IMF Committee on Balance of Payments Statistics

BPM6 Update

Direct Investment Task Team (DITT)

FOR PUBLIC CONSULTATION

D.17 Identifying Superdividends and Establishing the Borderline Between Dividends and Withdrawal of Equity in the context of Direct Investment

D.17 Identifying Superdividends and Establishing the Borderline Between Dividends and Withdrawal of Equity[1]

The superdividends concept to direct investment (DI)[2] *entails two major drawbacks: (i) difficulties in operationalization which may lead to international inconsistencies, and (ii) limited interpretability of the related reinvested earnings sub-item. In addition, the non-existence of the term in the* OECD Benchmark Definition of Foreign Direct Investment, fourth edition (BD4) *contrary to the* Balance of Payments and International Investment Position Manual, sixth edition (BPM6), *and the* System of National Accounts, 2008, *as well as* BD4*'s different treatment of distributed profits has revealed the need for a re-consideration of the concept for DI. This guidance note (GN) presents the shortcomings of the current methodological treatment, including the difficulties from a compiler's perspective and its analytical deficiencies. The GN proposes and discusses three different alternative treatments, weighing the pros and cons of each option, to the concept of super dividends, for consideration. The Direct Investment Task Team recommends revising the current* BPM6 *recommendations, with a majority support for the third alternative, which supports the treatment of any distributions of accumulated reserves from ordinary earnings as ordinary dividends. Under this alternative, only the earnings from non-operating activities (sales of fixed capital assets, liquidations of branches) would be treated as exceptional and recorded as withdrawals of equity.*

SECTION I: THE ISSUE

BACKGROUND

1. **The application of the superdividends concept to foreign direct investment (DI),[3] as based on the *System of National Accounts, 2008* (*2008 SNA*)/the *Balance of Payments Manual, sixth edition* (*BPM6*), entails two major drawbacks.** They are: (i) difficulties in operationalization likely leading to international inconsistencies and (ii) limited interpretability of the related reinvested earnings sub-item. In addition, the non-existence of the term in the *OECD Benchmark Definition of Foreign Direct Investment, fourth edition (BD4)* as well as *BD4*'s different treatment of distributed profits shows the need to re-open the discussion and to potentially re-consider the concept for DI.

2. **Regarding operationalization, both the *2008 SNA* and *BPM6*[4] point to identifying superdividends as disproportionately large to past levels.** The *2008 SNA* recommends comparing the ratio of dividends to distributable income over the recent past and assessing the plausibility that the current level of dividends declared is in line with past practice. If the level of dividends declared is greatly

[1] Prepared by Mirco Lattwein (Germany), Michael Abbondante in replacement for Paul Roberts, as from August 2020 (Australia Bureau of Statistics), Fernando Nieto (Bank of Spain), Ray Mataloni (U.S. Bureau of Economic Analysis), and Kenneth Egesa (IMF).

[2] In the following GN, DI is used interchangeably with FDI, that is always referring to cross border direct investment.

[3] In contrast to the *BPM6* and *BD4*, the *2008 SNA* does not address functional categories. As this is out of the Direct Investment Task Team (DITT) scope, this GN discusses the concept of superdividends, its implications and consequences for DI only.

[4] The current international standards for the treatment of super dividends in both the *2008 SNA* and *BPM6* are presented in Annex II.

in excess of this, the excess would be identified as superdividends. The *BPM6* recommends in paragraph 11.27 that superdividends are to be identified when payments are disproportionately large relative to the recent levels of dividends and earnings. If the level of dividends exceeds greatly previous dividends and trends in earnings, the excess should be excluded from dividends and shown as a withdrawal of equity. Given that it is difficult to make a meaningful comparison to recent patterns of dividends for many affiliates due to their unsteady payment behaviour, a significant share of dividends can be erroneously labelled as superdividends. In addition, the guidance does not address the issue of a new affiliate, which will not have a history of dividends to compare to. Overall, while both balance of payments and national accounts are consistent in describing superdividends and on the guidance of how to determine and record them, the implementation of the recommendation is difficult in DI and, thereby, likely leading to inconsistencies in countries' mirror data.

3. **Furthermore, both the *2008 SNA* (paragraph 7.130) and *BPM6* (paragraph 11.27) highlight that dividends are not recorded on a strict accrual basis.** This happens because corporations often smooth the payments of dividends, often paying out rather less than the operating surplus but sometimes paying out a little more, especially when the operating surplus itself is very low.

