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User Guide: Canadian System of Macroeconomic Accounts

Chapter 8 International Accounts

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This publication contains nine chapters to reflect the most of the macroeconomic accounts. Some chapters (1, 2, 3, 4, 6, 7 and 9) were updated on February 22, 2021 to fix some references. For more information on Satellite accounts and Natural resource accounts, please refer to Canadian System of Macroeconomic Accounts (13-607-X).

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An HTML version is also available.

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Chapter 8 International accounts

What this chapter seeks to do

The purpose of this chapter is to explain Canada's **international accounts**. These accounts provide a comprehensive statistical picture of Canada's economic relationships with non-residents. The chapter focuses on the internal structure of the balance of international payments and international investment position, the relationship of these accounts to the rest of the Canadian system of macroeconomic accounts and how these accounts are used to interpret economic developments.

This chapter links primarily to *System of National Accounts (SNA) 2008* Chapter 26 and to the *Balance of Payments and International Investment Position Manual, sixth edition (BPM6)*.

8.1 Introduction

Canada's economy is wide open to the rest of the world. Canadian households, corporations and governments engage in a variety of transactions with economic actors in other countries every day of the year. Over time Canadians have also accumulated large stocks of assets and liabilities in other parts of the world, as have non-residents in Canada. The international accounts keep track of these transactions with non-residents and the stocks of financial assets and liabilities that are associated with them.

Text box 8.1 highlights the wide variety of transaction types that are involved in Canada's economic relationship with the rest of the world. These different kinds of international transactions are the subject of later sections in this chapter.

Text box 8.1
Types of international transactions

- Exports and imports of goods (wheat, cars, oil and gas, etcetera)
- Exports and imports of services (travel, transportation, financial, etcetera)
- Compensation of employees working across the border
- Dividend, interest and other investment income flows, by type, across the border
- Current transfers across the border, such as foreign aid and personal transfers
- Capital transfers across the border, such as government forgiveness of foreign debts
- Direct investment flows, by type, across the border
- Portfolio investment flows, by type, across the border
- Other investment flows across the border
- Official international reserve flows

The international accounts are the central guide to and a vital framework for the analysis of Canada's cross-border trade and investment patterns, exchange rate policy, official reserves management, external financial exposure and many other economic issues. They are compiled according to the standards set out in the *Balance of Payments and International Investment Position Manual, sixth edition (BPM6),* which is the responsibility of the International Monetary Fund and was developed in close cooperation with balance of international payments experts from countries all over the world, participating in the International Monetary Fund Committee on Balance of Payments Statistics.[1]

8.2 The framework for the international accounts

8.2.1 Residence

The international accounts record information about transactions between **residents** and **non-residents**. The concept of residence was discussed in Chapter 3, section 3.2.4. As mentioned there, the residence of an institutional unit is defined in *BPM6* as "the economic territory with which it has the strongest connection, expressed as its centre of predominant economic interest".

As a practical matter residence is established for households on a calendar year basis. There are a number of special cases. Students and their spouses and children who go outside their home country to study remain residents of their home country. Similarly, patients who leave their country for the purpose of medical treatment maintain their original country of residence. The crews of ships, oil rigs, aircraft and the like are treated as resident in their home base territory. Diplomats, military personnel, staff of scientific research stations and other civil servants employed abroad in government enclaves are also considered to reside in their original economic territory, although locally recruited employees are resident in the country where their principal dwelling is located. Cross-border workers, seasonal employees and other temporary workers crossing the border are considered to reside in their country of principal residence rather than the country where they are employed.

According to *BPM6*, "an enterprise is resident in an economic territory when the enterprise is engaged in a significant amount of production of goods or services from a location in the territory." In practice this means the enterprise is resident in the country to whose laws it is mostly subject. Corporations that deliver goods or services from a base country to one or more other countries are considered to reside in the base country. An example would be a corporation that supplies equipment repair services in the U.S. from a home base in Canada. However, if the external operations of a construction company are substantial, a branch of the company may be defined that is resident in the country of operations.

8.2.2 International accounts structure

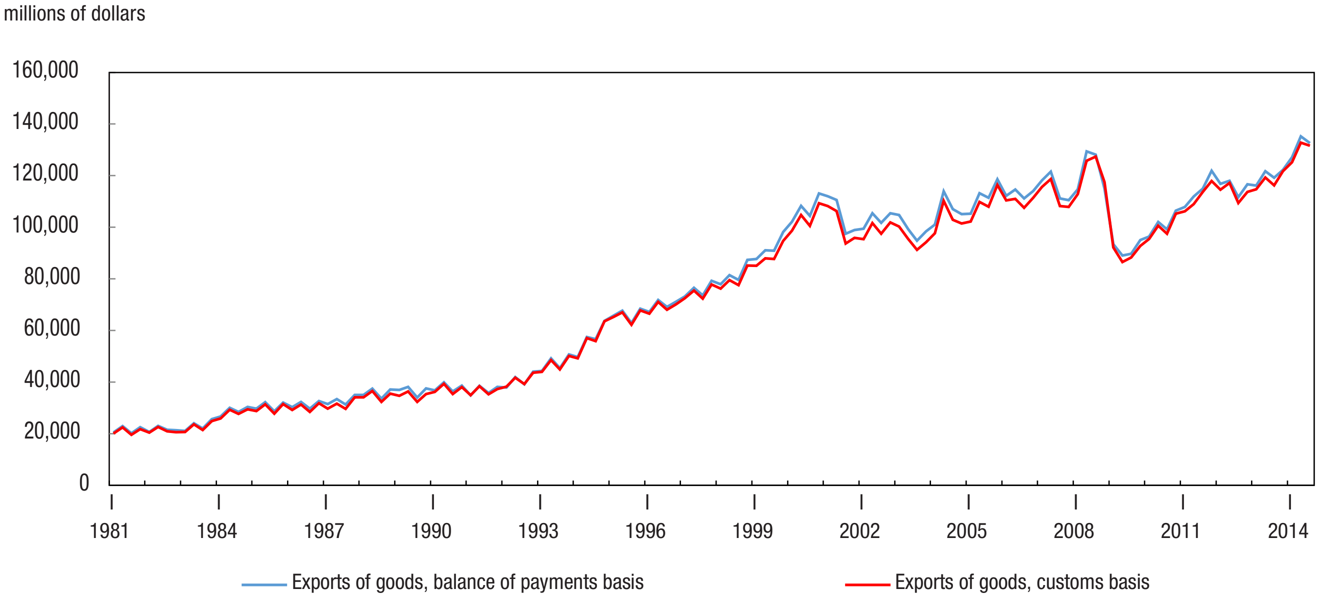
Earlier chapters in this volume have presented the SNA 2008 framework as a sequence of institutional accounts comprising six sectors:

- Households,
- Non-profit institutions serving households,
- Non-financial corporations,
- Financial corporations,
- Governments, and
- Non-residents.

