
Chapter 8. Other Changes in Financial Assets and Liabilities Account

A. Structure of the Account

8.1 This chapter will discuss the purpose and structure of the other changes in financial assets and liabilities account along the lines in the *1993 SNA* Chapter XII and *GFSM 2001* Chapter 10. It will state that this account captures changes in financial assets and liabilities that are not transactions, which are recorded in the financial account. The manual will propose that the scope of this account is determined by the scope of the international investment position, which includes only financial instruments. The manual will, however, note that events other than transactions occurring between residents and nonresidents may give rise to changes in holdings of nonfinancial nonproduced assets by residents (for example, the seizure of nonproduced intangible assets by nonresidents). The manual will propose that such information, particularly when important, should be provided as supplementary information. Information on changes in holdings of nonfinancial nonproduced assets due to other changes in volume of assets occurring between residents and nonresidents is necessary to prepare national balance sheets.

8.2 The manual will explain that other changes in assets and liabilities are genuine economic phenomena that should be recorded separately from transactions. These flows are not residual items but reflect economic realities. This section will contrast the flows recorded in this account with transactions recorded in other international accounts in terms of their economic nature and accounting entries. Two types of the other flows will be distinguished: (1) holding gains/losses (revaluations); and (2) other changes in volume of assets. Within the first category, the holding gains/losses due to exchange rate changes and price changes will be distinguished. Definitions of these concepts will be given. The relationship of this account with other international accounts as well as with the balance sheets of the national accounts will be discussed.

8.3 A table showing the structure and components of the other changes in financial assets and liabilities account with a numerical example will be presented. The table below shows only the main components, but the manual will provide a breakdown, along the lines of Table 5.3 in Chapter 5 Classifications. Full standard components will be presented in an appendix.

TABLE 8.1. Overview of Other Changes in Financial Assets and Liabilities Account

	Holding gains/losses		Other changes in volume
	Exchange rate changes	Other price changes	
<i>Net changes in financial assets arising from other flows</i>			
Direct investment			
Portfolio investment			
Financial derivatives and employee stock options			
Other investment			
Reserve assets			
Total net changes in financial assets resulting from other flows			
Of which:			
Equity finance			
Debt instruments			
Other instruments			
<i>Net changes in liabilities arising from other changes</i>			
Direct investment			
Portfolio investment			
Financial derivatives and employee stock options			
Other investment			
Total net changes in liabilities resulting from other flows			
Of which:			
Equity finance			
Debt instruments			
Other instruments			
<i>Changes in net IIP</i>			

B. Scope and Characteristics

1. Holding gains/losses

8.4 This section will define holding gains and losses. It will state that holding gains and losses in the international accounts apply only to financial assets and liabilities. The notions of realized and unrealized holding gains will be explained. The manual will note that changes in the value of assets arising from a change in quantity of a financial asset are transactions

OTHER CHANGES IN FINANCIAL ASSETS AND LIABILITIES ACCOUNT

but are not holding gains/losses, and it will give examples of such cases (e.g., the accrual of interest). The meaning of nominal holding gains will be discussed. The manual will state that unless specifically mentioned, the term “holding gains” refers to nominal holding gains and losses. The holding gains owing to exchange rate changes and price changes will be defined. It will be stated that such a separation is applicable only to financial instruments denominated in a foreign currency. It will mention that the *1993 SNA* classifies nominal holding gains further into neutral and real holding gains.

8.5 There will be separate paragraphs discussing holding gains for specific types of assets. The following particular cases may be distinguished and discussed:

- (a) Currency and deposits. The manual will state that monetary values of currency denominated in the currency used for the international accounts remain constant over time; hence, holding gains on these assets are always zero (along the lines of the *1993 SNA* para. 12.107). Assets denominated in another currency can change in value, owing to a change in exchange rate which is recorded as holding gains. The manual will explain that using different currencies to compile international accounts will have effects on this account, because changes in values resulting from exchange rate changes are holding gains/losses. For deposits, an issue is raised in Chapter 3 Accounting Principles about whether nominal and fair values should be followed. Based on the decision on this question, the manual will describe the issue of holding gains for deposits.
- (b) Write-off and write-down of loans. The manual will discuss the treatment of write-off and write-down of loans, and loans sold at discount, including loans that are traded but not sufficiently to become securities. The treatment of these items is not fully clear in various macroeconomic statistics manuals. According to the *1993 SNA* (para. 11.23), writing-off of debts (recognition by a creditor that a financial claim can no longer be collected owing to bankruptcy or other factors) is recorded in the other changes in volume of asset accounts for both the creditor and the debtor. Write-downs that reflect actual market values should be accounted for in the revaluation account. Write-offs or write-downs that are imposed solely to meet regulatory or supervisory requirements and do not reflect the actual market values of those financial assets should not be recorded (*1993 SNA*, para. 11.23). The *BPM5* mentions write-offs as changes resulting from the unwillingness or inability of a debtor to make full or partial repayment (para. 310). However, it states only that these write-offs are not transactions, without discussing whether they are revaluation or other changes in volume. The *MFSM* states that the value of a loan portfolio should be adjusted downward only when (1) loans are actually written off as uncollectible, or (2) the outstanding amount of the loan has been reduced through a formal debt reorganization (para. 206). These issues are also related to the issue of valuation of nontraded financial instruments (nominal or fair values), as raised in Chapter 3 Accounting Principles and in Chapter 6 International Investment Position. Clarification on the above issues will be given in the new manual.