4. **This leads to the second major drawback of applying the superdividends concept to DI, a potential misinterpretation of components of DI equity income data.** DI equity income comprises not only dividends, but also reinvested earnings. All income is assumed to be distributed because of the direct investor's control over the economic decisions of the direct investment enterprise and, hence, also its income distribution policy. A conscious decision on part of the direct investor to reinvest/disinvest through dividend distributions should therefore be visible in the corresponding reinvestment of earnings item. The current concept of superdividends, however, disturbs the relationship between distributed earnings (dividends) and reinvestment of earnings. In recording distributions out of accumulated reserves as withdrawals of equity, as stated in the *BPM6,* paragraph 11.27, reinvested earnings as a result will be higher, and the corresponding time series falsely indicate that the respective economy is more attractive for expansions of existing DI investments than it really is.[5] Because the direct investors income includes not only the distributed earnings but also the reinvested earnings in that period, it is always recorded on an accrual basis. This differs from the income of other investors where their income only includes the distributed earnings, and, thus, is not on an accrual basis.

5. **Misinterpretation is even more likely, as the conceptual basis in *BD4* differs from the other current statistical manuals, thus further facilitating a divergent treatment and implementation among compilers** (see BOPCOM 18/13c).[6] First of all, the term and concept of "superdividends" is not mentioned at all in the *BD4*, suggesting that all ordinary earnings (past and present) are to be recorded as dividends, when distributed/paid. This is supported by the fact that the *BD4* distributed earnings definition is in contrast to those put forth by the *2008 SNA* and *BPM6* (see OECD 2018 (section 12) and *BD4* 219). These drawbacks are particularly severe as the original aim of the superdividends concept, to align earnings and dividends paid, is not applicable to regular DI equity income (which, as stated above, tends to be distributed unsteadily).

[5] A numerical example to illustrate the different approaches is provided in the Annex.

[6] https://www.imf.org/external/pubs/ft/bop/2018/pdf/18-13c.pdf.

Concerns/Shortcomings of the Current Treatment

6. **The fundamental assumption the *2008 SNA* bases its concept of superdividends on is that "[a]n enterprise […] usually aims to have a smooth track record of dividend payments**" (*2008 SNA*, paragraph 11.90). Empirical research conducted by the USA, Poland, Brazil, and Switzerland (see WGIIS Document WD (2017)17), however, indicates that this assumption is invalid for intrafirm dividends, at least for most direct investment enterprises. In contrast to dividends paid to shareholders by publicly traded companies, DI enterprises seem to follow rather irregular patterns of dividend payments to their direct investors with long periods without any dividend transaction. Hence, slavishly identifying superdividends based on their size relative to the company's payment history yields numerous positive results, thereby making superdividends the norm, although originally perceived as the exception. This unintended behavior leads to uncertainty among compilers, who in turn deviate from the international requirements to provide their users with a comprehensible picture.

7. **Moreover, although most compilers face the same problem, their respective solutions vary greatly, which leads to asymmetries in the portion of reinvested earnings (RIE) of the income and the financial account.** This is also related to the compiler's ability to compare current payments with past earnings and payments, which is often limited. Furthermore, it should be noted, that although the identification of superdividends has no impact on the net current and net financial accounts, the composition of the subitems (RIE and equity) as illustrated by the numerical example in the Annex does change considerably. Most notably a transaction identified as a superdividend (and therefore not displayed as a negative reinvested earning) will increase (or less decrease) the reinvested earnings aggregate, creating the impression of an economy eligible for reinvested earnings and the expansion of existing businesses. This appears paradoxical since what in fact took place was the repatriation of capital.

ISSUES FOR DISCUSSION

8. **In order to overcome the operational shortcomings and the analytical deficiencies outlined above, three alternatives have been identified for the treatment of superdividends paid between affiliated enterprises.**[7] The first alternative (A1) maintains methodologically the status quo and sketches the fixing of the operational shortcomings. The second alternative (A2) relies on the clarification of superdividends concept in *European macro statistical system of accounting (ESA 2010)*, treating any distribution out of accumulated reserves as a superdividend. The third alternative (A3) offers a solution to the operational issues as well as to the analytical deficiency by discarding the concept of superdividends for accumulated reserves from ordinary earnings altogether for direct investment enterprises. All three alternatives are described in the following section. A brief overview of the major pros and cons of each alternative is presented in a summary table in Annex III.

[7] The proposed alternative treatments are supposed to be applied for direct investment enterprises only. As such, the outcome of this GN does not affect unaffiliated enterprises and has therefore no impact on other functional categories in the balance of payments, such as portfolio investment or other investment, or the treatment of distributed income of domestic corporations. This unique treatment of the distributions of DI enterprises is justified by the unique way that DI income is recorded in the accounts.

