



## Proposed Recommendations Document:

### 1.7 Recording of Fines and Penalties

#### Summary Details

<b>Related Guidance Note (SNA/BPM) or Discussion Note (GFSM):</b> <a href="#">GN C.8 Recording of Fines and Penalties</a>	
<b>Global Consultation(s):</b>	BP Consultation: <a href="#">February 2021</a> BP Consultation Outcome: <a href="#">February 2021</a>
<b>Discussions at AEG / BOPCOM Meeting(s):</b>	BOPCOM: <a href="#">February 2021</a>
<b>Discussions at GFSAC Meeting(s):</b>	To be determined
<b>Summary of Proposed Recommendations:</b> <p>To extend the current <i>GFSM 2014</i> definition of fines and penalties to clarify that they are compulsory payments imposed on units by courts of law or quasi-judicial bodies for violations of laws or administrative rules, which are <b>generally punitive in nature</b>. To further clarify that efforts should be made to distinguish between fines/penalties (which are punitive in nature) and compensation payments (which are intended to compensate for damage or injury), noting that a court ruling may commonly include both elements. To leave unchanged the current <i>GFSM 2014</i> guidance on the time of recording of fines and penalties. To align the language in the <i>GFSM</i> update to that of the draft 2025 <i>SNA</i> and <i>BPM7</i>, to the extent possible.</p>	

#### Background and Issues

1. In the international statistical standards, fines and penalties are treated similarly to current taxes on income, wealth, etc. However, in practice they are often more closely tied to payments for compensation for damages. For example, following a major event such as an oil spill, fines owed by the responsible party to the government and compensation owed by the responsible party to the affected parties are often determined in the same settlement; sometimes these amounts are reported indistinguishably. As fines and penalties have become more frequent and are sometimes very large, including large transactions involving fines related to corruption, banking supervision, and antitrust, there is a need to clarify the treatment in macroeconomic statistics of fines and penalties, including those which provide a compensation element.

2. The [BPM guidance note](#) refines the definition of *finances and penalties* and discusses three broad issues which are of relevance to the *GFSM* update, (i) how to distinguish between fines or penalties and compensation payments, (ii) when to record compensation payments as capital, rather than current transfers, and (iii) the time of recording for payments related to court judgments. The guidance note also discusses issues which are specific to external sector statistics, such as how to account for fine/penalty transactions imposed on multinational enterprises and impacting direct investment income, and how to reflect contingent fines and penalties in the recording of mergers and acquisitions. Finally, the guidance note recommends drafting additional compilation guidance on the identification and reporting of fines and penalties.

3. *GFSM 2014* (para. 5.142) defines fines and penalties as “*compulsory current transfers imposed on units by courts of law or quasi-judicial bodies for violations of laws or administrative rules, Out-of-court agreements are also included*”. This is a more complete definition than that in either the *2008 SNA* (paragraph 8.135) or the *BPM6* (paragraph 12.54) but it doesn’t sufficiently distinguish between fines/penalties and court-imposed compensation payments, both of which are compulsory in nature. To further distinguish between the two the *BPM* guidance note recommends that fines/penalties are defined as compulsory payments that are *punitive in nature*, that is, are intended to punish and/or deter certain activities or behavior, while compensation payments by contrast are intended to remedy specific harms, such as property damage or loss of income.

4. While fines and penalties are always current transfers this is not the case for compensation payments. The *GFSM 2014* (para. 5.148) notes that capital transfers receivable should include “*major nonrecurrent payments receivable in compensation for extensive damages or serious injuries not covered by insurance policies. The payments may be awarded by courts of law or settled out of court. They include payments of compensation for damages caused by major explosions, oil spillages, etc.*”. On the payable side *GFSM 2014* (para. 6.124) indicates that capital transfers should include “*major, nonrecurrent, exceptional payments in compensation for extensive damages or serious injuries such as those arising from catastrophes*”. *BPM6* uses very similar language (para. 13.29) as well as noting that “*major compensation payments for extensive damages (e.g., oil spillages or side effects or pharmaceutical products) are treated as capital rather than current transfer*” (para. 12.56). The *BPM* guidance note points out that while this guidance is helpful it is not always clear on what constitutes a “major payment” or “extensive damages”. After discussion it was therefore recommended to include an additional clarification that compensation payments should be treated as capital transfers if they are “intended to recover losses over a multi-year period or to replace an asset (financial or nonfinancial)”.

