

Proposed Recommendations Document:

1.24 Distinction between taxes, services and other flows

Summary Details

Links to Related Guidance/Discussion/Issue Notes and Latest Manuals: WS.14 The borderline between taxes, sales of service, and other government revenue boundary issues Draft 2025 SNA and Draft BPM7	
Global Consultation(s):	Global Consultation: March 2023
Discussions at the Advisory Expert Group on National Accounts (AEG) / Balance of Payments Committee (BOPCOM) Meeting(s):	Joint AEG/BOPCOM: March 2023 ; October 2022 AEG: July 2022 ; May 2022
Discussions at GFSAC Meeting(s):	To be determined
Summary of Proposed Recommendations: <p>This proposed recommendation details three issues for the update of <i>GFSM 2014</i> (all drawn from the SNA/BPM Guidance Note WS.14¹) namely:</p> <ul style="list-style-type: none"> (i) that compulsory payments to government for non-transferable licenses/permits required under a regulatory process should by default be classified as taxes; (ii) that payments to use or extract a natural resource for an extended period of time (for a period less than the lifespan of the natural resource) should be categorized as rent; and (iii) that additional guidance should be included on when to rearrange transactions, related to regulatory schemes, through government. <p>In addition, the SNA/BPM Guidance Note includes a decision tree to assist in classifying government revenue, which will be included in the draft 2025 SNA (Figure 30.2), and it is recommended to also include it in the updated GFSM.</p> <p>The most significant conceptual change is the recording by default of all payments for mandatory non-transferable government licenses/permits as taxes, rather than the current recording which splits them between taxes and sales of service (specifically, <i>administrative fees</i>).</p>	

¹ The SNA/BPM Guidance Note WS.14 also recommends clarifying the definition of what constitutes rent. This is not discussed in this Proposed Recommendation, but it is addressed in the Proposed Recommendations Document *1.2 Treatment of Rent*.

Background and Issues

1. The international statistical manuals contain guidance in relation to the different types of government revenue, including revenues received by government from the issuance of mandatory licenses and permits, the recording of payments to use or extract natural resources, and the rearrangement of transactions through government (impacting on government revenue when implemented). The SNA/BPM Guidance Note WS.14 on *The Borderline Between Taxes, Sales of Service, and Other Government Revenue Boundary Issues*, discusses the existing guidance and makes a number of recommendations on how to improve the guidance in the SNA and BPM. It is proposed to reflect these same improvements in the update to the *GFSM 2014*. A brief summary of the specific recommendations follows.
2. In *GFSM 2014* (paras. 5.72-5.75 and 5.138) it is explained that revenues receivable from issuance of **mandatory licenses and permits** are recorded as *administrative fees* (GFS Code 1422), part of *sales of goods and services* unless (i) permits are automatically granted and the government performs little or no work to issue the permit, (ii) the amount charged for the permits is out of all proportion to the costs of issuance; or (iii) some other specific exceptions. If one or more of these exceptions is met, such fees are recorded as part of taxes as *Other taxes on use of goods and on permission to use goods or perform activities* (GFS code 11452).
3. However the “out of all proportion” test is not well defined, and is applied unevenly across countries. Additionally, it is debateable whether the services that government provides through mandatory licensing and permitting regimes is a requited service to the individual or company seeking the license, or society as whole, who may be protected by policies like licensing regimes for drivers, or regulating travel through passports and visas.
4. **Extraction of natural resources** give rise to several sources of revenue for the government, and how to record these depend upon whether government is the owner of the natural resource, or whether government’s are extracting payments related to the exploitation of natural resources that government does not own. If government is not the owner of the natural resources then the payments to government will generally be recorded as taxes. Where government is the owner of the natural resources then some payments receivable by government may still be recorded as taxes, but others related to the use/extraction of the natural resources will be recorded as *rent* (GFS Code 1415). In the case where the government owner permits the extractor to use the natural resource to extinction the payments receivable are to be recorded as disposal of the natural resource asset.
5. But a further scenario is where government issues a license/permit for the natural resource to be used for an extended period of time in such a way that in effect the user controls the use of the resource during this time with little, if any, intervention from the legal owner, and the permit value is realizable (e.g., transferable). The current guidance in *GFSM 2014* (paras. A4.19-A4.21, and Figure A4.1) states that, in this scenario, the amounts receivable are to be excluded from rent, and instead treated as the *disposal of a contracts, leases and licenses asset* (GFS code 31441), not the sale of the underlying natural resources. This approach is not in line with the *European System of Accounts 2010 (ESA 2010)*, which guides to continue to record rent under this scenario as the natural resource remains on the government balance sheet. The *2008 SNA* is somewhat less clear than the *ESA 2010*, but the SNA/BPM Guidance