I. Alternative 1 (A1)

9. **The operationalization of superdividends lacks empirical evidence and therefore needs to be replaced, as shown in section 3.** Sticking to the approach to capture the phenomenon of “exceptional payments” out of current operational income by quantitative means, a threshold or ratio other than “greatly in excess of previous dividends and trends in earnings” needs to be applied (e.g., a “dividend in relation to recent equity ratio” as proposed in the OECD 2018, section 43). The main advantage of A1 is maintaining the current view, that superdividends may have a twofold character, namely exceptional distribution out of accumulated reserves on the one hand and distribution of income due to sales of assets or other extraordinary events on the other hand. It only replaces the operationalization, or in other words, the quantitative indicator. Yet, some disadvantages remain: first, in setting up a different calculation method in order to better capture the phenomenon “superdividends”, any indicator is essentially arbitrary. Hence, with a change in income distribution policy, the new recommendation may be outdated again. In addition, any new measure will also fall short of clearly allocating distributions out of accumulated reserves as either regular dividends or exceptional payments. Second, national compilers would still be obliged to analyze investment and distribution patterns on a micro-level, partially exceeding their capacities in terms of staff, IT infrastructure and data availability/quality.

II. Alternative 2 (A2)

10. ***ESA 2010*** **states that “distributions […] in excess of their operational profit excluding holding gains/losses” are “recorded as financial transactions as withdrawal of equity akin to a partial liquidation of the enterprise” and therefore part of instrument F.5 (Equity and investment fund shares) but not income.**[8] Following this rationale, distributions from accumulated reserves are not seen as dividends, but withdrawal of equity—or in other words, only dividends from the current period are recorded as income, and both irrespective of the size of the distribution. In doing so, A2 is superior to A1 and the status quo, as it leads to the desired result more accurately than any arbitrary indicator ever could.

III. Alternative 3 (A3)

11. **So far, the empirical evidence shows that for DI an irregular distribution policy within the firm is rather the rule than the exception.** Thus, in order to avoid misclassification of regular dividends as exceptional payments or superdividends, one should reconsider and acknowledge distributions of accumulated reserves—and as such earnings from previous periods—in any case as ordinary dividends and therefore to be recorded under primary income. Hence, exceptional payments recorded as withdrawal of equity in the financial account would only consist of sales of assets as defined in the *BPM6 Compilation Guide* (*BPM6 CG*) paragraph 13.78 (1). The advantages of A3 are straightforward: first, treating distributions out of accumulated reserves as ordinary dividends leads more often to negative reinvested earnings, capturing correctly the divestment character of these operations. Otherwise, if always—as practiced by some countries to date—accounted as withdrawal of equity, the resulting

[8] *ESA 2010* 20.122 (e), S. 435.

positive reinvested earnings may lead to the assumption, that the respective countries are a destination of investment, not divestment.

12. **The new approach would thus help to avoid a misinterpretation of components of balance of payments income data.** Second, the alignment under A3 removes the varying degree of comprehensive treatment of distributions out of accumulated reserves between the *BPM6* and *BD4* [9] (which in the *BPM6* are seen as exceptional and therefore withdrawal of equity, in *BD4* seen as ordinary and therefore as dividend).[10] Third, the new differentiation removes the contradiction between the *BPM6* paragraph 11.27 and the *BPM6* paragraph 11.46/*BD4* 537 regarding the impact of dividends on reinvested earnings.[11]

13. **The term "superdividends" is no longer necessary to flag remaining operations.** In fact, in reducing exceptional payments to distributions of earnings from sales of assets (present and past), and therefore eliminating the operationalization with regard to the characteristic "greatly in excess of previous dividends and trends in earnings", the term "superdividends" itself, that is somehow tied to this operationalization, is no longer needed to highlight the remaining operations. This could be seen as an additional advantage, for superdividends as the empirical evidence shows neither are "super" in terms of extraordinariness and size, nor are they supposed to be treated as dividends.

14. In conclusion, following A3, distributions are either exceptional (*BPM6 CG* paragraph 13.78(1)) and thus treated as withdrawal of equity or regular and therefore treated as dividend.

15. **This treatment would possibly lead to two inconsistencies with the current SNA-methodology for income.** First, redefining (narrowing) the conceptual scope for recordings distributions as withdrawal of equity and the corresponding abolishment of the term "superdividends" for DI enterprises. Second, recording distributions from (ordinary) accumulated reserves as dividends implies a macro-statistical double recording of these transactions (as reinvested earnings when earned and as dividends when paid). Though only affecting income sub-items as DI income is always equal to current period earnings plus net interest payments, this may not be in accordance with SNA principles on income. Yet, the national accounts income key data would remain unaffected as the treatment following A3 leads only to shifts in the DI income sub-aggregates (the higher dividends would decrease the reinvested earnings in that period by the same amount, leaving total income unaffected).

[9] "Distributed earnings can be paid out of current or past earnings and may result in negative reinvested earnings if the distribution of dividends exceeds total earnings in a particular reference period." *BD4* 219.

[10] Provided, the accumulated reserves do not include non-operational earnings. Otherwise, distributions out of accumulated reserves coming from non-operational earnings need to be separated from operational earnings.