The international accounts are fully consistent with this framework. If the first five of the above institutional sectors are consolidated, forming the resident sector of the Canadian economy, then the accounts discussed in this chapter can be thought of as depicting the relationship between the resident sector and non-resident sector. Note, however, that the international accounts should **not** be thought of as the non-resident sector accounts, since they are not presented from the non-resident sector's point of view. Rather, they should be seen as the resident sector's accounts vis-à-vis non-residents. They are, in effect, the mirror image of the non-resident sector accounts that are discussed in chapters 3, 5 and 6.

The Canadian international accounts are compiled in two broad sets of statistics: the balance of international payments (BOP) that aggregates all transactions between Canadian residents and non-residents and the international investment position (IIP) that presents the stocks of foreign financial assets and liabilities held by Canadian residents. These accounts can be viewed as an aggregated set of each resident sector's transactions and positions (see Figure 8.1). At the moment, only the aggregate BOP and IIP are released, with limited sectoral detail, although work is ongoing to develop such detail. The focus in the international accounts has traditionally been on the international geographical dimension, rather than on the sectoral breakdown of international transactions and stocks

Chart 8.1
Exports on a customs basis versus a balance of payments basis



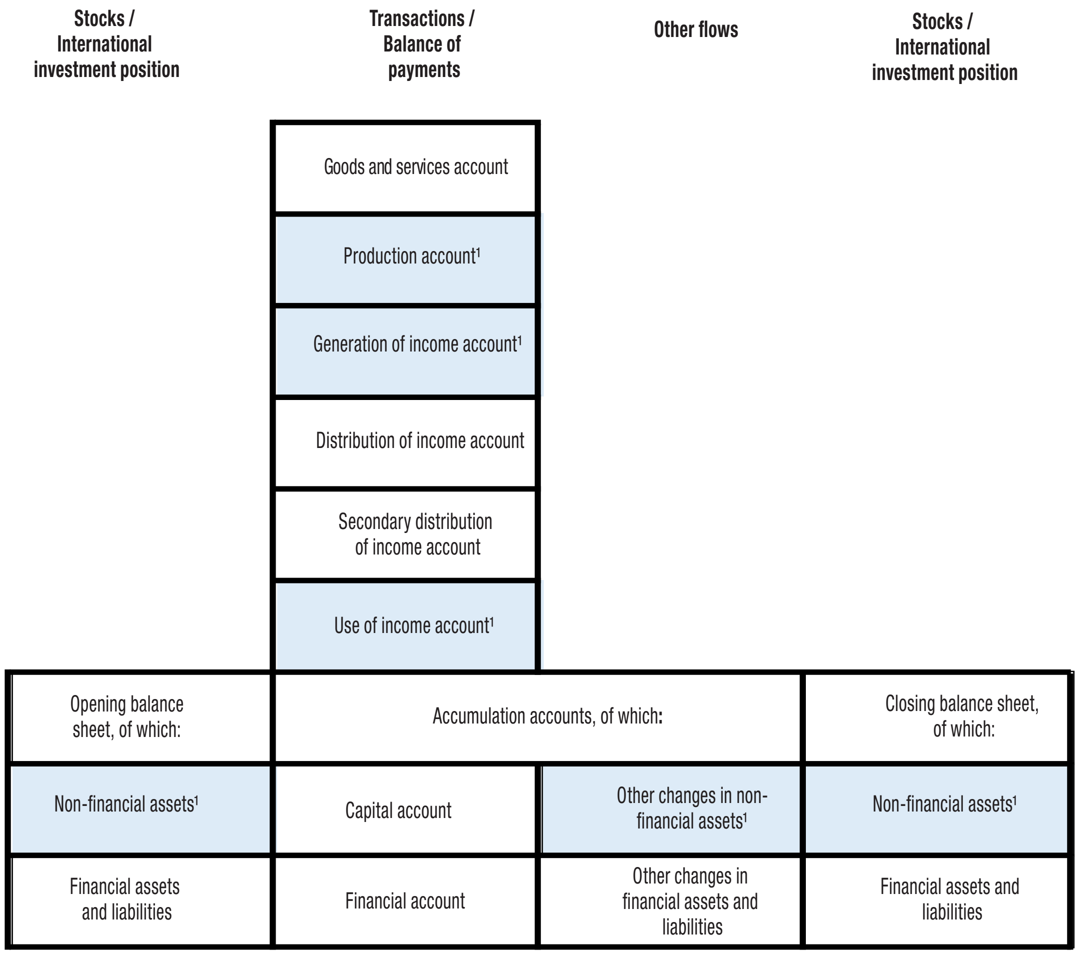
Source: Statistics Canada, *User Guide: Canadian System of Macroeconomic Accounts (13-606-G)*.

The inverted international accounts are defined as the non-resident sector in the context of the income and expenditure accounts (Chapter 5), the financial flow accounts and the balance sheet accounts (Chapter 6) in order to be able to produce a complete and closed set of accounts. Each of the other five sectors' accounts records transactions and related positions with the sixth sector, the non-residents sector, which is a mirror image of the international accounts. In effect, the foreign assets recorded in the international accounts (investment abroad) become non-resident sector liabilities in the national accounts and Canadian foreign liabilities become non-resident sector assets (investment in Canada) in those accounts.

8.2.2.1 The international accounting framework in words

Figure 3.1 in Chapter 3 provides a schematic depiction of the framework for Canada's macroeconomic accounts. That same framework applies to the international accounts, except that the framework is simpler due to the fact that, under the concepts and conventions of *SNA 2008* and *BPM6*, the non-resident sector is a non-producing sector and does not engage in capital formation within the context of the Canadian economy. It does not have 'production', 'generation of income' or 'use of income' accounts. The primary income account records transactions of institutional units in their capacity as recipients of primary incomes rather than as producers whose activities generate primary incomes. It also shows the property incomes receivable and payable by institutional units. The framework also does not record non-financial assets in the international investment position. Figure 8.2 depicts the framework for the international accounts within the broader context of the framework for *SNA 2008* as a whole.

Figure 8.2
***System of National Accounts 2008* framework including international accounts**



1. Account does not appear in the international accounts.
Source: Adapted by Statistics Canada from figure 2.1 in *Balance of Payments and International Investment Position Manual, 6th, Edition.*

8.2.2.1.1 The current account

The **current account** of the balance of international payments records non-capital, non-financial transactions of all kinds between the overall resident sector and non-resident sector. Transactions are recorded in both directions, as receipts and payments, and the difference between the two is the **current account balance**. The account has three component accounts:

- the **goods and services account**, recording international trade transactions in goods and services;
- the **primary income account**, logging cross-border income flows such as compensation of employees working outside their own economy and dividends and interest payments between resident and non-resident creditors and debtors; and
- the **secondary income account** setting out current transfer flows between countries such as government foreign aid and personal remittances between family members in different countries.