5. With regard to compulsory transfers the *BPM6* notes that they are to be recorded “when a legal claim to the funds is established, which may be when a court renders judgment or an administrative ruling is published” (para. 12.18). However, this guidance is insufficient as significant fines and penalties and rulings on other compulsory transfers are often appealed after they are issued, such that the final amount due may not be known until many years after the judgement is announced. The *GFSM 2014* already specifies that fines and penalties should be recorded “*when the general government unit has an unconditional claim to the funds*” (para. 5.144). The reference to an “unconditional claim” is only included in the *GFSM 2014* and is missing from the similar passages in the *2008 SNA* and *BPM6*. Regarding judgments or rulings that may not be final, the *GFSM 2014* states that if the “*judgment or ruling is subject to further appeal, then the time of recording is when the appeal is resolved*” (para. 3.85). This is important

as the counterpart entity of fines/penalties is classified inside general government, and only amounts that are irrevocable (unconditional) should be regarded as government revenue. The *BPM* guidance note recommended that both of the *GFSM 2014* clarifications regarding time of recording should be included in the draft *2025 SNA* and *BPM7* to bring the standards into alignment.

### Proposed Recommendations

6. The proposed recommendations are to adopt guidance in the updated *GFSM*:
  - a. To define a fine/penalty payment as one that is “punitive in nature” and to more clearly distinguish these payments from payments of compensation, which are intended to compensate for injury or damages;
  - b. To indicate that major compensation payments should be recorded as capital transfers (instead of current transfers) if they are “intended to recover losses incurred over a multi-year period or to replace an asset (financial or nonfinancial).”

### Rationale for Proposed Recommendations

7. The proposed recommendations aim to harmonize the updated *GFSM* with the *2025 SNA* and *BPM7*, a key objective of the *GFSM 2014* update process. Specifically, it will provide consistency across all the macroeconomic statistical standards in (i) distinguishing punitive in nature payments from payments of compensation—intended to compensate for injury or damages, and (ii) recording major compensation payments as capital transfers—when they are intended to recover losses incurred over multi-year periods or to replace an asset.

### Proposed Text for GFSM Update

8. Align or supplement the text of the *GFSM 2014* to that in the draft *2025 SNA* (paras. 9.138-9.141 and 9.146-9.147) and *BPM7* (paras. 13.54-13.56 and 14.29) the text of which is reproduced below.

#### Draft 2025 SNA:

#### **Fines and penalties**

*9.138 Fines and penalties are compulsory payments imposed on institutional units by courts of law or quasi-judicial bodies. However, fines or other penalties imposed by tax authorities for the evasion or late payment of taxes cannot usually be distinguished from the taxes themselves and are, therefore, grouped with the latter in practice and not recorded under this heading; nor are payments of fees to obtain government licenses. (see paragraphs 9.54 and 9.55).*

*9.139 Fines and penalties should be distinguished from payments of compensation (see paragraph 9.146). While fines and penalties are compulsory payments that are punitive in nature, that is, are intended to punish and/or deter certain activities or behavior, compensation payments are intended to remedy specific harms, such as property damage or loss of income. As such, it may be appropriate to treat certain fines and penalties that are identified in legal documents as a fine/penalty, but are actually intended to compensate for damages, as payments for compensation of damages. Fines and penalties are always recorded as a current transfer.*

*9.140 Given the number of appeals that often follow an initial ruling, fines and penalties should not be recorded until the unit issuing the fine/penalty has an unconditional claim to the funds. If a judgment or*