[11] The *BPM6,* paragraph 11.46 states that "Reinvested earnings can be negative when a direct investment enterprise has a loss on its operations or the dividends declared in a period are larger than net income in that period.", Additionally, in line with the *BPM6,* paragraph 11.46, *BD4* 537 states "[…] However, if a DIE generates a loss from its current operations (that is, the sum of its operating surplus and its net property income is negative), or if it declares a dividend for more than it has earned in the reference period, a negative debit should be recorded in the Direct Investment Income Account under reinvested earnings (RE) for the DIE […]". Yet, in contrast, the *BPM6,* paragraph 11.27 states that "[e]xceptional payments by corporations (including quasi corporations such as branches) to their shareholders that are made out of accumulated reserves or sales of assets should not be treated as dividends." In doing so, dividends could never exceed the net income and therefore never lead to negative reinvested earnings. So, the *BPM6* paragraphs 11.27 and 11.46 are contradictory.

SECTION II: OUTCOMES

16. **The DITT agrees with the recommendation to revise the *BPM6* regarding the treatment of distributions out of accumulated reserves.**[12] To overcome the drawbacks of the current treatment discussed in Section I, the majority of DITT members supports the proposed alternative A3 which recommends to regard distributions of accumulated reserves from ordinary earnings[13] in any case as ordinary dividend and therefore to record them in the primary income.[14] One member, although supporting A3, stressed the need to develop compilation guidance in the manuals for identifying the exceptional payments from sales of assets as the practical difficulties in identifying such distributions could lead to asymmetries in treatment across countries. Given the difficulties of developing guidance for reporters to identify exceptional payments, this DITT member preferred that the application of exceptional payments be limited to DI compilers who would apply it conservatively.

17. **The recommendation is further to regard earnings from non-operating activities (sales of fixed capital assets, liquidations of branches) as exceptional and the corresponding distribution as a withdrawal of equity, which in turn are not to be recorded under primary income but in the financial account.** The term "superdividends" should not be used for the distribution of those exceptional earnings in order to avoid the current misleading interpretation as the term "dividend" should be used only for operations recorded under primary income. This recommendation follows alternative A3. As stated above, as the national accounts remain unaffected, the resulting inconsistencies—if they are regarded as such—between SNA and BPM in following A3 seem to be negligible.

18. **Some DITT members indicated they would find it analytically useful to introduce as supplementary information, an *of which* position of withdrawal of equity, to distinguish between withdrawal of assets and exceptional distributions from the proceeds resulting from the sales of assets.** However, it was stressed that this supplementary information could be subject to confidentiality restrictions. Some members also recommended that the Balance of Payments Task Team (BPTT) explore the need to reconsider the treatment of superdividends for the other functional categories. There was also a request that clearer guidance or definitions to identify the exceptional nature of the distributed earnings would be useful.

19. **The BPTT overall agrees with the recommendation to revise the *BPM6* regarding the treatment of distributions out of accumulated reserves.[15]** A large majority supported Alternative 3, yet some members expressed concerns, that the proposed alternative might be contradictory to principles in national accounting (as addressed in para. 15 and Annex III). Therefore, it was proposed to submit the GN to Financial and Payments Task Team (FITT) and the Intersecretariat Working Group on National

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[12] Comments were received from Brazil, Canada, France, Japan, Luxembourg, Poland, Russia, South Africa, Zambia, the European Central Bank, the IMF and OECD.

[13] Ordinary earnings as defined by the current operating performance concept (COPC, see OECD (2008), para. 208), which is the fundamental basis for DI income within both—Balance of Payments and National Accounts.

[14] One DITT member, while supporting A.3, indicated that the concept of superdividends as defined in the first two alternatives would remain valid for captive financial corporations specifically (S127). The special case of superdividends in the context of captive financial institutions would be addressed within the GN D.3: "*Treatment of Collective Investment Institutions*".

[15] Comments were received from Brazil, Canada, China, ECB, Eurostat, Germany, IMF, Netherlands, UN, United States, and Zambia.

Accounts' Advisory Expert Group (AEG) in order to obtain a holistic view towards a commonly agreed proposal for public consultation. Regarding inserting an additional "of which"-position in the financial account, a majority of BPTT members did not agree due to lack of analytical value or expressed concerns that the analytical value gained might not set off the increased response burden and confidentiality issues due to higher granularity. As regards the term "superdividends", there was disagreement within BPTT whether to maintain or replace it. One member proposed to label the respective phenomenon as "distributions of the proceeds from sales of assets," referring to 13.78 (1) of the *BPM6 CG* (as quoted in Annex II).

