

**Eighteenth Meeting of the  
IMF Committee on Balance of Payments Statistics  
Washington, D.C., June 27–July 1, 2005**

**Land and Building Owned by Nonresidents**

**I. DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)**  
**II. OUTCOME PAPER (DITEG) # 15**

**April 8, 2005**

**1. Topic: Long-term leases on land and buildings**

**2. Issues: See DITEG Issue Paper # 15 Land and buildings owned by nonresidents on a long-term leasehold basis by IMF.**

- (i) DITEG noted that the present manual and the Benchmark Definition do not provide guidance on the treatment of long-term leaseholds of land (and buildings).
- (ii) The group noted that determining the appropriate classification for the purchase of a long-term lease on land (and buildings) by a nonresident is based in whether that lease is equivalent to an operational or financial lease, that is, whether effective ownership has been transferred or not. The group felt the term of the lease was a secondary consideration.
- (iii) The group noted that it is possible for ownership of an asset to be split between two parties where long-term leases are involved. The group also noted the similarity between long-term leases in land (and buildings) and licenses for (most) broad band spectra. The group noted that, for these latter, the treatment in the national accounts is for the lessee to acquire an asset (representing the present value of the future income derivable over the life of the lease), but that, while the underlying value of the asset remains unchanged (assuming no price changes) over time, the value to the lessee falls and the value for the lessor rises as the license moves towards maturity. In principle, DITEG thought the same would apply for long-term leases on land (and buildings).
- (iv) The group discussed two examples of transactions in a long-term lease on land (and buildings), one between a resident and a nonresident, and a second between two nonresidents. The group came to the conclusion that whatever the residence of the transactors, the lease could not be identified as "other capital" because the land (and buildings) would be deemed to be owned by the (notional) direct investment entity (resident in the economy where the land is located, in the same manner as an outright purchase of land by a nonresident) and that it is the nature of the nonresident's claim on that direct investment entity that is the relevant consideration. Most members of the group felt that that investment would represent equity, which would fall in value as the lease moved to maturity (assuming no price changes).
- (v) DITEG took note that the question of how to treat a long-term lease that requires an annual (or periodic) land lease payment is to be discussed by Canberra II in March 2005. The group was advised that the new SNA will discuss finance leasing in more detail and be less focused on the length of the lease.

**3. Recommendations:**

- (i) DITEG recognized the existence of long-term leases on land (and buildings) and recommended that they need clarifying in the new balance of payments manual and the revised Benchmark Definition.
- (ii) DITEG felt that where an effective change in ownership takes place through a lease on land (and buildings), in a manner comparable to a finance lease, a notional enterprise should be created, in the same way it is when land (and buildings) are acquired outright. DITEG also felt that the claim on the direct investment entity should be considered to be equity and that the value of the asset would fall as the lease moves to maturity (assuming no price changes).
- (iii) DITEG did not think that an arbitrary rule regarding the length of the lease (to determine whether the lease represented an effective change of ownership or not) should be adopted, noting that an (original) term of one year seemed too short.
- (iv) DITEG felt that it would be appropriate to wait until Canberra II has held its meeting in April 2005 before making a final recommendation.

**4. Rejected Alternatives:**

Treating land (and buildings) acquired under a long-term lease by households for noncommercial purposes as “other investment”.

**5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)**

- (i) *Do the Committee and the WIIS agree that long-term leases on land (and buildings) need to be clarified in the new balance of payments manual and the revised Benchmark Definition? See 3(i).*
- (ii) *Do the Committee and the WIIS agree, where an effective change in ownership takes place through a lease on land (and buildings), in a manner comparable to a finance lease, that a notional enterprise should be created, in the same way as an outright purchase of land (and buildings)?*
- (iii) *And if they agree to the creation of a notional direct investment entity Question 2, do the Committee and the WIIS agree that the claim on that direct investment entity should be considered to be equity? See 3(ii) above.*
- (iv) *And if they agree to the treatment of the claim on the notional direct investment entity as equity (as per Question 3), do the Committee and the WIIS agree that the value of the asset would fall as the lease moves to maturity (assuming no price changes)? See 3(ii) above.*
- (v) *Do the Committee and the WIIS agree that an arbitrary rule regarding the length of the lease (to determine whether the lease represented an effective change of ownership or not) should not be adopted? See 3(iii) above.*