It can be easily shown (see section 8.2.2.2) that Canada's **current account balance**—the difference between receipts and payments on each of the above three component accounts combined—is equal to the difference between national saving and investment. In other words, when Canadians save more than they invest the current account balance is positive, signifying that the 'excess' savings are being invested abroad, and when they invest more than they save the current account balance is negative, indicating that Canada is borrowing on a net basis from other countries. Canada has had a substantial current account negative balance (or current account deficit) for much of its history,[2] reflecting the need for its relatively young and expanding economy to finance part of its investment abroad.

8.2.2.1.2 The capital account

The **capital account** records capital transfers between economies, such as debt forgiveness, foreign capital assistance and unusually large cross-border non-life insurance claims. In Canada, the acquisition and disposal of non-produced non-financial assets between residents and non-residents are also included in this account. The receipts, payments and balance in the capital account are typically quite small in Canada's case, compared to the current account.

The sum of the balances in the current and capital accounts is **net lending or borrowing** by the resident sector to/from the non-resident sector.

8.2.2.1.3 The financial account

The **financial account** records financial transactions that mirror the transactions shown in the current account. Thus, for example, when Canada exports goods worth $10 million, which would be recorded in the goods and services account, it might receive payment by cheque, deposited in a bank account. That $10 million acquisition of financial assets would be reported in the financial account. The sum of all such net transactions in financial assets less the net incurrence of liabilities is the financial account balance, which is also equal, in concept, to net lending or borrowing.[3] Accordingly, the statistics in the international accounts yield two estimates of net lending or borrowing which should be, but in fact virtually never are, exactly equal. The difference between the two is shown explicitly and is termed the BOP **net errors and omissions**.

These net errors and omissions occur because imperfect data from a variety of sources are used to compile the balance of international payments estimates, each source having its particular strengths and weaknesses. The estimates are almost always subject to a variety of types of error. The aggregate of the errors in all the different components of the account—with many of those errors tending to offset—is captured in net errors and omissions. When large, net errors and omissions provides international accounts compilers with a signal about the quality of the source data and causes them to investigate, make changes and invest in improvements to the statistical program.

8.2.2.1.4 The other changes in financial assets and liabilities account

In addition to the current, capital and financial accounts just mentioned, there is one more that is called the **other changes in financial assets and liabilities account**. This account records changes to the value of residents' financial assets and liabilities abroad that are **attributable to factors other than transactions**. For example, when households change their economy of residence, the appearance (in their new economy) or disappearance (in their old economy) of their assets and liabilities is recorded in this account. Certain valuation changes also are recorded in this account. For example, the value of resident liabilities might rise if a Canadian energy company in which non-residents owned equity discovered new oil and gas reserves. The equity value of the non-resident holdings might rise simply because those holdings gained an increased valuation in the stock market. As another example, the Canadian-dollar-value of Canadian-held assets in the U.S. might rise due to an increase in the value of the U.S. dollar relative to the Canadian dollar.

For example, suppose a Canadian resident purchased an equity stake in a U.S. corporation on the New York Stock Exchange in the third quarter of 2012 in the form of 1000 shares each trading at US$50.00, representing a total value of US$50,000.00. Given the 1.0054 exchange rate at the time, this investment was equivalent to CAN$49,733.59. Two years later the Canadian resident still owned the stock but the equity price had risen on the market from $50 per share to $60 per share and the exchange rate had decreased to 0.7640. The investment was then worth US$60,000 or CAN$78,534.72. In this example, the other changes in financial assets and liabilities account would record an appreciation of CAN$28,801.13 on this asset over the two-year period.

8.2.2.1.5 The international investment position

The sequence of international accounts begins with the opening balances in the international investment position, which record the stocks of assets and liabilities held by residents vis-à-vis non-residents. Then the current account and the capital accounts determine resident sector saving and net lending or borrowing vis-à-vis non-residents. The financial account records international transactions in financial assets and liabilities, also yielding net lending or borrowing. The difference between the two, as noted previously, is net errors and omissions. The other changes in financial assets and liabilities account then determines changes in financial assets and liabilities held by residents vis-à-vis non-residents that are not directly linked to transactions. Finally, the closing balances are determined in the international investment position account by adding all the financial transactions (or, at the aggregated level, the net lending or borrowing) and other changes in financial assets and liabilities to the opening balances.

8.2.2.2 The international accounting framework – a mathematical representation

This section provides a mathematical representation of the framework of the international accounts. The following symbols, pertaining to the consolidated resident sector of the economy, are employed:

Table 8.1
Symbols pertaining to the consolidated resident sector of the economy[1]

Symbol	Definition
C	Consumption expenditure by households
CAB	Current account balance
FAA	Net transactions in financial assets
FAL	Net transactions in liabilities
G	Consumption expenditure by governments
GDP	Gross domestic product
GNDI	Gross national disposable income
GNI	Gross national income
I	Gross domestic investment
IIPA	International investment position assets
IIPL	International investment position liabilities
KAB	Capital account balance
KTP	Capital transfer payments
KTR	Capital transfer receipts
M	Imports of goods and services
NEO	Net errors and omissions
NFI	Net financial investment
NIIP	Net international investment position
NIIPE	Net international investment position at end of period
NIIPS	Net international investment position at start of period
NLB	Net lending or borrowing
NNW	National net worth
NP	Consumption expenditure by non-profit institutions serving households
NPNFAP	Non-produced non-financial asset payments
NPNFAR	Non-produced non-financial asset receipts
NW	National wealth, the economy's total non-financial assets
OCFAL	Other changes in financial assets and liabilities
PIP	Primary income payments
PIR	Primary income receipts
S	Gross national saving
SIP	Secondary income payments
SIR	Secondary income receipts
X	Exports of goods and services

1. For the interrelationships among these terms, see the equations in the text.

Source: Statistics Canada, *User Guide: Canadian System of Macroeconomic Accounts*, 2017.

8.2.2.2.1 Current account balance and gross national disposable income

In Canada the current account balance is an important part of Canada's gross national disposable income. Parts of it also enter into gross domestic product and gross national income. This is illustrated below though accounting identities linking the CAB to GNDI.

First, the current account balance is defined by equation (8.1).

(8.1)

$$CAB \equiv (X - M) + (PIR - PIP) + (SIR - SIP)$$

Gross domestic product is defined by equation (8.2), gross national income by equation (8.3) and gross national disposable income by equation (8.4).