FITT and AEG consultation

20. **There was overall support from the FITT, as well to revise the *BPM6* with regard to the treatment of distributions out of accumulated reserves.**[16] As in DITT and BPTT, a majority expressed support for A3, one member was in favor of A2 given the substantial changes resulting from the implementation of A3. The additional "of which"-position as well as the replacement of the term "superdividends" were overall rejected. A majority saw no analytical value regarding the "of which"-position given the expected confidentiality constraints and had no strong view to change the term "superdividends" as no appropriate alternative could be offered so far. Additionally, one member stressed, that the semantic harmonization of the term "superdividends" and treatment recommended between the relevant manuals would be beneficial.

21. **Feedback from AEG indicates objections to A3 due to alleged deviations in the treatment of DI income from the status quo.**[17] Furthermore, an additional "of which"-position was not favored, as respondents emphasized that confidentiality constraints would lead to little analytical use. Finally, AEG respondents stressed that the term "superdividend" should remain as it is considered the correct label.

22. **Concerns were also expressed that A3 might distort the National Accounts income claiming that this recommended approach deviates from the current dividends concept, which is not necessarily valid.** Thus, this specific issue needs further clarification. It is true, that following A3, the dividends concept would receive an adjustment for DI dividends and therefore would deviate conceptually from the understanding of, for example, portfolio dividends. However, it is also true that the re-formulation of DI dividends would not affect DI total income (numerically and conceptually). Why? In contrast to portfolio investment, DI income consists not only of dividends and interest, but also of reinvested earnings.[18] These are to be seen as a complementary measure to dividend payments within DI equity income and are understood (and most often calculated) as a residual of total DI equity income minus dividends.[19] The conceptual basis for the compilation of DI equity income, on the other hand, remains unchanged. Thus, if—under A3—dividends increase, reinvested earnings decrease (ceteris paribus). The rationale behind this is that in contrast to portfolio investment (PI), in DI, by convention all earnings that the direct investor has a claim on are considered distributed in the current period and then recorded as the portion distributed and the portion reinvested (the latter also being recorded as increase of equity

[16] Comments were received from Armenia, Bank of International Settlement, United Kingdom, and South Africa.

[17] Comments were received from Costa Rica, Ireland, Netherlands, United Kingdom and the ECB.

[18] This asymmetric treatment is addressed in GN F.2.

[19] See OECD (2008), paragraph 199.

in the financial account) depending on the decision of the direct investor. Therefore, even under A3, the DI equity income definition remains unchanged and, therefore, consistent with the National Accounts income concept. All A3 does is establish, or redefine, the borderline between the sub-aggregates of dividends and reinvested earnings, as the table in Annex V illustrates. In other words: since there is no proposal to change how the total DI income is measured, the consistency with the National Accounts will be retained, even if DI dividends will not be measured in the same way as other dividends.

REJECTED ALTERNATIVES

23. **Alternative A1** was rejected on the basis that it represents the status quo since it only changes the definition of the quantitative indicator, thereby remaining an arbitrary solution difficult to apply. **Alternative A2** was rejected given that it still contradicts the internal logic of DI income for it does not show negative reinvested earnings if accumulated reserves are dissolved and distributed. Following A2 in recording distributions of accumulated reserves as withdrawal of equity, negative reinvested earnings could only occur in case of losses in the current period. Hence the resulting reinvested earnings time series would offer no information on the extent to which, over time, an entity's earning have been reinvested in the economy or not. One member pointed out that A2 and A3 could be considered as possible alternative treatments, with A2 being easier to implement relative to A3, should the treatment of superdividends be reconsidered for other functional categories.

Questions to the Committee:

1. *Taking into consideration the strengths and weaknesses of each proposed alternative, do you support alternative A3?*
2. *Taking into consideration potential confidentiality constraints, do you consider an additional "of which"-position of withdrawal of equity to distinguish exceptional distributions from sales of assets in the financial account necessary in order to gain more analytical power?*
3. *Given the misleading implication that superdividends might be part of the income as they are labeled dividends, but treated as withdrawal of equity, do you think there are needs to replace "superdividends" for DI or can the manuals alternatively simply refer to the treatment of distributions of the proceeds from the sales of assets?*

Annex I. Supplementary Information

TITLE OF REFERENCED DOCUMENT

IMF (2008), *Balance of Payments and International Investment Position Manual, sixth edition,* Washington, DC.

OECD (2018), *Recording of Direct Investment Income, Reinvested Earnings, and Dividends: The Case of Superdividends*, Presented at the IMF BOPCOM October 2018 meeting (ref. BOPCOM 18-13c), Washington DC, and at the OECD WGIIS October 2018 meeting (ref. DAF/INV/STAT(2018)8), Paris.

UN (2009), *System of National Accounts*, New York.

OECD (2008), *Benchmark Definition of Foreign Direct Investment, fourth edition*, Paris.

Eurostat (2013*), European system of account 2010*, Luxembourg.