*ruling is subject to further appeal, an unconditional claim only exists when the appeal is resolved. Fines and penalties accrued but not yet paid should be recorded as other accounts receivable and payable.*

**9.141** *Some fines and penalties may be established in contracts of mergers and acquisitions where the contract may include contingent fines or penalties based on, for example, profitability, or a pending lawsuit, and resulting in a payment between the buyer and seller after the initial transaction. In these cases, the fines and penalties would be interpreted as an adjustment or update of the exchange value of the acquired enterprise and treated as a direct investment transaction (or a portfolio investment transaction if the buyer has less than 10 percent of the voting power), instead of a current transfer.*

### **Payments of compensation**

**9.146** *Payments of compensation consist of current transfers paid by institutional units to other institutional units in compensation for injury to persons or damage to property caused by the former that are not settled as payments of non-life insurance claims. Payments of compensation could be either compulsory payments awarded by courts of law, or ex gratia payments agreed out of court. This heading covers compensation for injuries or damages caused by other institutional units and ex gratia payments made by government units or NPISHs in compensation for injuries or damages caused by natural disasters. However, major compensation payments should be recorded as capital transfers (instead of current transfers) if they are intended to recover losses incurred over a multi-year period or to replace a financial or non-financial asset.*

**9.147** *Regarding the time of recording of compensation payments, the same rules apply as the ones for fines and penalties (see paragraph 9.140).*

### **Draft BPM7:**

### **Fines and penalties**

**13.54** *Fines and penalties are compulsory payments imposed on institutional units by courts of law or quasi-judicial bodies. Fines and penalties are generally punitive in nature and are treated as miscellaneous current transfers. Fines and penalties imposed by courts of law or other government bodies that are actually intended to compensate for injury to persons, damage to property, or other losses should be considered as compensation payments (instead of fines and penalties) and would be recorded as either current or capital transfers as explained in paragraphs [13.55 and 13.56]. Early or late repayment penalties agreed as part of a contract are not included in current transfers; they should be treated along with the associated good, or service, or income, as appropriate.*

**13.54a** *Some fines and penalties may be established in contracts of mergers and acquisitions where the contract may include contingent fines or penalties based, for instance, on profitability, or a pending lawsuit, and resulting in a payment between the buyer and seller after the initial transaction. In these cases, the fines and penalties would be interpreted as an adjustment or update of the market price of the acquired enterprise and are treated as a direct investment transaction (or a portfolio investment transaction if the buyer has less than 10 percent of the voting power), instead of a current transfer.*

### **Compensation payments**

**13.55** *Compensation payments consist of transfers paid by institutional units to other institutional units in compensation for injury to persons, damage to property, or other losses (usually caused by the former) that are not settled as payments of nonlife insurance claims. Payments of compensation could be either compulsory payments awarded by courts of law or settlements agreed out of court. Compensation may cover nonfulfillment of contracts, injuries to persons, damages to property, or other losses that are not covered by insurance policies. This heading covers compensation for injuries or damage caused by other institutional units. It also includes ex gratia payments made by government units or NPISHs in compensation for injuries or damages caused by natural disasters.*

*13.56 Major compensation payments for extensive damages (e.g., oil spillages or side effects of pharmaceutical products, or anti-competitive behavior) are treated as capital rather than current transfers (see also paragraph [14.29]).*

*14.29 Major payments in compensation for extensive damages or serious injuries not covered by insurance policies that are typically intended to recover losses over a multi-year period or to replace a nonfinancial or financial asset are included in capital transfers. The payments may be awarded by courts of law or by arbitration or settled out of court. They include payments of compensation for damages caused by major explosions, oil spillages, the side effects of pharmaceutical products, anti-competitive behavior, and so forth. However, if an amount payable under a court order or settlement is identifiable to a specific unpaid debt, it should be recorded under the relevant financial account item. See also paragraphs [13.55–13.56] for payments of compensation included in current transfers.*

**Current GFSM 2014 references:**

- Paragraphs 5.142-5.144 and 5.148
- Paragraphs 6.123-6.124
- Paragraph A7.124