(8.2)

$$GDP \equiv C + NP + G + I + X - M$$

(8.3)

$$GNI \equiv GDP + (PIR - PIP)$$

(8.4)

$$GNDI \equiv GNI + (SIR - SIP) = CAB + C + NP + G + I$$

In other words, the X–M part of the current account balance enters directly into the calculation of GDP, this portion plus the PIR–PIP part both enter into GNI and the entire current account balance is part of GNDI.

8.2.2.2.2 Current account balance, saving and investment

Gross national saving net of gross investment is equal to the current account balance. In other words, any excess of national saving vis-à-vis investment is reflected in a positive current account balance and any deficiency in national saving relative to investment implies a negative current account balance. This is shown in the identities below.

Gross national saving is defined by equation (8.5).

(8.5)

$$S \equiv GNDI - C - NP - G$$

Substituting equation (8.4) into equation (8.5) yields equation (8.6).

(8.6)

$$S=GNI+(SIR-SIP)-C-NP-G$$

Substituting equation (8.3) into equation (8.6) yields equation (8.7).

(8.7)

$$S=GDP+(PIR-PIP)+(SIR-SIP)-C-NP-G$$

Substituting equation (8.2) into equation (8.7) yields equation (8.8).

(8.8)

$$S=C+NP+G+I+(X-M)+(PIR-PIP)+(SIR-SIP)-C-NP-G$$

Cancelling terms and substituting from equation (8.1) yields equation (8.9), underlining the fact that the current account balance brings gross domestic investment and gross national saving into balance.

(8.9)

$$S=I+CAB$$

Finally, rearranging terms in equation (8.9) yields equation (8.10), showing that the difference between gross national saving and gross investment expenditure is the current account balance.

(8.10)

$$CAB=S-I$$

8.2.2.2.3 Current account balance and net worth

The current account balance also, in combination with the capital account balance, determines net lending or borrowing which in turn contributes to the explanation of changes in the international investment position and net national worth. This is shown in the identities below.

The capital account balance is defined by equation (8.11).

(8.11)

$$KAB\equiv(KTR-KTP)+(NPNFAR-NPNFAP)$$

Net lending or borrowing is defined by equation (8.12), and also on the financial accounts side by equation (8.13).

(8.12)

$$NLB \equiv CAB + KAB$$

(8.13)

$$NFI \equiv FAA - FAL$$

These two balances are equated via the net errors and omissions (8.14).

(8.14)

$$NFI = NLB + NEO$$

Finally, it is essential to link the flows and stocks. The net international investment position in any period is calculated as in equation (8.15).

(8.15)

$$NIIP = IIPA - IIPL$$

More interesting is the change in NIIP, which is closely related to NLB. At the end of an accounting period NIIP is determined by equation (8.16).

(8.16)

$$NIIPE = NIIPS + NFI + OCFAL$$

This can be re-written as (8.17)

(8.17)

$$NIIPE = NIIPS + NLB + NEO + OCFAL$$

The NIIP is also essential in determining national net worth from national wealth on the aggregate national balance sheet of the national balance sheet accounts (Chapter 6). The derivation is shown in equation (8.18).

(8.18)

$$NNW = NW + NIIP$$

8.3 The current account

8.3.1 The goods and services account

The goods and services account records transactions in goods and services between residents and non-residents that are the result of production activities. The largest categories of receipts and payments in the current account, by far, are those for exchanges of goods and services. As shown in Table 8.2, total receipts of goods were $367,211 million and those of services were $78,481 million in 2009 while payments were $373,985 million and $94,853 million respectively.

Table 8.2
Balance of international payments, current, capital and financial accounts, 2009

	2009
	millions of dollars
Current account receipts	...
Goods and services	445,692
Goods	367,211
Services	78,481
Primary income	56,266
Compensation of employees	1,361
Investment income	54,904
Direct investment income	29,029
Portfolio investment income	19,888
Other investment income	5,986
Secondary income	9,051
Private transfers	3,474
Government transfers	5,577
Total current account receipts	511,009
Current account payments	...
Goods and services	468,837
Goods	373,985
Services	94,853
Primary income	75,826
Compensation of employees	2,878
Investment income	72,949
Direct investment income	30,653
Portfolio investment income	34,539
Other investment income	7,757
Secondary income	12,536
Private transfers	8,007
Government transfers	4,528
Total current account payments	557,199
Current account balances	...
Goods and services	-23,146
Goods	-6,774
Services	-16,371
Primary income	-19,561
Compensation of employees	-1,515
Investment income	-18,044
Direct investment income	-1,623
Portfolio investment income	-14,650
Other investment income	-1,772
Secondary income	-3,484

Table 8.2
Balance of international payments, current, capital and financial accounts, 2009

	2009
	millions of dollars
Private transfers	-4,533
Government transfers	1,050
Total current account balance	-46,190
Capital account	...
Receipts	248
Payments	1,066
Capital account balance	-819
Net lending / net borrowing from current and capital accounts	-47,009
Financial account	...
Net acquisition of financial assets	97,624
Direct investment assets	42,769
Canadian portfolio investment	8,733
Foreign debt securities	-7,186
Foreign equity and investment fund shares	15,919
Official international reserves	11,618
Other Canadian investment	34,504
Loans	17,481
Currency and deposits	17,946
Other accounts receivable	-667
Net incurrence of liabilities	145,189
Direct investment liabilities	23,448
Foreign portfolio investment	112,727
Canadian debt securities	86,481
Canadian equity and investment fund shares	26,246
Other foreign investment	9,014
Loans	-11,989
Currency and deposits	13,185
Special drawing rights	8,825
Other accounts payable	-419
Net lending / net borrowing from financial account	-47,565
Discrepancy (net errors and omissions)	-556

... not applicable

Source: Statistics Canada, tables 36-10-0471-01 and 36-10-0016-01.

The valuation of goods in this account includes transportation costs within the exporting economy plus retail and wholesale margins that are not separately distinguishable in the price of the goods. In other words, 'Free on board' (FOB) valuation principles, as described in earlier chapters, apply. In addition, as will be explained below, the value of some services, as they are defined, includes the value of some goods, such as in the cases of travel, construction and government services. For transactions in goods and services between affiliated enterprises there can be special valuation difficulties because of transfer pricing.

As with transaction entries in all of the component accounts in the current account, there are entries in other accounts that correspond to those in the goods and services account. For example, if an export flow is paid for in currency, there is a corresponding 'currency and deposits' entry in the financial account. If the export flow is foreign aid in kind, the corresponding entries are under 'current transfers' or 'capital transfers'.

8.3.1.1 The goods account

The goods account of the balance of international payments is fundamentally based on merchandise trade statistics, which measure the cross border physical flow of merchandise. However, trade in goods differs from merchandise trade in a number of ways that will be discussed below. Perhaps most importantly international trade in goods follows the principle of ownership change as opposed to the concept of physical flow in the merchandise trade statistics.