Note indicates that the *ESA 2010* treatment is understood to be in accordance with the *2008 SNA* and recommends further clarification in the draft *2025 SNA*.

6. **Rearrangement of transactions** involves either rerouting, partitioning, or reassignment. All the statistical manuals contain similar descriptions of the three types of rearrangement. The existing guidance is relatively clear on when to partition a transaction or to reassign a transaction. The *2008 SNA* (paras. 3.61–3.74), *GFSM 2014* (paras. 3.27-3.30), and *ESA 2010* (paras. 1.72–1.78 and 20.204) all have consistent guidance on rearrangement of these types of transactions.

7. However, what is less clear in the current guidance is when to rearrange transactions that are imposed or mandated by government. There are numerous real-world examples of governments mandating payments directly between consumers and / or producers to have the same economic impact as a direct tax and transfer scheme would have. One common example is “feed-in tariffs”, where government requires electricity suppliers to buy electricity at above market prices from suppliers of (more expensive) renewable energy, achieved by raising prices on their customers – acting in a similar way as a tax on electricity bills and direct subsidies to the renewable producers. These forced transactions can thus be seen as compulsory and unrequited payments, as well as redistributive, and some countries reroute these through the government accounts as taxes/subsidies, but others do not.

8. Although there is guidance in the manuals for some specific instances where transactions should be rerouted (e.g., *GFSM 2014* explicitly mentions transactions related to social security or retirement schemes (para. 6.19), distribution of profits of fiscal monopolies (para. 5.68) and non-resident government SPEs (paras. 2.136-2.139)), there is no explicit guidance on schemes such as feed-in tariffs or the other scenarios described in the guidance note.

9. The guidance note WS.14, recommends that rearrangement should be recorded in the following three scenarios: (i) Where government replaces a pre-existing scheme involving payments to and from government with a new scheme under which the payments, which provide a similar economic outcome, are made directly and not through government; (ii) Where government mandates unrequited payments between economic actors that would not take place without the government intervention; (iii) Where government instigates a price cap, or price fix, but has a mechanism to fund the difference between the price cap and the market price (or another price) by mandating others to make payment direct to the suppliers to whom the price cap/fix applies.

Proposed Recommendations

10. With respect to **mandatory licenses and permits**, the proposed recommendation is that compulsory payments to government for non-transferable licenses issued as part of a mandatory regulatory process should be recorded as *taxes* as the default option, but that under limited scenarios some such payments may still be recorded as sales of service, if the recording can be justified based on principles in the manuals. This will result in most revenues currently recorded as *administrative fees* (GFS Code 1422) under *GFSM 2014* being reclassified as *taxes* as they are by nature compulsory and unrequited. The specific tax category will depend on the payment base and details, but most will likely be categorized under *Taxes on use of goods and on permission to use goods or perform activities* (GFS Code 1145). While the default recording for these mandatory licenses and permits should be taxes, identifying a significant service element could lead to recording as a payment of services in exceptional

cases. Additional guidance to governments on how to identify the significance (materiality) of the service element may be needed.

11. With respect to **treatment of permits to use a natural resource for an extended period of time** the proposed recommendation is to amend *GFSM 2014* to indicate that such permits do not transfer the ownership of the underlying natural resource, and so payments to the government owner should be recorded as *rent* (GFS Code 1415).

