

***THEORETICAL AND PRACTICAL ISSUES ON RECORDING
TRANSPORTATION SERVICES IN THE BALANCE OF PAYMENTS***

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1. INTRODUCTION

This paper deals with international freight services. Although it covers only sea transport of merchandise, most of the cases are applicable to other means of transportation.

The purpose of the paper is twofold:

- a) To discuss some specific transactions, as regards their accounting in the Balance of Payments
- b) To analyze the feasibility of using the Bill of Lading (B/L) as a source of information for freight services.

The idea of looking for non-traditional sources of information stems from:

- i) deficiencies in traditional sources such as surveys
- ii) the need for more complete information to meet new requirements, such as geographical breakdown.

In relation to the topic of sources of information for freight services, paragraph N°220 of the Compilation Guide distinguishes between an approach based on individual ships and one based on the entities that operate those vessels. Both approaches have advantages and disadvantages, and should be viewed as complementary rather than competitive.

In Chile, resident operating transportation companies are surveyed annually or quarterly. The advantage of this source of information is that it covers comprehensive data that meets both Balance of Payments (BOP) and System of National Accounts (SNA) requirements. However, it has serious problems in terms of quality, coverage and timeliness. For this reason, the Central Bank has developed a program to obtain information on freight directly from Customs data (import and export declarations). Customs data in Chile is reasonably accurate, as it is considered official, and non-compliance is subject to penalties. In addition, it is timely, frequent, and covers a significant number of variables (for example: counterpart countries, ports, commissions). One of the drawbacks of this source of information is that it covers international freight only on exports and imports. Therefore, in Chile, BOP data are compiled using both traditional surveys and customs sources.

Using this new source of information has brought to the attention of Chilean BOP compilers some problems, which are related mainly to specific transactions affecting the sea transport of goods. The cases presented in the paper, therefore, reflect on-going work and discussions within the Central Bank of Chile.

The approach suggested in the paper is based on the ships, and relies on the transportation contract, i.e., the Bill of Lading (B/L), as the basic unit from which the relevant information is derived. In Chile, data on freight derived from customs documentation data is based on this document.

The Balance of Payments Manual and accompanying guides (the Compilation Guide and the Textbook) provide guidelines and analyze cases which are generally applicable to different economies. However, when analyzing more specific aspects, borderline or more complicated cases make it sometimes necessary to apply approaches or procedures not specifically set out in the general conventions. The paper may also be used as a guide to discuss to what extent these approaches may be applied in other cases.

2. METHODOLOGICAL ASPECTS

2.1 General background

Freight covers services related to the shipment of goods (be it by sea, air or other means) provided by residents of an economy to non-resident entities. The international transport of goods is generally backed by an agreement or contract whereby an exporter or importer (usually through an intermediary), entrusts the transfer of merchandise to a carrier (or to an intermediary), paying a conventional rate. In the case of international sea transport, the contract is called Bill of Lading (B/L).

The parties involved in these contracts are: the supplier of the freight service, which is usually the operator of the carrier (or its representative), and the unit that demands the service, which is ultimately the importer, regardless of the various modalities of the operation and the number of intermediaries that participate in it. It is frequent practice to have other parties involved, such as forwarders - who usually act on behalf of an importer or exporter, and shipping agencies, on behalf of an operator.

The questions raised are:

- a) To what entity (and thus, country), are freight services to be attributed in certain transactions?
- b) How is the value of freight and its distribution among parties determined in certain cases?

To answer these questions, it is necessary to analyze the nature of the freight operation, since:

- a) the distinction between a contract for leasing a ship and a contract for transporting goods is not always clear-cut.

b) in some cases it is not easy to determine to whom the freight should be assigned.

2.2. *Attribution of transportation services*

For BOP purposes it is useful to review the nature of maritime contracts.

2.2.1 It is possible to distinguish two aspects of them, according to the type of underlying responsibility

a) Operational responsibility:

It falls on the entity that assumes the government and direction of the vessel and that, therefore, determines the ship's routes and schedules (the "operator"). In the case of sea transport, this responsibility would fall on the entity authorized to name the Captain of the ship.

b) Commercial responsibility:

It falls on the entity that makes a commitment with the exporter or importer (or their representative), to transport a certain merchandise in the terms defined in the corresponding B/L (the "shipper").