Table 8.3 shows trade in goods, by product category, on a balance of international payments basis, for the year 2009. The product classes are those of the North American Product Classification System (NAPCS). Canada had a trade deficit of $6,774 million that year, reflecting relatively large deficits in consumer goods, electronic and electrical equipment and parts, and motor vehicles and parts combined with notable surpluses in energy products and forestry products and building and packaging materials. Total trade that year (exports plus imports) was $741,195 million. This was equivalent to 47% of gross domestic product, illustrating how important goods trade is to Canada's economy.

Table 8.3
Exports and imports of goods, 2009

	2009		
	Exports	Imports	Balance
	millions of dollars		
Total of all merchandise	**367,211**	**373,985**	**-6,774**
Farm, fishing and intermediate food products	20,331	11,019	9,312
Energy products	74,369	32,242	42,126
Metal ores and non-metallic minerals	12,573	6,636	5,937
Metal and non-metallic mineral products	37,832	30,482	7,350
Basic and industrial chemical, plastic and rubber products	26,284	26,882	-598
Forestry products and building and packaging materials	27,488	16,302	11,187
Industrial machinery, equipment and parts	23,625	33,307	-9,682
Electronic and electrical equipment and parts	24,146	46,905	-22,758
Motor vehicles and parts	44,227	58,175	-13,948
Aircraft and other transportation equipment and parts	17,746	13,713	4,034
Consumer goods	47,696	86,101	-38,405
Special transactions trade	4,739	4,489	249
Other balance of payments adjustments	6,156	7,732	-1,575

Source: Statistics Canada, table 36-10-0110-01. Based on the North American Product Classification System.

Most Canadian statistics on trade in goods originate in Canadian Customs administrative records. This is true for imports of goods and also for exports of goods to countries other than the U.S. For trade with the U.S. the two countries have agreed, since 1990, each to use the other's detailed trade data for imports as its measure of exports. This is explained in the following paragraph:

> "In July 1987 Canada and the United States embarked upon a grand experiment by signing a Memorandum of Understanding (MOU) to exchange import statistics starting with January 1990 data. From this date, the two statistical agencies would no longer base their bilateral export statistics on export declarations. Instead, they would rely on the import statistics of the counterpart country. Statistics Canada relies on American imports from Canada as compiled by the U.S. Census Bureau as the source of its export data. Likewise, the U.S. Census Bureau derives its exports to Canada from data on imports from the United States compiled by Statistics Canada. Because of the greater scrutiny paid to imports by the Customs agencies in both countries, this exchange provides a more reliable measure of the bilateral trade. In addition, the reporting burden on exporters and forwarders in both countries was significantly reduced, as export declarations are no longer required for trade between the two partners. It was one of the first agreements between trading nations relating strictly to trade statistics."[4]

BPM6 includes a long list of items that are specifically included or excluded in the concept of trade in goods. The list is summarized in Table 8.4.

Table 8.4
Merchandise trade inclusions and exclusions

Some specific inclusions	
1	Bank notes and coins not in current circulation and unissued securities. They are to be valued as commodities rather than at face value.
2	Electricity, gas and water (however, charges invoiced separately for the transmission, transport or distribution of these products are included in services).
3	Products such as packaged software and video and audio recordings that are purchased outright (that is, not through end-user or other licenses) if provided on disk, CD-ROM or other magnetic media. These products are valued at their full transaction value. If the products are downloaded online they would be included in trade in services (downloading computer software would be an import of computer services).
4	Goods supplied or acquired by carriers away from the territory of residence of the operator (for example, a Canadian ship catching fish outside of Canada's economic territory and selling them abroad would be an export).

Table 8.4
Merchandise trade inclusions and exclusions

Some specific inclusions	
5	Goods acquired by a lessee under a financial lease.
6	Goods sent abroad without a change in ownership, but later sold. Goods sent abroad on consignment or for storage, repair, exhibition or processing without a change in ownership are not recorded at the time they are sent abroad, but if they are later sold to a resident of an economy different from that of the owner, they should be treated as goods exports or imports.
7	Equipment that is bought/sold while outside the territory of residence of new/original owner.
8	Trade in illegal goods.
9	Smuggled goods that are otherwise legal.
10	Goods exempted from Customs procedures (for example, shuttle trade, acquisition of ships or aircraft and trade between free trade zones and non-residents).
11	Gifts and parcel post.
12	Goods lost or destroyed after ownership has been acquired by an importer but before the goods have crossed a frontier.
13	Government sales of goods to and purchases of goods from non-residents.
14	Humanitarian aid in the form of goods.
Some specific exclusions	
1	Transit trade (goods passing through an economic territory).
2	Migrants' personal effects (individuals changing residency from one economic territory to another).
3	Goods consigned to embassies, military bases, etcetera from their home authorities and vice versa (for example, armoured personal carriers moved to a military base in Afghanistan).
4	Goods temporarily exported or imported without a change of ownership, such as goods for repair, as part of an operational lease, for storage and animals or artifacts for participation in exhibitions or competitions (such as the circus).
5	Goods with no positive value.
6	Returned goods.
7	Samples of no commercial value.
8	Trade in goods between free trade zones and residents of the same economy.
9	Goods acquired by a lessor under a financial lease.
10	Goods temporarily exported or imported with a change in ownership (for example, goods for repair, artifacts for participating in exhibitions or competitions).
11	Goods that are included in travel services.
12	Goods acquired by persons undertaking study or medical treatment.
13	Goods that are acquired by border, seasonal, and other short-term workers.
14	Goods that are acquired by diplomats, consular staff, military personnel.
15	Goods locally acquired for construction undertaken by non-resident enterprises (construction services).
16	Customized devices (for example, disks which belong in computer services).
17	Products (for example, packaged software, video and audio recording) under a fixed-period license to use (services).
18	Licenses to reproduce or distribute audio and video that are conveyed by supply of the original recording (services).
19	Customized blueprints and non-bulk newspapers and periodicals (services).

Source: *Balance of Payments and International Investment Position Manual 6th Edition*, pages 151 to 154.

8.3.1.1.1 Valuation of goods trade

Delivery of goods by an exporter to an importer signifies a change of ownership and may occur at any time and place from the point at which the goods are produced to the point of final use. The terms of delivery of goods are the responsibility of the buyer and seller as specified under each transaction contract and they differ from case to case. Consequently, transaction prices agreed between exporters and importers include varying amounts of distributive costs containing none, some or all of wholesaling, transport, insurance and taxes. In order to promote consistency between the accounts of different countries, it is important to establish a common valuation principal.