12. The sale of such a permit is not recorded as the disposal of an asset (either natural resource or intangible nonproduced nonfinancial asset). However, any permit payments should be assessed against estimates of total natural resource rent using the residual value split asset approach (see draft *2025 SNA* Chapter 27), then allocated (through *an other volume change*) between the permit holder and the government owner to reflect their respective shares of the future economic benefits to be earned. This topic is further discussed in the *GFSM 2014* Update research project 2.19 *Accounting for natural resources and their exploitation in GFS*.

13. With respect to **rearrangement of transactions** through government, the recommendation is to amend *GFSM 2014* to include additional guidance on when transactions related to regulatory schemes should be rerouted through the government sector. This guidance should be based on the text agreed for inclusion in the draft *2025 SNA*, reproduced below in paragraph 22.

14. Consider as part of the *GFSM* update whether the scenarios detailed in the draft *2025 SNA* are sufficiently described and whether there may be additional scenarios where the rearrangement of transactions through government may best reflect the economic reality and support fiscal analysis.

Rationale for Proposed Recommendations

15. The proposed recommendations aim to harmonize the updated *GFSM* with the *2025 SNA* and *BPM7*, a key objective of the *GFSM 2014* update process.

16. The proposed recommendation with respect to **mandatory permits and licenses** addresses the main problem with the existing guidance and inconsistent application of the “out of proportion test”, as well as recognizing the conceptual argument that most mandatory licenses and permits exist to serve a wider societal purpose, rather than for the benefit of the individuals or companies that are required to purchase the permit or license. As a result of this change, mandatory payments to the government are (largely) recorded as either taxes, social contributions or fines and penalties, rather than also including, in some cases, significant revenues under sales of goods and services.

17. The proposed changes to the recording of the **sale of permits to use a natural resource for an extended period of time** is to bring the *GFSM 2014* guidance into line with the principle of resource leases and definition of rent, i.e., that payments made by the economic owner to the legal owner for use of a natural resource in production, for a period less than the lifespan of the natural resource, should be recorded as rent. This will also bring a greater coherence to the recording, as the natural resource asset to which the rent payments relate remains on the government balance sheet.

18. The proposed recommendation for expanding guidance on **rerouting of transactions through government** proposes providing additional guidance on when governments should reroute flows through

the government accounts. This takes into account the increasing use of schemes and policies with the same economic impact of conventional taxes and subsidies, but where those transactions are not currently recorded in the government accounts.

Proposed Text for GFSM Update

19. The main changes arising from the guidance on **mandatory permits and licenses** will require amendments to the existing text in *GFSM 2014*, (paras. 5.73-5.75 and 5.138) in line with the revised guidance in the draft 2025 SNA (paras. 8.82-8.84 9.54-9.55, 9.66, 10.71, and 30.87-30.91). Adjustments may also be needed to the introductory text in *GFSM 2014* (para. 5.26). The proposed language in the draft 2025 SNA (key sections are underlined) states that:

8.82 and 9.54 One of the regulatory functions of governments is to forbid the ownership or use of certain goods or the pursuit of certain activities, unless specific permission is granted by issuing a licence or other certificate for which a fee is demanded. Price levels for these types of mandatory permissions are set by the government, often through some type of executive, legislative, or statutory power. Those seeking the permission or authorization frequently pay with no option to receive a refund should the licence (or similar) not be granted. The permission or authorization granted under these types of schemes is not transferable or tradeable, and so has no direct economic value. Indeed, for many such regulatory schemes the payer of the fee is not to be seen as the primary beneficiary, as the motivation behind the regulation or licencing of an activity or good is to protect society as a whole and ensure that those engaging in an activity or owning a good are able to do so safely in accordance with laws. For example, driving licences are intended to ensure that those using the road networks have the necessary skills and knowledge to do so safely. Although the payer benefits from being able to drive the primary beneficiary is society. For the above reasons, mandatory payments for most regulatory licences, or similar certificates, are to be recorded as taxes, as they are by nature compulsory and unrequited.