If there are no intermediaries, these two types of responsibilities are undertaken by the carrier. In the case of the multimodal transport, for example, the shipper has commercial responsibility over the whole period during which the goods are under its custody, whereas operational responsibility falls on several means of transport. In this case there could be two or more entities with operational and commercial responsibility.

The general rule in BPM5 is that freight should be assigned to the operator of the ship, regardless of who its owner might be.

2.2.2 It is useful to distinguish between contracts for transporting goods and contracts for leasing ships, a distinction which is not always clear-cut.

Regarding lease contracts, it is necessary to recall the distinction between leasing a bare boat and leasing a ship with crew.

If leasing a bare boat, the entity can sublease it, or operate it. For the latter purpose, it would have to equip the boat and hire the crew. In this case, the entity would become an operator, and it would therefore be necessary to attribute to it, the revenues of the freight of the goods that it transports.

The classification of leases of ships by trip or by time are special cases in which the same approach must be followed.

2.2.3 Another important distinction to make is among different types of Bills of Lading:

- a) A Master B/L is that issued by the operator
- b) A so-called House B/L is issued by a non-operator entity (NVOCC, non-vessel operating common carrier), and underlies a secondary or sub-transportation contract, which refers to the total or part of the object leased in a master B/L.

3. *SELECTED CASES*

3.1 *Joint services*

It is frequent in the shipping business to form a kind of consortium of companies to exploit a certain traffic. This association -which may have different administrative and other arrangements, is known as a joint service arrangement. The intervening lines may assign one or more ships to this service, according to the provisions of the agreement. It is usual for the lines to provide cargo capacity in terms of teus¹. In this context, a ship may carry cargo in terms established under a master B/L issued not only by the company that operates the ship - the “effective operator” - but also by the other intervening lines- “operators”.

The relevant question in practical terms, specially if the B/L is to be used as a source of data, is: if the B/L is issued by a company different from the effective operator, who should the freight be attributed to ?

This idea may be explained by the following example applicable to Chile:

Consider a joint service in which the participants are vessels belonging to CSV, a resident Chilean transport company, and ships belonging to HL and HS, two German transport companies. According to the joint service arrangement, CSV (acting as an operator) can transport cargo on board HL or HS ships (the effective operators), issuing master BLs. Conversely, HL and HS (acting as operators), can carry cargo on CSV ships (effective operator), issuing their own master B/Ls.

This may be illustrated by presenting the case of a hypothetical joint service in which the participants are the Chilean company CSV and the German companies HL and HS. Consider an export from Chile to Norway carried on board a ship operated by CSV, but whose B/L is issued by HL. The value of the freight collected from the importer is worth 1.000, and the effective cost of the service is 950 monetary units.

Two approaches could be followed for BOP accounting:

¹ Twenty foot container equivalent unit

a)- Freight is attributed to the effective operator (in this case, CSAV), even though this line doesn't receive the value of the freight from the Norwegian importer, as the transport contract takes place between the importer and the German line (HL).

The rationale behind this would be that the issuer of the master B/L (HL in this example), collects the value of the freight from the Norwegian importer on behalf of CSV, who is the operator providing the service. According to this approach, HL would be acting as a sort of cargo agent or forwarder, earning a differential (this amount could be considered as a commission for obtaining the business) between the value that it receives from the importer and the one that it pays CSV (according to the terms of the joint service agreement).

The entry in the BOP of Chile would be:

ENTRY N° 1	CREDIT	DEBIT	NET
Transportation freight (b 1.1.2)	1.000		1.000
Banks (3.1.3.3.)		950	-950
Sea transport-other (b.1.1.3)		50	-50

The value 1.000 represents a transaction between CSV, resident of Chile, and the importer, resident of Norway. The “commission”, worth 50, would be a transaction between CSV and HL, resident of Germany.

b) Freight could be attributed to the issuer of the master BL, in the example, to HL, even though this company is not the effective operator of the vessel.

i) Accordingly, no entry for transport of the merchandise itself would be made in the Chilean BOP, as it would be considered a transaction between non-residents.

ii) However, the use of space by HL on the CSV vessel could be viewed as a type of “lease of space” on a vessel, and would be a transaction between a resident (CSV) and a non-resident, and therefore be recorded as an export of services in the BOP. According to paragraph 500 of Compilation Guide, it would be included under Transportation-freight (b.1.1.2).