Within the balance of international payments framework, the point of uniform valuation is at the Customs frontier of the economy from which the goods are first exported, which means:

- 'Free on board' (FOB) at a port on the frontier of the exporting country (for goods dispatched by sea or inland waterways);
- 'Free carrier' (FCA) at a terminal on the frontier of the exporting country (for goods dispatched by means of transport to which FOB is not applicable); or
- 'Delivered at frontier' of the exporting country (for goods dispatched by means of transport to which FOB and FCA are not applicable, such as when goods are exported by railroad or pipeline).

The Customs imports value excludes transportation charges and insurance that occur after the point of direct shipment (typically this is the border), but includes all the transportation costs from the point of production to the point of direct shipment.

Suppose, for example, goods are imported to Canada from Mexico valued at $20 at the plant and it costs $2 to move the goods from the plant to the U.S.-Mexico border and an additional $5 for a U.S. carrier to move the goods from the U.S.-Mexico border to the Canada-U.S. border. In this scenario, the imported goods would be valued at $22 on an FOB basis and in addition there would be $5 of imports of transportation services.

For imports from the U.S. it is slightly different. Customs will record the value at the point of direct shipment, but in the case of imports by truck, by rail or by pipeline the point of direct shipment is unlikely to be equivalent to the Canada-U.S. border. For example, if a product is manufactured in California, put on a truck in San Francisco and delivered to Vancouver, the freight charge from San Francisco to the border (which will not be included in the Customs transaction value) will have to be added to get the balance of international payments value.

In some cases, an estimate of a market price equivalent may need to be made. Barter trade, overseas shipments of aid goods, provision of goods and services between affiliated enterprises where transfer pricing is a concern,[5] goods on consignment or for auction, or where goods change ownership but a final price is determined later may require adjustment to the goods value.

8.3.1.1.2 Balance of international payments adjustments

While the Customs data from which most of the goods trade statistics are derived are timely and very detailed, by product class and by country of origin or destination, they do not conform to all of the conceptual requirements of the balance of international payments so a number of adjustments are made. These account for differences in coverage, timing, valuation and classification. Most of these adjustments are applied to specific product categories for specific reasons. Some, such as certain coverage adjustments, are applied at the global level.

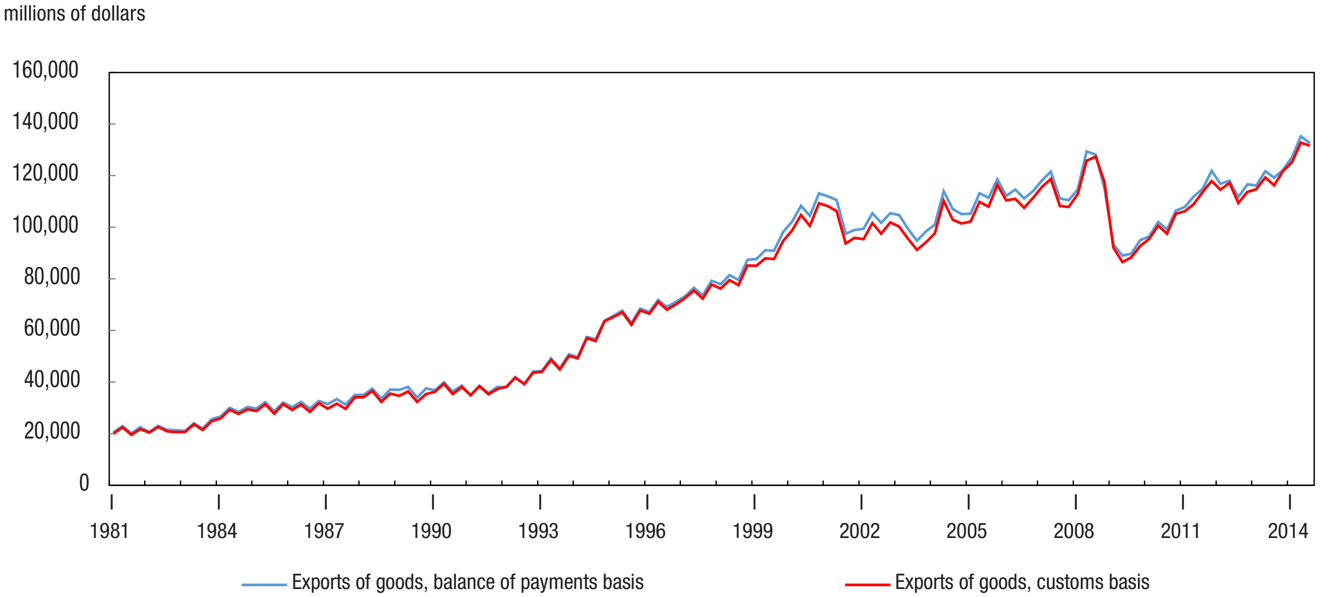
The aggregate effect of these adjustments is quite small relative to total exports and imports of goods (see Table 8.5 and Chart 8.1), but the adjustments can be significant for particular goods categories or countries of origin and destination. This section will discuss the more important of these adjustments.

Table 8.5
Balance of payments adjustments, 2009

	2009		
	Exports	Imports	Balance
	millions of dollars		
Inland freight	6,157	7,732	-1,575
Valuation and residency	-8,213	202	-8,415
Timing	-187	0	-187
Coverage	9,700	691	9,009
Total	7,457	8,625	-1,168

Source: Statistics Canada, tables 36-10-0019-01 and 36-10-0020-01.

Chart 8.1
Exports on a customs basis versus a balance of payments basis



Source: Statistics Canada, *User Guide: Canadian System of Macroeconomic Accounts (13-606-G)*.

Adjustments for **wheat** consist of replacing Customs data with information on clearances that are obtained from the Canadian Grain Commission. These data reflect more accurately the timing of shipment of Canadian grains.

Trade data for various **energy** products require special treatment for coverage and timing. Canadian exports of natural gas and petroleum shipped to the U.S. by pipeline are derived from Canadian sources, rather than from U.S. Customs data, because the former are viewed as more accurate. Data are obtained from Statistics Canada pipeline surveys and the National Energy Board.

An adjustment is made from 1996 forward for duplication of custom **software** already classified and covered in services imports and for undervaluation of prepackaged software exports.

Some freight adjustments are made to reported trade data to include inland freight between the plant and the border, or to reflect transaction as opposed to list prices. For example, deductions are made from exports to cover discounts and handling charges for **forestry** products.

Balance of international payments adjustments are also made to include transactions in **gold** between residents and non-residents where the gold is located in Canada and remains in Canada, since these transactions generate no Customs records.

On a customs basis, imports are allocated to the country of origin. This treatment was adopted in 1988 with the introduction of the international Harmonized Commodity Description and Coding System, or HS. For balance of international payments purposes, however, the country of last shipment better reflects the concept of ownership change.