8.83 and 9.55 Although most payments under mandatory regulatory schemes should be recorded as taxes, there may be cases where recording as a sale of service is appropriate despite the compulsory nature of the payment. For instance, the cost of a mandatory safety inspection may be based on the cost to government of conducting the inspection and could include a service element, such as providing guidance on how identified safety hazards can be rectified. In this case it might be appropriate to record the payment as a payment of service rather than a tax, but only if the service element of the payment is considered sufficiently material. To recap, the default recording for payments under government-imposed mandatory regulatory schemes should be as taxes, unless a significant service element can be identified leading to recording as a payment of service.

30.88 One of the regulatory functions of governments is to forbid the ownership or use of certain goods, or the pursuit of certain activities, unless specific permission has been granted by issuing a permit or license for which a fee must be paid. Most mandatory payments for permits and licenses authorizing pursuit of an activity or ownership of a good can be considered unrequited, making them a tax rather than a fee for services. Usually, the primary beneficiary of the regulatory schemes that require these payments is society as a whole, not the individual unit making the payment. In other cases, the permit is simply issued automatically upon receipt of the payment. Furthermore, the payments to apply for a permit or license are frequently nonrefundable if the permit or license is not granted.

30.89 Nevertheless, as noted in paragraph 9.55, in cases where the transaction involves a material service element and the payment amount is not disproportionate to the cost of supplying the service, recording a sale of services to the recipient of the permit or license may be appropriate.

20. With regard to **permits to use a natural resource for an extended period of time**, the existing text in *GFSM 2014* (para. 5.124), as well as the extended text on Resource Leases in Appendix 4,

including Figure A4.1 will require amendments. These amendments will make clear that, where permits are issued for the use of a natural resource for a period less than the natural resource economic lifespan, payments received by government as economic owner of the resource should be recorded as rent. The text will be aligned with the related draft 2025 SNA text in Chapters 11, 13 and 27.

21. In addition, the guidance note includes a new decision tree to help guide the classification of government receipts. This decision tree (see Annex) included in the draft *SNA 2025* (Figure 30.2) should also be included in the updated *GFSM*. This will support both the new guidance on mandatory permits and licenses and the new guidance on permits to use a natural resource for an extended period of time.