If the information on the cost the German line pays CSV for using the space on the Chilean ship – 950 in the example – were available, the following entry in the BOP of Chile could be made :

ENTRY N° 2	CREDIT	DEBIT	NET
Transportation-freight (B.1.1.2)	950		950
Banks (3.1.3.3.)		950	-950

From a practical point of view, in the Chilean case, both alternatives a and b.ii would imply considerable efforts, given the almost null possibility of obtaining information on revenues and cost provisions of joint services. Therefore, the more simple approach (b.i) is suggested. Accordingly, the determination of the freight supplier is simple, since it would be the issuer of the master B/L, regardless of whether the ship be operated by CSV, HL, or HS.

Problems of proposed approach

This treatment underestimates transportation credits of individual exports, as may be seen in the example.

However, if viewed from a broader perspective, the possible underrecording would be netted out against overrecording which would occur in the opposite cases; i.e., of exports carried on vessels operated by HL and HS under master B/Ls issued by CSV, according to the terms of the joint agreement.

This is so if, as is common practice, joint agreements involve proportional sharing of cargo on certain routes operated by the participants. In the example, to simplify, it can be assumed that each of the 3 lines places a ship of certain characteristics, and that in each of those vessels, the space is divided equally among them (1/3 for each company). As can be seen in the example of the Appendix, the final result of the BOP entries of the proposed practical approach would be the same as in the theoretical treatment (a), when all exports carried on the three ships are considered.

Further, joint services may be viewed as being provided by a special type of operator. As was pointed out previously, one of the functions of an operator is to govern and direct the ship, and to determine the routes and itineraries that it will follow. With the proposed approach, freight is attributed to the issuer of the master B/L, which is not the effective operator of the ship. Nevertheless, the operational responsibility in a joint service may be viewed as being undertaken by the group of companies, as it is the group that decides the routes and itineraries

to be followed by the participants in the joint services agreement. It follows that -on the aggregate – it is as if each joining line were operating "effectively" each of the ships assigned to the joint service, but for a proportion of the cargo (one third, in the example).

This approach has the advantage that in this case it is data on the issuer of the master B/L that is usually available, while the possibility of obtaining information on the distribution of the costs and benefits of the joint service among the joining lines is practically null.

3.2 Intervention of non-operating intermediaries

Another frequent case in the shipping business is the participation of forwarders, entities that don't operate ships. Their main functions are:

- a) to provide a series of related services such as administrative paperwork and procedures related to shipment, packing, consultantship in routes, rates, etc.
- b) to make optimum use of space in the transport of goods. This second function may be viewed as serving as retailers of cargo, in the commercial chain that links transport lines with final users of these services.

An example to clarify the latter could be the following:

A forwarder, - say, Panalpina - signs a contract with Mitsui O.S.K. Lines, Ltd. - a Japanese carrier- according to which it leases space (1 TEU) on a trip from Osaka to Valparaíso - for a conventional rate of US \$2.000 for teu. Mitsui issues a Master B/L. In order to fill the hired space, the forwarder looks for clients interested in sending cargo through that route. To simplify , it is assumed that no other intermediary is involved in this transaction. Panalpina signs contracts with 2 Chilean importers (or their representatives), agreeing on a rate of US \$2.200 for teu. Panalpina issues two house B/Ls, related to the master B/L issued by Mitsui.

Again, it is necessary to determine:

- a) To whom the freight should be attributed
- b) The value of the service (US \$2.000 or US \$2.200 for teu?)

These problems don't pose significant theoretical difficulties, as it is possible to view the transportation service as being provided by the entity that issues the master BL (Mitsui), and that the value of the service is US \$2.000 per teu. The differential of US \$200 - which represents the difference between the wholesaler and retailer cost of the service - should be considered as a commission. Its inclusion in the BOP depends on the residences of the intervening parts. If the forwarder is a Japanese resident, the following entry should be made in the Chilean BOP:

ENTRY N° 3	CREDIT	DEBIT	NET
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Transportation – Freight (b.1.1.2)		2.000	-2.000
Transportation - Other (b.1.1.3)		200	-200
Banks (3.1.1.3)	2.200		

This case is relatively simple from the theoretical point of view. However, in Chile, it involves a practical problem if the data are to be derived from B/Ls. Chilean Customs documentation is based on the last B/L issued (house, or other than master B/Ls, according to the number of intermediaries involved); that is to say, the B/L in which the participants are either the importer or exporter (or their representative) and the forwarder. The information on freight services, therefore, is of retail values. It is possible to identify the issuer of the master B/L, but not the value therein. Therefore, there is no information on the differential perceived by the forwarder, and estimates of these commissions should be considered in order to not overestimate freight figures. In the example, the differential between US \$2.200 and US \$2.000 should be estimated on the basis of the first amount.