OECD (2017), *Progress Report of the WGIIS Electronic Discussion Group on FDI Income*, presented at the October 2017 WGIIS meeting.

Annex II. Current International Standards for the Treatment of the Issue

BPM6:

11.27 "Exceptional payments by corporations (including quasi corporations such as branches) to their shareholders that are made out of accumulated reserves or sales of assets should not be treated as dividends. Such exceptional payments, sometimes called superdividends, are treated as withdrawals of equity, and therefore recorded in the financial account (as noted in paragraph 8.23). The exceptional nature of the payments is normally determined as being disproportionately large relative to the recent level of dividends and earnings. Although dividends are notionally paid out of the current period's operating sur-plus, corporations often smooth the payments of dividends, sometimes paying out rather less than operating surplus but other times paying out a little more, especially when the operating surplus itself is very low. For practical reasons, no attempt is made to align dividend payments with earnings except when the dividends are disproportionately large. If the level of dividends declared is greatly in excess of previous dividends and trends in earnings, the excess should be excluded from dividends and shown as a withdrawal of equity (see paragraph 8.23)."

BPM6 COMPILATION GUIDE:

13.78 "The superdividends can be identified by the following characteristics:

(1) They are often paid out of the proceeds from sales of fixed assets, operating units, or liquidations.

(2) The level of dividends declared is greatly in excess of previous dividends and trends in earnings (considering around the last five years)."

2008 SNA:

7.131 "Although dividends are notionally paid out of the current period's operating surplus, corporations often smooth the payments of dividends, often paying out rather less than operating surplus but sometimes paying out a little more, especially when the operating surplus itself is very low. For practical reasons, no attempt is made in the SNA to align dividend payments with earnings except in one circumstance. The exception occurs when the dividends are disproportionately large relative to the recent level of dividends and earnings. In order to determine whether the dividends are disproportionately large, it is helpful to introduce the concept of distributable income. Distributable income of a corporation is equal to entrepreneurial income, plus all current transfers receivable, less all current transfers payable and less the adjustment for the change in pension entitlements relating to the pension scheme of that corporation. From this, it is possible to look at the ratio of dividends to distributable income over the recent past and assess the plausibility that the current level of dividends declared is in line with past practice, accepting some degree of smoothing from year to year. If the level of dividends declared is greatly in excess of this, the excess should be treated as a financial transaction, specifically the withdrawal of owners' equity from the corporation.

11.90 "The second type of transaction concerning equity is capital injections by the owners or, on occasion, withdrawals of equity by the owners. Dividends are recorded in the distribution of primary income account as if they were always paid out of operating surplus earned in the current period. An enterprise, though, usually aims to have a smooth track record of dividend payments and will therefore sometimes pay out more than the current operating surplus and sometimes rather less, the balance carrying through to the accumulation accounts by way of saving (which might be negative). However, if the dividends paid out are significantly in excess of recent average earnings, then the excess should no longer all be recorded in the allocation of primary income account but should be regarded as a withdrawal of equity by the owners and be reflected under this item. Such payments are sometimes referred to as "superdividends". Withdrawals may take the form of proceeds from sales of fixed or other assets, transfers of fixed and other assets from the quasi corporation to the owner and funds taken from accumulated retained earnings and reserves for the consumption of fixed capital. (The particular case of payments between government and public enterprises is discussed in Chapter 22.) Equally, liquidating dividends paid to shareholders when an enterprise becomes bankrupt should be recorded as withdrawal of equity."

Annex III. Overview of the Advantages and Disadvantages of A1 vs. A2 vs. A3

Alternative 1	Alternative 2	Alternative 3
Pros	**Pros**	**Pros**
• A clear-cut quantitative criterion remains • The "equity ratio" can also be utilized for newly acquired affiliated enterprises • Accumulated earnings could be viewed as a financial asset	• Maintains the concept of superdividends, while eliminating the existing ambiguity in their operationalization • No micro-analysis is required • Reduce the risks of asymmetries arising from different interpretation of the manuals	• Intra-Consistency of the *BPM6* by removing the current contradiction that exists within and Inter-Consistency of the *BPM6* and the *BD4* by adopting coherent guidance • Comprehensible compilation of disinvestments • Meets compilers practical needs • No micro-analysis is required because the needed classification is provided by the reporting entity • Historical consistency; i.e., accumulated dividends will equal accumulated earnings on a current operating performance concept basis
Cons	**Cons**	**Cons**
• The risk of misinterpreting erroneously positive or too high reinvested earnings remains. • The specification of the criterion remains somewhat arbitrary • A micro-analysis is still required • Historical inconsistency, i.e., accumulated dividends will not equal accumulated earnings on a current operating performance concept basis	• The risk of misinterpreting erroneously positive or too high reinvested earnings remains. • The case of negative reinvested earnings would degrade into an exception, only applied in the case of negative profits of the direct investment enterprise (DIE) • Only meaningful at annual basis.	• Distribution of Extraordinary earnings in the accumulated reserves need to be distinguished from distribution of ordinary earnings. • Inconsistencies with current SNA • Accumulated earnings could be viewed as a financial asset