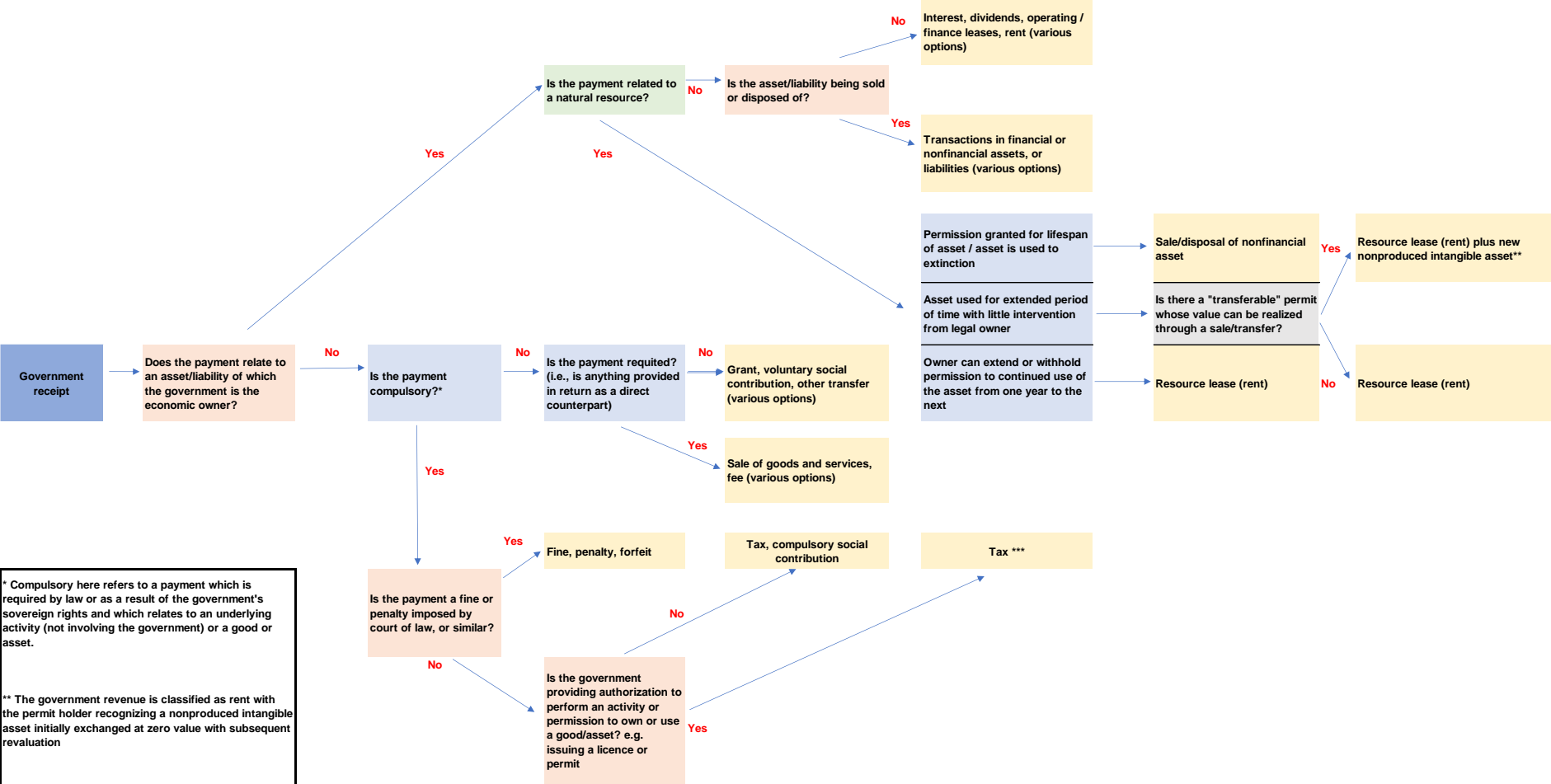
22. Finally, with respect to the **rearrangement of transactions through government**, the existing text on rerouting in *GFSM 2014* (para. 3.28) will be expanded to add additional examples of cases where it is appropriate to reroute, in line with the discussion in the GN WS.14 and guidance in the draft 2025 SNA (paras. 30.170-30.171), reproduced below:

30.170 Government regulatory schemes may also give rise to situations where transactions involving nongovernment units should be rerouted through the government accounts. For instance, the government may mandate that certain economic units (e.g., fossil fuel based energy suppliers) make regular payments directly to other economic units (e.g., renewable energy suppliers). In such a case it can be assumed that the payments would not be made without the intervention of the government, and to capture the economic reality the payments might be rerouted through the government unit imposing the regulation as taxes from the units making the payments and subsequent subsidies to the units receiving the payments. However, care should be taken to not apply this principle too widely. Rerouting transactions through government should be limited to where government obliges non-government units to make unrequited payments to other non-government units (such as by replacing a tax and subsidy scheme with a regulatory scheme).

30.171 One additional area where rearrangement may be considered is where government fixes a price, or price cap, for certain goods or services. The existence of a fixed price or price cap should not by itself lead to any rearrangement through the government accounts. However, in some circumstances the government may have a mechanism where it agrees to fund the difference between the observed market price and the price cap. If the government simply pays the difference then no rearrangement is required, but if the government imposes a tax (or similar arrangement) to fund the difference and this is not paid to the government but directly to the suppliers to whom the price cap/fix applies, then this should be rerouted through the government accounts.

23. In addition, where government instigates a price cap, or price fix, but has no mechanism to fund the difference between the price cap and the market price (or another price), some further consideration may be needed on how to transparently report in government accounts on these differences.

Annex: Decision Tree for Classifying Government Receipts



* Compulsory here refers to a payment which is required by law or as a result of the government's sovereign rights and which relates to an underlying activity (not involving the government) or a good or asset.

** The government revenue is classified as rent with the permit holder recognizing a nonproduced intangible asset initially exchanged at zero value with subsequent revaluation

*** There may remain some limited scenarios where such payments might be recorded as a Sale of Services, but these must be fully justified in accordance with the principles of the manuals.