A practical solution could be to isolate (through a computer program) those transactions in which issuers of master B/Ls differ from issuers of house (or other) B/Ls. Once determined, commissions charged in these operations could be estimated.

A more simple, albeit unorthodox, approach, would be to attribute the provision of the service to the issuer of the house B/L, Panalpina in the example, and to register it as a debit worth 2.200.

3.3 Other non-operating issuers of B/L s

This refers to cases in which an entity that is not a ship operator, usually an exporter or importer, leases a ship (totally or partially) to transport its own merchandise. This company may be entitled to issue B/Ls when it subleases space to others. The important thing is to highlight that the company only leases space, by trip or for a certain period of time, without intervening in the vessel's operation.

According to the guidelines (paragraph N°500 of the Compilation Guide), these payments should be registered under Freight. This is because the underlying nature of the contract is the transportation of goods. The entity really providing the freight service is the

operator of the ship, while the one that demands it is, ultimately, the importer (or his representative). The distinction between the party contracting the service- the exporter or importer - and the final demander of that service - the importer- is important, as may be seen in the following example.

Suppose that Peachapple and Co., a Chilean exporter of fruit, leases an equipped ship (with crew) for a period of 6 months in order to export its merchandise to European markets.

It is necessary to bear in mind that if Peachapple and Co. pays the service it is because the fruit it sells is delivered in Europe, that is to say, it sells in CIF or C&F terms. Therefore, the cost of transportation - included in the sale price of the fruit - is recovered when the fruit is sold. In other words, the situation is the same as if Peachapple and Co. sells in FOB terms and pays the freight on behalf of the European importer.

For BOP purposes, two cases should be considered:

a) that the operator of the ship is a resident of Chile

In this case, the freight service should be registered in BOP since both the entity operating the ship and the company hiring the space on the ship are residents of Chile, and the importer, who ultimately demands the service, is a non-resident. The accounting would be similar to that of entry N° 2 (a credit entry under Transportation-freight, and a debit under banks, for the same amount).

b) that the operator is a non-resident

In this case, two approaches may be followed

i) Not to register freight in the BOP

The rationale is that, since the carrier and the importer are both non-residents, the transportation service in itself would be a transaction between two non-residents.

ii) To register the transportation service between Peachapple and the European operator of the ship and make a compensatory entry in the same item of the BOP.

Interpreting the approach suggested in paragraph N°500 of the Compilation Guide, the service provided by the non-resident carrier to Peachapple would be a debit under freight, and a credit, also under freight, would be the counterpart, which could be interpreted as the freight service provided by Peachapple (resident of Chile), to the importer (resident of Europe). The complete operation in the Chilean BOP would be the following, assuming that the FOB value of the fruit is 1.000, and that of the lease is 100:

ENTRY N° 4	CREDIT	DEBIT	NET
Transportation freight (1.1.2)		100	-100
Banks (3.1.3.3.)	100		100

The debit in freight represents the transaction between Peachapple and the European operator of the vessel (a service provided by the operator to Peachapple).

ENTRY N° 5	CREDIT	DEBIT	NET
Merchandise -FOB (1)	1.000		1.000
Transportation freight (1.1.2)	100		100
Banks (3.1.3.3)		1.100	-1.100

Credits are the fob value of fruit exports and the value of freight (the transaction between Peachapple, viewed as a provider of the service, and the importer).

The credit and debit in freight cancel out , thus, in net terms, both forms of recording (b.i and b.ii) are equivalent.

In practical terms, in the example, the B/L is usually issued by the operator, a non-resident of Chile, therefore, approach b.i would result automatically from customs data (export declarations).

When these companies issue B/Ls for other exporters or importers, they perform the role of forwarders, and the appropriate approach would be that set out in number 3.2 .

