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**Working Party on National Accounts**

**PROGRESS REPORT**  
**Note by the UNECE Task Force on Global Production**

**To be held on 3-4 October 2013**  
**OECD Conference Centre**  
**Beginning at 9:00 a.m. on the first day**

*This document has been prepared by Michael Connolly (Statistical Office of Ireland) and will be presented under item 3*

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## **PROGRESS REPORT**

### **Note by the UNECE Task Force on Global Production**

#### **BACKGROUND**

1. The Bureau of the Conference of European Statisticians (CES) set up the UNECE Task Force (TF) on Global Production in November 2011 and in February 2012 endorsed a detailed work plan. According to the terms of reference, the objectives of the TF are twofold. The first goal is to develop guidance on the unresolved conceptual issues arising from System of National Accounts, 2008 (2008 SNA) and the 6<sup>th</sup> revision of the Balance of Payments Manual (BPM6) in relation to global production. The second goal is to develop further guidance on implementation aspects. In order to do so, the TF will study the existing practices of countries in relation to the different types of global production arrangements.

2. The final output of the TF, to be presented to the CES tentatively in April 2014, will be a guide to assist national accounts and balance of payments compilers with recording global production related activities in their accounts. At this point in time, the TF is finalizing its work. It has closed the discussion on most of the issues identified in the research agenda and developed draft recommendations. Almost all chapters of the guide have been redrafted to reflect the comments of the Expert Group on National Accounts. After a final review, the guide will be submitted for approval by the CES Bureau.

3. This paper will inform the OECD WPNA on the progress of work and discuss recent developments since the last TF report of October 2012. The paper will also provide an overview of the revised outline of the guide.

#### **MAIN FINDINGS OF THE TASK FORCE**

4. In 2013 the TF on Global Production had two face to face meetings: one on 21-22 January and one on 5 April. It discussed the main issues on the research agenda, the content of the individual chapters and agreed on a revised outline for the Guide on Global Production.

5. The main findings of the TF concerning the implementation of the 2008 SNA and BPM6 in respect to global production arrangements are listed below.

##### ***Providing a typology of global production arrangements***

6. The typology is advanced for those arrangements related to the manufacturing of goods. However, in recent years, global production seems to stretch out to the domain of services as well. The TF discussions on 'merchandising of services' indicate the need for further research in this area, based on the examination of new case studies. At this point in time, the evidence on the international 'arrangers of services' appeared to be too limited to develop further guidance.

***Reconsidering the industrial classification of the so-called ‘Factoryless Producers’ (FGP) and the nature of their output (goods instead of services)***

7. FGPs are producers that outsource the manufacturing transformation activities but own the underlying intellectual property products (IPPs) and control the outcome of the production process. A strict interpretation of the International Standard Industrial Classification of All Economic Activities (ISIC), Revision 4 is that an FGP should be classified as a distributor if the FGP does not provide (own) the material inputs subject to processing, even though the FGP provides the technical specifications of the output and owns and supplies other critical inputs.

8. The opinion of the TF is that ownership of material inputs should not be the sole determining factor in classifying an FGP. An FGP that controls the outcome of the production process and provides (owns) either the IPP inputs or other inputs (goods and services) to a contract processor should be classified to manufacturing as a separate and new subset of existing classifications that highlights the factoryless characteristic of the firm. This view would affect the interpretation and implementation of international recommendations.

9. The TF also explored the borderline between factoryless goods producers and traders, based on examining the significance of IPPs in the production activities of such firms.

***The concept of economic ownership is not always easy to apply in the context of global production...***

10. Breaking down the various production steps in a global production chain on a country-by-country basis may lead to the identification of activity units, which are in reality fully controlled by a foreign unit. This is particularly true for so-called special purpose entities (SPEs), which are incorporated in economies different from the parent. Applying the principles of economic ownership to such cases, in contrast to legal ownership, is not an easy task. Similar problems may exist when recording the activities of multiterritory, or similar kinds of enterprises. Recording their activities on a country-by-country basis requires prorating of asset ownership and output and imputing transactions. This hampers the recording of imports and exports strictly on transfer of ownership basis, as recommended in the SNA.

***...and determining economic ownership of IPPs inside global production is even more challenging***

11. The TF developed a decision tree that may assist national accounts compilers in determining the economic owners of IPPs inside global production chains (of MNEs and other global producers), and help to identify IPP related transactions such as transactions in IPP originals and IPP related capital services (e.g. licenses, royalties). One key objective of the decision tree is properly allocating IPP use inside global production chains.

***The TF identified the data items needed to record import and export of goods on an ownership transfer basis and explored the related measurement challenges***

12. The TF paid special attention to the changes in the international standards (2008 SNA, BPM6) with regard to the recording of goods sent abroad for processing and merchanting. In addition, the issue of quasi-transit trade was also examined.