*(vi) Do the Committee and the WIIS agree that it would be appropriate to wait until Canberra II has met (in April 2005) before making a final decision? See 3(iv) above.*

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**IMF COMMITTEE ON BALANCE OF PAYMENTS STATISTICS AND OECD  
WORKSHOP ON INTERNATIONAL INVESTMENT STATISTICS**

**DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)**

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**ISSUES PAPER (DITEG) #15**

**LAND AND BUILDINGS OWNED BY NONRESIDENTS  
ON A LONG-TERM LEASEHOLD BASIS**

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**November 2004**

## DIRECT INVESTMENT TECHNICAL EXPERT GROUP

### ISSUES PAPER (DITEG) #15: LAND AND BUILDINGS OWNED BY NONRESIDENTS ON A LONG-TERM LEASEHOLD BASIS

#### I. Current international standards for the statistical treatment of the issue

1. The fifth edition of the IMF *Balance of Payments Manual (BPM5)* states that in instances of ownership of land and buildings by a nonresident, “the owner is treated as if he has transferred his ownership to a notional institutional unit that is actually resident in the country. The notional unit is treated as being owned and controlled by the nonresident owners—much as a quasi-corporation is owned and controlled by its owner.” (paragraph 64). Although not specifically stated in the *BPM5*, the IMF *Balance of Payments Textbook (BOP Textbook)* indicates that “The relationship between the nonresident legal owner of the land and the notional entity is a direct investment relationship.” (Paragraph 550.) *BPM5* also makes it clear that “private, nonbusiness real estate investment (e.g. holiday and other residences owned by nonresidents for personal use...) is, in principle, included in direct investment.” (Paragraph 382.)

2. The third edition of the OECD *Benchmark Definition of Foreign Direct Investment (BD3)*, indicates that the direct investment data should cover “Land, structures (except those structures owned by foreign government entities), and immovable equipment and objects, in the host country, that are directly owned by a foreign resident. Holiday and second homes owned by nonresidents are therefore regarded as part of direct investment...” (Paragraph 10.)

3. Although neither the *BPM5* or *BD3* indicate the component of direct investment under which land and buildings are to be classified, the IMF *Balance of Payments Compilation Guide* specifies that purchases and sales of land and buildings by nonresidents are to be classified under the equity capital component of direct investment (Table 16.2, page 158), as does the *BOP Textbook* (paragraph 551).

#### II. Concerns/shortcomings of the current treatment

6. The fact that neither the *BPM5* or *BD3* specifically state that land and buildings purchased/owned by nonresidents on a long-term leasehold basis, as opposed to land and buildings purchased/owned outright on a free-hold basis, are to be included in the direct investment data has caused some confusion amongst compilers.

7. The manuals also do not address the issues of whether the data should cover only leases that are long-term, and if so, the precise definition of those “long-term” leases.

8. In response to these concerns the *Annotated Outline for the Revision of BPM5 (AO)* proposes that the treatment of land and buildings indicated in the present manuals will also be applied to long-term leases of immovable assets on the basis that long-term leases approximate ownership. The *AO* also asks for views on whether this proposed treatment is considered to be appropriate, and if so, whether the definition of “long-term” should be one year or whether it should be a longer period. (Paragraph 4.24.)

### **III. Possible alternative treatments**

9. There are three possible options:

(a) To expand the text in the manuals to make it clear that (i) purchases/ownership of land and buildings by nonresidents on a long-term leasehold basis are to be included in the direct investment data, (ii) the definition of long-term leases should be consistent with that used for other debt instruments, namely, “leases with a duration of one year or more”, and (iii) purchases/ownership of land and buildings by nonresidents on a long-term leasehold basis are to be classified under equity capital, together with land and buildings owned outright by nonresidents.