One of the global adjustments made is a timing adjustment applied to non-U.S. exports since 1998. Its purpose is to adjust for Customs documents expected but not yet received in the accounting period.

Another global adjustment arises from goods trade reconciliation studies with Japan and the European Union which indicate that Canadian exports on a customs basis were understated in relation to counterpart imports for these and several additional countries other than the U.S. For this reason a coverage adjustment is applied from 1986 forward. Following other studies made in collaboration with Canada Customs and Revenue Agency (CCRA), the undervaluation of exports is re-estimated annually.

8.3.1.1.3 Re-exports and re-imports

BPM6 defines re-exports as follows (page 157): “Re-exports are foreign goods (goods produced in other economies and previously imported) that are exported with no substantial transformation from the state in which they were previously imported. The price of the re-exported good may differ from its price at the time it was originally imported, due to factors such as transport costs, dealers’ margins, and holding gains or losses. For goods to be included in re-exports for balance of international payments statistics, a resident must acquire then resell the goods with the goods passing through the territory.”

This category is to be distinguished from goods sold under merchanting, goods in transit through Canada and returned goods, none of which are classified as re-exports. Re-exports are included in Canada’s balance of international payments.

Some countries, like Hong Kong and the Netherlands, have very large re-exports relative to the size of their economies. In Canada, however, re-exports are relatively small. They were $25,183 million in 2009, about 5 per cent of total exports. It is useful to separate them from other exports because re-exported goods are not produced in Canada and therefore have less connection to other macroeconomic trends in the domestic economy compared to other goods exports.

Re-imports are the opposite of re-exports: domestic goods imported in the same state as previously exported, without any substantial transformation occurring to the goods while they were outside the territory. For goods to be included in re-imports, a non-resident must have acquired the goods from a resident institutional unit in Canada, then resold them to a resident institutional unit. In cases where there was no change of ownership they are omitted from imports, such as goods shipped for repair. Goods crossing the border for processing should be treated similarly but, like in most other countries, this is not currently the case.

8.3.1.1.4 Merchanting

BPM6 (page 157) defines merchanting “… as the purchase of goods by a resident (of the compiling economy) from a non-resident combined with the subsequent resale of the same goods to another non-resident without the goods being present in the compiling economy.” The acquisition of goods by such merchants is shown as a negative export of goods under merchanting. The subsequent sale of the goods is shown as a positive export of goods under merchanting. The net difference between the two, known as ‘net exports of goods under merchanting’, includes merchants’ margins and holding gains and losses and may be positive or negative.

For example, suppose a Canadian wholesaler purchased $1 million worth of goods from a Chinese manufacturer and subsequently sold the goods to a U.S. firm for $1.5 million without having the goods cross the Canadian border. In the accounting period when the goods were acquired, a negative $1 million export of goods under merchanting would be recorded. In the subsequent period when the goods were sold to the U.S. firm a positive export of goods under merchanting of $1.5 million would be recorded.

This kind of transaction is increasingly common in the global economy. However, it is not captured in Canadian administrative data sources or surveys and is for this reason difficult to measure accurately. Canada, as with most other countries, does not presently include merchanting trade in its balance of international payments statistics.

8.3.1.1.5 Goods for processing

The forces of globalization have, in recent decades, brought a much tighter integration of production processes across national boundaries. It is increasingly common for enterprises to operate corporations in two or more countries and to ship goods back and forth from one such corporation to another for different stages of processing. In the past these cross-border shipments for processing have been treated as merchandise trade, even if ownership of the goods does not change. *SNA 2008* and *BPM6* recommend that in these kinds of circumstances the transactions be treated as services trade (processing) rather than goods trade.

For example, suppose a Canadian automobile manufacturing plant shipped some parts to another plant in the U.S. for additional tooling and finishing. The value of the original parts shipped to the U.S. was $10 million and the value of the same parts after tooling and finishing when shipped back to Canada was $12 million. Instead of recording an export of $10 million followed by an import of $12 million, a single processing services import transaction of $2 million would be recorded.

This recommendation has not yet been implemented in Canada's international accounts.

8.3.1.1.6 Non-monetary gold

Gold has played a special role in international trade for centuries, both as a store of value and as a medium of exchange. There was a time when many countries fixed the value of their currencies in terms of a specific quantity of gold. Today most countries have long abandoned this 'gold standard'. For this reason among others the role of gold in global financial affairs is relatively less important today than in the past. Nevertheless it continues to be a part of the official international reserves of many countries. It is treated separately in the balance of international payments for this reason.

For purposes of the national and international accounts there are two types of gold—monetary and non-monetary. According to *BPM6* (page 93): "**Monetary gold** is gold to which the monetary authorities (or others who are subject to the effective control of the monetary authorities) have title and is held as reserve assets. Gold includes gold bullion and unallocated[6] gold accounts with non-residents that give title to claim the delivery of gold. Gold bullion takes the form of coins, ingots, or bars with a purity of at least 995 parts per 1,000, including such gold held in allocated gold accounts. All monetary gold is included in reserve assets or is held by international financial organizations." **Non-monetary gold** consists of all gold that is not monetary and it is a good, not a financial asset. Changes in the classification of a quantity of gold between the monetary and non-monetary categories are recorded in the other changes in financial assets and liabilities account.

Transactions in non-monetary gold are recorded in the same fashion as transactions in other products, although special treatment is sometimes required. If a Canadian resident imports or exports non-monetary gold it is recorded as a non-monetary gold import or export. This aligns with Customs data. If a Canadian resident sells gold to a non-resident but the gold remains in Canada this is recorded in the balance of international payments as an export of non-monetary gold, even though it is not recorded in the Customs data.

If the Bank of Canada is involved in a gold transaction with a central bank in another country, this transaction is not recorded in the current account but rather in the financial account since it is a transaction in financial assets. However, if the Bank of Canada buys or sells gold in the open market the transaction is recorded in the current account and a corresponding increase or decrease in Canada's monetary gold assets is recorded in the other changes in financial assets and liabilities account.

8.3.1.2 The services account

Trade in services is growing in importance. In 1981 it accounted for 11% of total trade in goods and services whereas in 2015 this percentage was 16%. However, this component is more difficult to measure than trade in goods because there are usually no associated Customs records. It is sometimes referred to as '**invisibles trade**'. In most cases it is measured by business survey vehicles that provide a lot less product and country of origin or destination detail than is the case for trade in goods.[7] Nevertheless, substantial services trade detail is available by country, on an annual basis, for product class aggregates.

The classification for traded services products that is used in Canada is the Extended Balance of Payments Services (EBOPS) classification. This is consistent with, but somewhat more detailed than the services categories elaborated in *BPM6*. It is product based and linked to the international Central Product Classification (CPC), version 2.