4 CONCLUSIONS

- a) The use of customs information based on the issuer of B/L and the values contained therein is a promising source of information for transportation services
- b) Certain arrangements involve important theoretical and practical questions that need to be fully explored, specially if the use of information linked to B/Ls is to be used
- c) Three cases are discussed:
 - i) For joint services, freight may be assigned to the issuer of the B/L, even though it may not be operating the ship. This would be an exception to the general rule of assigning freight to the operator. The rationale is that in joint services, decisions on routes, itineraries and, in general, on commercial policy, are made jointly by the participants of the agreement, and that the overall result is the same when all transactions are considered.
 - ii) When cargo intermediaries (forwarders) intervene, freight should be assigned to the issuer of the master B/L, in accordance with the general principles in the Manual. However, in Chile, it would be necessary to estimate the difference between the value of freight collected by the issuer of the last B/L in the commercial chain, and the amount received by the operator. In other words, it is necessary to estimate the difference between the retailer and the wholesaler price of the freight.

iii) The cases in which an entity leases a ship with crew (for a certain time or trip), to transport its own merchandise, are not common in Chile, but are analyzed mainly for theoretical reasons. Even so, in these cases, the usual practice makes the B/L an adequate tool for obtaining information to assign freight.

APPENDIX

Consider a joint service in which the participants are vessels belonging to CSV, a resident Chilean transport company, and ships belonging to HL and HS, two German transport companies. According to the joint service arrangement, CSV (acting as an operator) can transport cargo on board HL or HS ships (the effective operators), issuing master B/Ls. Conversely, HL and HS (acting as operators), can carry cargo on CSAV ships (effective operator), issuing their own master B/Ls.

To illustrate alternative BOP recording, we can examine the case of an export from Chile to Norway carried on board a ship operated by CSV, but whose B/L is issued by HL. The value of freight collected from the importer is 1.000, and the effective cost of the service is 950 monetary units.

It is common practice that joint agreements involve proportional sharing of cargo on certain routes operated by the participants. In the example, to simplify, it can be assumed that each of the 3 lines places a ship of certain characteristics in the same route, and that in each of those vessels, the space is divided equally among them (1/3 for each company). Therefore, it is assumed that each boat carries 3.000 worth of freight of Chilean exports, distributed evenly among the participants (1.000 each). If all three ships are considered, the total value of freight would be 9.000.

1. -According to the orthodox approach, all exports on board the ship effectively operated by CSV would be attributed to Chile, and would therefore give rise to the following record in Chile's BOP:

	CREDITS	DEBITS		NET
Transportation-freight	3.000			3.000
Other transport		100	-	100
Banks		2.900		-2.900

Credits reflect freight on the ship operated by CSV (resident of Chile), and debits under transport would be the "commissions" paid by CSV to HL (50) and HS (50), for obtaining merchandise to be carried on the ship.

The trips of the remaining vessels participating in the joint service would be recorded as follows:

	CREDITS	DEBITS	NET
Transportation-freight			
Other transport	100		100
Banks		100	-100

No entries for freight would be made, as they would be transactions among non-residents (HL and HS, with the importers). 100 would be an export of services (the commissions received by CSV)

In this way, the records involving all three ships would be:

	CREDITS	DEBITS	NET
Transportation-freight	3.000		3.000
Other transport	100	100	
Banks		3.000	-3.000

Making these entries requires having data on the values and costs among participating entities. The fact that this information is practically impossible to collect explains the practical proposal.

2. -The suggested practical approach is to assign freight according to the residence of the issuer of the master B/L. This, for practical reasons, as it is easy to determine.

Accordingly, the entries derived from total exports carried on board the CSV ship would be:

	CREDITS	DEBITS	NET
Transportation-freight	1.000		1.000
Banks		3.000	-3.000
Errors and Omissions	2.000		2.000

Credits under freight (1.000) reflect transportation of CSV's own cargo (master B/Ls issued by CSV, equal to one third of the cargo of the ship). This would result in errors and omissions equal to the difference between 1.000 and the actual movement of the banking accounts.

This problem would be offset by entries related to shipments on the other vessels participating in the joint services.

For the same route, according to the terms of the joint services agreement, the ships operated by HL and HS also carry Chilean exports, and would generate master B/Ls issued by CSV equal to one third of each vessel's cargo. Thus, summing both voyages, additional credits worth 2.000 would be recorded under Transportation-freight in Chile's BOP.

	CREDITS	DEBITS	NET
Transportation-freight	2.000	2.000	
Errors and Omissions	2.000	-2.000	

The final result in BOP accounting would be similar, in net terms, to one in which there were no joint services agreement, and in which each company obtained all the revenues generated by the operation of its ship.

	CREDITS	DEBITS	NET
Transportation-freight	3.000		3.000
Banks		3.000	-3.000
Errors and Omissions			

This approach seems to clash with the recommendation of attributing freight to the operator of the ship. However, it may be interpreted as a case involving a special type of operator.