(b) To amend the current methodology to make a distinction between land and buildings owned outright by nonresidents and those owned on a leasehold basis, with the former being classified under the equity capital component of direct investment, and the latter being classified under the other capital component of direct investment, as is the present practice of a few countries.

(c) To amend the current methodology to make a distinction between land and buildings owned outright by nonresidents and those owned on a leasehold basis, with the former being classified under the equity capital component of direct investment, and the latter being excluded from the direct investment data, and instead classified under the Other Investment category in the balance of payments statistics, as is the present practice of several countries.

10. The preliminary results of the 2003 Survey of the Implementation of International Methodological Standards for Direct Investment (SIMSDI) indicate that a significant number of countries already apply the classification and definition proposed in 9(a) above. Of the 56 respondent countries<sup>1</sup> for which purchases of land and buildings on long-term leases are applicable:

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<sup>1</sup> At time of writing, the issue was not applicable for 52 countries, and the 2003 SIMSDI questionnaire responses for 5 OECD countries and 3 non-OECD countries had not been received.

(a) 21 countries<sup>2</sup> include the land and buildings purchased/owned by nonresidents on long-term leases in their direct investment data.

(b) All of the 21 countries classified these transactions/positions as equity capital, together with the data on outright purchases/ownership of land and buildings by nonresidents.

(c) Of the 14 countries that provided information on the definition of “long-term leases” used for their data, 2 countries made no distinction between land and buildings owned outright by nonresidents and those owned on a leasehold arrangement, and all but 2 of the remaining 12 countries used the standard definition for long-term debt, namely leases with a duration of one year or more.<sup>3</sup>

11. The 2003 SIMSDI questionnaire does not address the reasons why the remaining 35 countries do not include purchases/ownership of land and buildings by nonresidents on long-term leases in their direct investment data.

12. The comments on the questions raised in the *AO (Is the proposed treatment for long-term leases of land suitable? If so, what is the definition of “long-term”? Is it one year, as in other cases or something longer?)* also support the proposal in 9(a) above.

Total responses	12	
Yes	11	• 1 year (4); 3 years (1); 3-5 years (1); 30-50 years (1); long, at country’s discretion (1).
Other	1	• If yes, longer than 1 year.

#### IV. Points for discussion

1. *Do DITEG members consider that the revisions to BPM5 and BD3 should clarify that (i) land and buildings purchased/owned by nonresidents on a long-term leasehold basis are to be included in the direct investment data, (ii) the definition of long-term leases should be consistent with that used for other debt instruments, namely, “leases with a duration of one year or more”, and (iii) land and buildings purchased/owned by nonresidents on a long-term*

<sup>2</sup> These countries comprise 4 OECD countries, Mexico, Spain, the United Kingdom, and the United States), and 17 non-OECD countries, including Malaysia, Pakistan, Russia, Singapore, and Tunisia.

<sup>3</sup> Costa Rica defines long-term leases for the purchase of land and buildings by nonresidents as being those with a duration of 10 years or more, or leases that includes an option to buy. Pakistan defines long-term leases for the purchase of land and buildings by nonresidents as being 99 years.



*leasehold basis are to be classified under equity capital, together with land and buildings owned outright by nonresidents ? or*

*(b) Do DITEG members consider that the methodology should be amended to make a distinction between land and buildings owned outright by nonresidents and those owned on a long-term leasehold basis, with the former being classified under the equity capital component of direct investment, and the latter being classified under the other capital component of direct investment? or*

3 *Do DITEG members consider that the methodology should be amended to make a distinction between land and buildings owned outright by nonresidents and those owned on a long-term leasehold basis, with the former being classified under the equity capital component of direct investment, and the latter being excluded from the direct investment data, and instead classified under the Other Investment category of the balance of payments statistics?*

## **References**

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