***Globalization demands for new directions in which national accounts and balance of payments statistics are compiled***

13. Data collection becomes increasingly challenging as the result of ongoing globalization. Certain aspects of global production are difficult to measure, or may even remain unobserved. The additional data needs could easily lead to substantial expansion of data collection frameworks. In many countries, this is infeasible due to ongoing pressures to reduce costs and respondent burdens. This means that modes of data collection and compilation must be explored.

14. In this context, the TF collected the experiences of so-called 'large and complex cases units' recently set up by several national statistical institutes. These units appear to be successful in collecting and compiling data on the largest and most complex multinational enterprises in a consistent way. Other approaches are the exchange of international trade data between statistical institutes, as an attempt to avoid asymmetries in trade statistics, and the development of common business registers for multinationals, which may assist in assigning their activities on a country-by-country basis and recording their international transactions in a mutual consistent way.

**CONSULTATIONS AND INTERNATIONAL COORDINATION**

15. The main issues identified by the TF in respect to global production arrangements, that would impact the implementation of the 2008 SNA were consulted with relevant international meetings and working groups. Coordination with other task forces working on related topics was also ensured.

***CES Bureau***

16. In February 2013, the Task Force presented a report to the CES Bureau. The Bureau supported the work of the TF and highlighted its importance in the context of the SNA 2008 implementation. The Bureau expressed concern with a possible delay of the work. It highlighted the importance of practically oriented guidelines. Due to the complexity of the global production phenomenon, the TF should pay particular attention to drafting practical guidelines that will be easy to implement.

17. The Bureau asked the TF to carry out early consultations with the Intersecretariat Working Group on National Accounts (ISWGNA) and the Advisory Expert Group (AEG) on National Accounts regarding the issues that may require further clarification in the 2008 SNA, BPM6 and other international standards or recommendations (e.g., how to report and measure the output of factoryless production). The Bureau also noted that treatment of intellectual property products is a core issue in various economic statistics. Guidelines in this area will greatly benefit the quality of statistics.

***Group of Experts on National Accounts***

18. The twelfth meeting of the Group of Experts on National Accounts on 3-4 April 2013 discussed the draft chapters prepared by the TF. The TF sent the drafts for country consultation in advance of the meeting.

19. The meeting recommended to call the TF report a guide in order to highlight the fact that the aim of the publication is to provide practically oriented compilation guidance on the implementation of the 2008 SNA and BPM6 in relation to global production arrangements. The proposals' relationship to international standards should be more explicit. It should be clear if the TF recommendations fall within the frame of existing standards or if they raise issues for future revisions. It could also be indicated more clearly if the TF came to a firm conclusion on a given issue, or if further research is needed.

20. The meeting supported the TF proposal to treat FGPs as being genuinely engaged in production or manufacturing.

21. Issues related to economic ownership also provoked discussion. The meeting asked the TF to strengthen the practical advice and guidance on how to interpret the SNA ownership concepts by using concrete cases, particularly for recording of the SPEs in the accounts. Proposals for supplementary data sets could be explored.

22. The meeting recommended restructuring the chapters to better connect the key concepts to the key challenges of measuring global production. As a logical consequence, discussions related to FGP or to VAT registrations will be centralized in one place in the guide. The measurement challenges with recording imports and exports of goods on transfer of ownership basis and the issues with recording production abroad will be brought together and presented in one chapter.

23. The meeting also provided more specific comments on each chapter, which are very useful for finalizing the guide. The TF was concerned by the lack of responses to the call for case studies. However, some new countries have recently agreed to contribute to the work.

#### ***AEG consultation on factoryless goods producers***

24. The TF brought the issue concerning the industrial classification of FGPs for discussion at the AEG meeting in May 2013. The proposal of the TF was supported by the AEG.

25. The following paragraphs present the outcome of the AEG meeting.

“The Advisory Expert Group on National Accounts:...

16. Agreed that factoryless producers — supplying intellectual property capital and marketing services, and controlling the production process while using contract manufacturers to produce goods — are to be considered goods producers and should not be classified in distributive services.

17. Recommended that factoryless producers producing manufacturing type of goods should be identified separately within manufacturing, but that this need not be taken to a greater level of detail within subclasses of manufacturing.

18. Supported the classification criteria proposed by the Global Production Task Force on defining the boundary between goods production and distribution services based on intellectual property products (IPP) inputs and other inputs of goods and services.”

#### ***Other international working groups***

26. The work of the TF relates to that of several other expert groups. It logically extends the work of the Joint UNECE/Eurostat/OECD working group on the Impact of Globalization on National Accounts. In addition, the TF on Global Production tried to coordinate closely with the Eurostat task force on Goods Sent Abroad for Processing. Chapter 5 benefits substantially from experiences of EU member countries collected in the course of the TF’s work.