Annex IV. List of Chapters to Update

STATISTICAL MANUAL—CHAPTER AND PARAGRAPH(S)

Regarding the current statistical standards, implementing A3 would require the following changes:

BPM6: adjustment of 5., 8.23, 11.27, 11.30 to reflect that superdividends should not be applied to direct investment

BPM6 Compilation Guide: deletion of 13.78

2008 SNA: adjustment of 7.132 to clarify that superdividends should not be applied to direct investment enterprises.

BD4: adjustment of 537

STATISTICAL MANUAL—CHAPTER AND PARAGRAPH(S)

Current State	Suggestion for Direct Investment
BPM	
5. Superdividends **8.23** Superdividends and liquidating dividends are defined in paragraphs 11.28 and 11.30. They are treated as a withdrawal of equity, rather than as income payable to the owners. Accordingly, these amounts are excluded from dividends and are shown as a reduction in equity in the financial account, just as any other withdrawal of equity. They also arise for equity other than direct investment.	**5. ~~Superdividends~~ Sales of fixed assets** **8.23** ~~Superdividends~~ Sales of fixed assets and liquidating dividends are defined in paragraphs 11.28 and 11.30. They are treated as a withdrawal of equity, rather than as income payable to the owners. Accordingly, these amounts are excluded from dividends and are shown as a reduction in equity in the financial account, just as any other withdrawal of equity. For practical reasons they are only identified in ~~They also arise for equity other than~~ direct investment.
11.27 Exceptional payments by corporations (including quasi corporations such as branches) to their shareholders that are made out of accumulated reserves or sales of assets should not be treated as dividends. Such exceptional payments, sometimes called superdividends, are treated as withdrawals of equity, and therefore recorded in the financial account (as noted in paragraph 8.23). The exceptional nature of the payments is normally determined as being disproportionately large relative to the recent level of dividends and earnings. Although dividends are notionally paid out of the current period's operating surplus, corporations often	**11.27** Exceptional payments by corporations (including quasi corporations such as branches) to their shareholders that are made out of ~~accumulated reserves or~~ sales of assets should not be treated as dividends. Such exceptional payments~~, sometimes called superdividends,~~ are treated as withdrawals of equity, and therefore recorded in the financial account and displayed under the "of which"-position "sales of fixed assets" (as noted in paragraph 8.23). The exceptional nature of the payments is best determined based on information provided by the reporting entity. An identification on merely quantitative grounds (like the dividend's size

Current State	Suggestion for Direct Investment
smooth the payments of dividends, sometimes paying out rather less than operating surplus but other times paying out a little more, especially when the operating surplus itself is very low. For practical reasons, no attempt is made to align dividend payments with earnings except when the dividends are disproportionately large. If the level of dividends declared is greatly in excess of previous dividends and trends in earnings, the excess should be excluded from dividends and shown as a withdrawal of equity (see paragraph 8.23).	compared to the dividend payment's history) has proven to be misleading due to the generally irregular pattern of dividend payments in direct investment. ~~normally determined as being disproportionately large relative to the recent level of dividends and earnings. Although dividends are notionally paid out of the current period's operating surplus, corporations often smooth the payments of dividends, sometimes paying out rather less than operating surplus but other times paying out a little more, especially when the operating surplus itself is very low. For practical reasons, no attempt is made to align dividend payments with earnings except when the dividends are disproportionately large. If the level of dividends declared is greatly in excess of previous dividends and trends in earnings, the excess should be excluded from dividends and shown as a withdrawal of equity (see paragraph 8.23).~~ Exceptional payments out of accumulated reserves on the other hand should be treated as dividends.
11.30 Liquidating dividends, whether partial or total, arise mainly at the time of the termination of a company. These are treated as a withdrawal of equity, shown in the financial account, as a convention based on the assumption that liquidating dividends are more likely to involve previously existing equity finance rather than current income.	**11.30** Liquidating dividends, whether partial or total, arise mainly at the time of the termination of a company. These are treated as a withdrawal of equity, shown in the financial account under the "of which"-position "sales of fixed assets", as a convention based on the assumption that liquidating dividends are more likely to involve previously existing equity finance rather than current income.
***BPM6 CG* for Direct Investment**	
13.78 The superdividends can be identified by the following characteristics: (1) They are often paid out of the proceeds from sales of fixed assets, operating units, or liquidations. (2) The level of dividends declared is greatly in excess of previous dividends and trends in earnings (considering around the last five years).	~~**13.78** The superdividends can be identified by the following characteristics:~~ ~~(1) They are often paid out of the proceeds from sales of fixed assets, operating units, or liquidations.~~ ~~(2) The level of dividends declared is greatly in excess of previous dividends and trends in earnings (considering around the last five years).~~

