentioned as one criterion for defining the ownership over the contract. It was noted that in the case of United Kingdom, the licence contract includes a clause that government can appropriate or cancel the contract in case of national emergency. However, it was pointed out that cancellability does not affect the ownership if the risks and benefits are shifted to the licence-holder. Another indicator that could be used is the length of the contract. The example of renting a piece of land for 90 years was mentioned. In this respect it was argued that the longer the contact, the easier it is to treat it as a transfer of ownership. In conclusion it was noted that there is a range of criteria which can be used to define ownership.

35. Parallels between contracts in using land and spectrum were discussed at some length. It was noted that many countries treat the land lease as an asset. There was a general agreement that there are clear parallels between the treatment of contracts in using land and spectrum. However, despite the similarities different countries treat them differently.

36. Participants also discussed the issue whether the value stays with the spectrum or with the contract. It was concluded that the actual situation is that the value of the licence is established at the time of its sale, for example by way of auction. The value of the licence declines over time.

37. The relevance of length of the licence was also discussed. Some participants felt that the criterion of one year, which is used in the position of the ISWGNA to delineate sales of assets from rent is too short. An example was given with sub-soil assets, which are used under long-term leases. Other participants noted that there is a big difference between the treatment of licences and sub-soil assets because the sub-soil assets are exhaustible. For example the petrol is extracted and sold out. The situation is not the same with the mobile phone licences .

38. As regards the impact on 'net worth' of the society, there was a general agreement that when the spectrum is recognised as an asset, this changes the 'net worth' of the society. The same is valid for land. It was noted that enterprises recognise the spectrum as an asset in their business accounts. It was also pointed out that establishing property rights on something has an impact on the 'net worth' of the society. In this respect it was mentioned that the issue is discussed in para. 7 and 9 of the ISWGNA report on the June 2000 meeting.

IV. SOME CONCLUSIONS AGREED ON AT THE MEETING

39. Concluding the discussion it was stressed that a number of very interesting presentations concerning the treatment of mobile phone licences in the national accounts were made. It was noted that the discussion did not lead to unanimous agreement although on several occasions some agreement had emerged.

40. It was pointed out that the meeting had gone beyond the previous discussions by treating issues, such as 'ownership', 'value' and 'length of contract.' It was also mentioned that the deliberations were more focused than in the previous meetings.

41. Most participants maintain the view that the spectrum is an asset itself. However, still the main issue of discussion was whether the licence should be treated as a sale or as a rent.

42. The meeting discussed a number of criteria to define the ownership. Participants agreed that a whole range of criteria has to be looked at.

43. Concerning the issue whether the value stays with the contract or with the asset no common agreement was achieved.

44. Participants agreed that it is necessary to look at the behaviour of the society when considering the length of contract. They also agreed that when the spectrum is classified as an asset this has an impact on the net worth of the society.

45. There was a general agreement that timing of the payment is not that important but rather the nature of the payment and to whom it refers.

46. Finally, it was stressed that the discussion brought important clarification on the issue of the treatment of mobile phone licences which will help the ISWGNA to decide about its report to the UN Statistical Commission. The number of agreements between various views has increased as compared to the meetings held in June and September 2000. It was also noted that the meeting in Washington

made valuable contributions to getting to a position on the treatment of mobile phone licences in national accounts.