- (c) Loans sold at discount, including loans that are traded but not sufficiently to become securities. The *1993 SNA*'s treatment for loans subject to discounts as stated in para. 14.51, is also suggested in the *BPM5*, para. 471 (market value on the creditor's side and nominal value on the debtor's side). However, it is not consistent with the overall concept of symmetric recording. If the nominal value is used for positions, the difference between nominal and transaction values will be shown as a valuation change. This issue will be discussed fully in Chapter 3 Accounting Principles, with a cross-reference in this chapter.
- (d) Debt reorganizations. The manual will explain debt rescheduling, debt refinancing, debt assumption, and debt swaps (debt-debt swap and debt-equity swap).
- (e) Accrual of interest on debt instruments. The manual will describe changes in the value of debt securities resulting from change in their quantity from the accrual of interest. It will state that these changes are not holding gains. (Cross-references will be made to Chapters 3, 5, 6, and 7).
- (f) Debt securities. The manual will discuss holding gains on debt securities as the change in their value owing to interest rate changes that reflect, among other things, changes in credit ratings. The treatment of foreign currency-denominated securities and index-linked securities will be discussed. In the case of debt instruments denominated in a foreign currency, the current recommendation is to classify changes in the value of the principal in domestic currency terms that arise from exchange rate variations as holding gains (nontransactions). However, in the case of debt instruments indexed to a foreign currency, such changes are treated as interest (transactions). The manual will recommend that for debt instruments with both principal and coupons indexed to a foreign currency, the change in principal in domestic currency terms that arises from a change in the exchange rate should be shown as a revaluation, and the effect of changes in the exchange rate on the amount of accrued interest expressed in domestic currency is to be included in interest.
- (g) Financial derivatives and employee stock options. The manual will describe holding gains/losses on financial derivatives based on para. FD14 of the *BPM5 Supplement*. Holding gains and losses on employee stock options will be discussed.
- (h) Equity finance. The manual will discuss holding gains on shares and holding gains on equity of quasi-corporations, including the equity of a notional unit owning immovable assets such as land and buildings.
- (i) Insurance technical reserves and equity on pension funds. The manual will discuss holding gains on these assets/liabilities.

OTHER CHANGES IN FINANCIAL ASSETS AND LIABILITIES ACCOUNT

2. Other changes in volume of assets

8.6 This section will define other changes in the volume of assets. The *BPM5* shows other changes in the volume of financial assets and liabilities only. The new manual will note that changes in nonfinancial nonproduced assets arising from transactions with nonresidents enter into the national balance sheets through the capital account. The changes in the resident holdings of nonfinancial nonproduced assets resulting from events, occurring between residents and nonresidents, other than transactions are to be classified as other changes in the volume of assets. The manual will propose that the scope of this account be limited to the scope of the IIP, which includes only financial instruments. However, it will recommend that supplementary information on nonproduced nonfinancial assets be prepared where it is considered to be significant or analytically useful.

8.7 The manual will describe events that give rise to the recording of other changes in the volume of assets in the international accounts. These events will be divided into three broad categories:

- (a) Catastrophic losses and uncompensated seizures. The events that are to be classified under this category will be described. Changes in sovereignty over areas occurring involuntarily (such as arising from a war) will be noted as other changes in the volume of assets (BOPCOM-02/59).
- (b) Changes in classifications. This category will cover (i) changes in classification of assets and liabilities [for example, classification between direct and portfolio investment, monetization and demonetization of monetary gold, etc.], (ii) changes in sector classification and structure, and (iii) changes in residence of individuals/households. In view of importance of changes in financial claims and liabilities owing to changes in residence of individuals for assessing mode 4 delivery of services in the context of the General Agreement on Trade in Services (GATS), the manual will explore whether supplementary information on them is desirable.

[Question: Is supplementary information on changes in financial claims and liabilities owing to changes in residence of individual desirable?]

- (c) Other volume changes. This category will mention (i) allocation and cancellation of SDRs, (ii) shutdown of a direct investment enterprise, including enterprises set up for natural resources exploration, and (iii) miscellaneous other volume changes.

C. Timing

8.8 The section will describe the time of recording for holding gains and other volume changes in assets and liabilities.

D. Valuation Principles

8.9 The section will discuss general valuation principles applicable to holding gains and other volume changes in assets and liabilities.

OTHER CHANGES IN FINANCIAL ASSETS AND LIABILITIES ACCOUNT

References

BPM5 chapters 2 and 23;

1993 *SNA* chapter XII;

GFSM chapter 10;

MFSM chapter V;

IMF, *Clarification of Foreign Direct Investment Recommendations*, BOPCOM-01/20A; and

IMF, *Residence* (BOPCOM-02/59).

Changes from *BPM5*

(a) *Changes proposed:*

Limit Other Changes in Financial Assets and Liabilities Account to the scope of IIP, which includes only financial instruments (para. 8.1).

For debt instruments with both principal and coupons indexed to a foreign currency, the change in principal in domestic currency terms that arises from a change in the exchange rate represents a revaluation (para. 8.5(a)).

Treat “migrants’ transfers” as “other changes in financial assets/liabilities,” instead of as a capital account transaction (para. 8.7(b)).

(b) *Changes raised as an option:*

Provide supplementary information on changes in holdings of nonfinancial nonproduced assets owing to other changes in volume of assets occurring between residents and nonresidents, where significant (para. 8.1).

Clarification on the treatment of write-off and write-down of loans, and loans sold at discount, including loans that are traded but not sufficiently to become securities (para. 8.5(b)).

Whether supplementary information is desirable on changes in financial claims and liabilities arising from changes in residence of individual (para. 8.7(b)).

Glossary

Holding gains

Other changes in volume of assets

Debt rescheduling
Debt refinancing
Debt assumption
Debt swaps
Debt-debt swap
Debt-equity swap
Catastrophic losses
Uncompensated seizures
Changes in classification of assets and liabilities
Changes in sector classification and structure
Changes in residence of individuals/households