Current State	Suggestion for Direct Investment
SNA	
7.132 This treatment applies to all corporations, whether incorporated or quasi corporate and whether subject to public, foreign or domestic private control. There is more discussion on the case of publicly controlled corporations in chapter 22.	7.132 This treatment applies to all corporations, whether incorporated or quasi corporate and whether subject to public~~, foreign~~ or domestic private control, with the exception of direct investment enterprises. There is more discussion on the case of publicly controlled corporations in chapter 22.
BD	
537. It should be noted that RE (and reinvestment of earnings) can be both negative or positive in sign for both the DI and the DIE. Typically, RE will be a debit for income payable by the DIE to the DI, and a credit for such income receivable by the DI (with the offsetting entries for reinvestment of earnings in the direct investment transactions and positions accounts reflecting the opposite directions for these flows). However, if a DIE generates a loss from its current operations (that is, the sum of its operating surplus and its net property income is negative), or if it declares a dividend for more than it has earned in the reference period, a negative debit should be recorded in the Direct Investment Income Account under RE for the DIE (and, correspondingly, a negative credit for the DI). An offsetting negative entry should also be recorded in the Direct Investment Transactions Account (and also be reflected in the Direct Investment Positions Account) of the DIE's economy for the reinvestment of earnings; correspondingly, a positive entry for the same amount should appear in the same accounts of the DI's economy. These entries should be made for both the asset/liability and the directional presentations for both economies. Where a DIE is 100% owned by its DI(s), it will have no net saving of its own, but where there are shareholders not in a FDI relationship with the DIE (whether portfolio investors, if residents of economies other than that of the DIE, or other shareholders who are residents of the same economy as the DIE), the DIE will have savings of its own.	**537.** It should be noted that RE (and reinvestment of earnings) can be both negative or positive in sign for both the DI and the DIE. Typically, RE will be a debit for income payable by the DIE to the DI, and a credit for such income receivable by the DI (with the offsetting entries for reinvestment of earnings in the direct investment transactions and positions accounts reflecting the opposite directions for these flows). However, if a DIE generates a loss from its current operations (that is, the sum of its operating surplus and its net property income is negative), or if it declares a dividend for more than it has earned in the reference period (e. g. by decreasing its accumulated reserves), a negative debit should be recorded in the Direct Investment Income Account under RE for the DIE (and, correspondingly, a negative credit for the DI). An offsetting negative entry should also be recorded in the Direct Investment Transactions Account (and also be reflected in the Direct Investment Positions Account) of the DIE's economy for the reinvestment of earnings; correspondingly, a positive entry for the same amount should appear in the same accounts of the DI's economy. These entries should be made for both the asset/liability and the directional presentations for both economies. Where a DIE is 100% owned by its DI(s), it will have no net saving of its own, but where there are shareholders not in a FDI relationship with the DIE (whether portfolio investors, if residents of economies other than that of the DIE, or other shareholders who are residents of the same economy as the DIE), the DIE will have savings of its own.

Annex V. Supplementary Information

NUMERICAL EXAMPLE A1 VS. A2 VS. A3

	A1*	A1**	A2	A3
Primary income (t)	**1000**	**1000**	**1000**	**1000**
Income on equity	1000	1000	1000	1000
Dividends	0	500	1000	1200
Reinvested earnings	1000	500	0	-200
Financial Account (t)	**-200**	**-200**	**-200**	**-200**
Equity	-200	-200	-200	-200
Equity other than reinvestment of earnings	-1200	-700	-200	0
Reinvestment of earnings	1000	500	0	-200
Change in direct investment position				
Position (yearend t-1)	2000	2000	2000	2000
Financial account transactions	-200	-200	-200	-200
Equity other than reinvestment of earnings	-1200	-700	-200	0
Reinvestment of earnings	1000	500	0	-200
Other changes in volume and valuation	0	0	0	0
Position (yearend t)	**1800**	**1800**	**1800**	**1800**

Scenario: Total income t = 1000, distributions from current period 1000, distributions from accumulated reserves 200

*/**impact depends on which indicator should be applied. To emphasize the arbitrary character of A1, the whole distribution in example A1* is considered “extraordinary” (high in terms of historical pattern of distribution policy on firm-level), in A1** 50%.The aim of this assumption is not to show that A1 or the status quo is completely unfounded. The aim is to underline the impact of the decision, if a specific distribution is extraordinary or not, on the sub-aggregates within DI income: the lower the share of extraordinary distributions, the more A1 approaches A2 (numerically).