27. Further, the AEG asked the TF on Global production to follow up on the work of the ECB/Eurostat/OECD task force report on Head Offices, Holding Companies and Special Purpose Entities and to put forward more concrete proposals on clarification of recognition of (economic) ownership and the subsequent recording of certain assets of SPEs.

28. The issue of the industrial classification of FGP was brought to the attention of Expert Group on International Statistical Classifications, which took place in May 2013.

## OUTLINE OF THE GUIDE ON GLOBAL PRODUCTION

29. Based on the feedback of the meeting of the Group of Experts on National Accounts and the decisions of the CES Bureau and the AEG, the TF on Global Production prepared a revised outline of the guide.

30. In the revised outline, the introduction, which explains the main goals and structure of the guide and discusses the main features of global production, will be followed by discussion on a typology of global production arrangements in *Chapter 2*. Initially this chapter discusses the various kinds of economic relationships that may exist between a principal (or leading) enterprise and other units participating in the global value chain, such as contract producers. Next, the chapter introduces the typology of global production arrangements and provides several numerical examples. This chapter also discusses factoryless production in detail.

31. The SNA principles of economic ownership are addressed in *Chapter 3*. The objective of this chapter is to discuss aspects of MNE activities related to ownership and to highlight trading arrangements that pose particular difficulties. The chapter will review statistical and business accounting standards as they relate to economic ownership in general.

32. *Chapter 4* extends the discussions on economic ownership to the ownership of IPPs and related transactions inside global production chains and MNEs. The methodological recommendations systematically address accounting for (a) production, (b) gross fixed capital formation, (c) transfers between countries and (d) use of IPPs in production. A wider range of IPP related transactions will be discussed, such as charges for use of IPPs, IPP related capital transfers and direct foreign investments. Drawing on existing experience, the chapter reviews data collection methods and approaches to overcome data gaps.

33. *Chapter 5* brings together the measurement challenges of a selected number of global production arrangements: goods sent abroad for processing, merchanting and factoryless production from the point of view of measuring production and international trade flows. Attention is given to the changing accounting conventions between the 1993 and 2008 versions of the SNA and differences between the BPM5 and BPM6, particularly with respect to their data requirements and analysis. This chapter benefits substantially from the work carried out by the Eurostat taskforce on ‘Goods sent abroad for processing’ and the related manual that was compiled as a follow up to the task force report. However, the chapter reflects the experiences from a broader range of countries, including Canada, China, EU member states, Israel, Ireland, Kyrgyzstan, Mexico and the United States.

34. In recent years, several NSIs established so called large and complex enterprises units (LCU), and their experiences with observing and measuring global production are presented in *Chapter 6*. The TF conducted a survey to get a better understanding of the organization of work and the type of analyses carried out by LCUs. This chapter focuses mainly on the findings of the survey. The chapter also touches briefly on issues other than globalization that cause data inconsistency, since these are part of the focus of the LCUs.

35. An area of economic analysis, closely related to global production, is the measurement of global value chains and the value added content of international trade. The Trade in value added (TiVA) initiative

is presented in *Chapter 7*. This chapter also discusses issues related to input-output implications and related modelling.

36. *Chapter 8* reviews the concepts and principles of multiterritory enterprises as presented in the 2008 SNA and BPM6. In addition, it discusses the difficulties and measurement problems related to applying methods and obtaining the required data sources. These challenges are exemplified by several case studies presented in the chapter.

37. The objective of *Chapter 9* is to advance the research on “merchanting/arranging of services”. It distinguishes merchanting/arranging of services and services subcontracting, by emphasizing the respective roles of the transactors: the role of the entity facilitating the service transaction (i.e., the arranger who is actually producing a margin service on a service transaction), and the roles of the provider and the consumer of the service, who are located outside the country of the arranger.

38. *Chapter 10* discusses statistical measurement issues associated with so-called “quasi-transit trade” and similar phenomena. Quasi-transit trade occurs when goods enter an economy and are declared as imports for customs purposes at values that differ from those declared when the goods leave the same economy, without the transit economy having acquired ownership of the goods. This phenomenon is most relevant in custom unions (CUs), such as the European Union (EU), where goods often enter the union without having changed ownership (so-called fiscal representatives may declare the goods in imports).

39. *Chapter 11* presents conclusions and recommendations for future work. It will describe a number of issues that were not addressed by the TF, due to time constraints, and formulate proposals for further research (e.g., price and volume measurement).

## **FINALIZATION OF THE GUIDE**

40. The TF expects to complete its work in early 2014. Following the discussion at the OECD WPNA, the TF will have a meeting on 4 October to review the latest versions of the chapters and agree on a timetable for their finalization.

41. The guide will be presented to the January 2014 meeting of the CES Bureau. If feedback is positive, the guide will be submitted for electronic consultation with the CES member countries in February, with anticipated endorsement by the CES in April 2014.

42. The delegates are welcome to express their comments on this report.