Table 8.6 shows trade in services in the year 2009 while Table 8.7 lists some additional tables that provide further details on trade in services. Services exports were $78 billion while services imports were $95 billion, implying a sizeable services trade deficit. There are four principal categories which are travel services, transportation services, commercial services and government services.

Table 8.6
Exports and imports of services, 2009

	2009		
	Exports	Imports	Balance
	millions of dollars		
Total, all services	**78,481**	**94,853**	**-16,372**
Travel	15,546	27,679	-12,133
Business travel	2,530	3,531	-1,001
Personal travel	13,017	24,150	-11,133
Transport	11,625	20,077	-8,452
Water transport	2,738	8,044	-5,306
Air transport	4,818	8,879	-4,061
Land and other transport	4,070	3,153	917
Commercial services	49,503	46,006	3,497
Maintenance and repair services	1,821	268	1,553
Construction services	374	351	23
Insurance services	1,493	3,641	-2,148
Financial services	5,090	5,409	-319
Financial intermediation services	1,890	817	1,073
Other financial services	3,200	4,593	-1,393
Telecommunications, computer, and information services	8,566	4,666	3,900
Charges for the use of intellectual property	4,111	10,164	-6,053
Professional and management consulting services	10,833	9,902	931
Research and development services	4,160	1,064	3,096
Technical, trade-related and other business services	10,631	8,179	2,452
Personal, cultural and recreational services	2,423	2,360	63
Government services	1,806	1,091	715

Source: Statistics Canada, table 36-10-0021-01.

Table 8.7
Trade in services, other breakdowns

Table number	Table title	Frequency	Availability
36-10-0004-01	International transactions in services, travel by category and geographical area	annual	1961 to date
36-10-0005-01	International transactions in services, transportation by category	annual	1961 to date
36-10-0006-01	International transactions in services, commercial services by category	annual	1961 to date
36-10-0007-01	International transactions in services, by selected countries	annual	1990 to date
36-10-0022-01	International transactions in services, commercial services, by North American Industry Classification System	annual	2007 to date
36-10-0070-01	International transactions in services, commercial services, by selected countries and regions (archived)	annual	1990 to 2000
36-10-0071-01	International transactions in services, commercial services by industry (archived)	annual	1990 to 2001
36-10-0093-01	International transactions in services, commercial services, by North American Industry Classification System (archived)	annual	1999 to 2009
36-10-0072-01	International transactions in services, by category (archived)	quarterly	First quarter 1995 to second quarter 2012

Source: Statistics Canada.

8.3.1.2.1 Travel services

The **travel services** category covers goods and services purchased for own use, or as gifts, during visits to another economy. The goods and services include food, lodging, recreational gifts and other incidentals as well as local transportation purchased in the country of travel. It excludes passenger fares for international travel.

The visits must be for less than one year.[8] There are two sub-categories, one for business travel and the other for personal travel. The latter is normally much larger than the former, as seen in Table 8.6 for 2009. Each trip is allocated either to business services in its entirety or to personal services in its entirety, based on the primary purpose of the travel.

Unlike most other services categories, travel is an assortment of goods and services, rather than strictly services. For this reason travel per se is not identified as a services category in the North American Product Classification System, although traveller accommodation and travel arrangement, reservation and planning services are recognized.

Business travel services pertain to goods and services acquired for personal use[9] by persons whose primary purpose of travel is for business. That means:

- employees on business travel,
- employees of international organizations on official business,
- employees doing work for enterprises that are not resident in the economies in which the work occurs,
- individuals temporarily engaged in productive activities (seasonal work, ongoing cross-border work and other short-term workers) directly for an entity resident in the compiling economy (their expenditures on goods and services in the host economy are included in travel) and
- carrier crews on lay over.

For example, suppose an individual in Canada is sent by her company to the U.S. to install some software. The client in the U.S. agrees to pay the company in Canada $8,000 per day, for an expected period of 10 days. The cost to fly the employee to the U.S. and back, on an American airline, is $1000 and the hotel and incidentals cost $4,000 for the two-week stay. While in the U.S., the employee buys gifts for her family and attends an opera at a total cost of $1,000.

In this example, all of the travel would be allocated to business services because that is the primary purpose of the travel. Canada would import $5,000 of business travel services. The export of the installation services of an expected $80,000 would be captured in commercial services and the imported airline services of $1000 would be in transportation services.

Similarly, **personal travel services** cover goods[10] and services acquired by persons going abroad for purposes other than business, such as vacations, participation in recreational and cultural activities, visits with friends and relatives, religious pilgrimages and education- and health-related travel.

8.3.1.2.2 Transport services

Transport services include:

- carriage of passengers,
- movement of freight,
- rentals (charters) of carriers with crew,
- supporting and auxiliary services such as cargo handling, navigation fees and cleaning of carriers, and
- postal and courier services.

Table 8.6 shows transportation services by type of carrier. It is also possible to break out these services by functional category: passenger, freight and other transport services.

Passenger transportation includes fares and other expenditures related to the carriage of passengers, such as charges for excess baggage items purchased on board carriers, provided in the international transport of non-residents by resident carriers (exports of transport services) and residents by non-resident carriers (imports of transport services). Also included are passenger services performed within an economy by non-resident carriers. An example of the former would be a U.S. non-resident flying on Air Canada to Canada or some foreign destination while an example of the latter would be a Canadian resident flying on United Airlines to the U.S. or some other foreign destination. Note that passenger services provided by a resident institutional unit to non-residents within the territory of residence of the carrier are included in travel rather than in transport services. Goods and services bought by non-resident travellers within the compiling economy are included either in travel or government services, not transport services.

The treatment of **freight services** is a consequence of adopting FOB as the uniform valuation principle for goods. By convention, all freight costs up to the Customs frontier are shown as incurred by the exporting country and all freight costs beyond the Customs frontier are incurred by the importing country. In addition to freight on exports and imports of goods, freight transport services may also apply to goods moved with no change of ownership, such as goods sent for storage or processing in another country and the shipment of migrants' personal effects.[11]

For example, suppose goods are imported into the U.S. from Japan, entering North America through the Port of Vancouver. The goods are then shipped by rail from Vancouver to the east coast of the U.S. using a Canadian carrier. The goods are valued at $10,000 and the cost of transporting them from Vancouver to the east coast is $1,000. In this example, Canada would show exports of transport services to the U.S. of $1,000. In its balance of international payments, the U.S. would record imports of goods from Japan of $10,000 and imports of transport services from Canada of $1,000.

8.3.1.2.3 Commercial services

Commercial services is by far the largest of the main categories of trade in services, as seen in Table 8.6. It has ten sub-categories.

8.3.1.2.3.1 Maintenance and repair services

The **maintenance and repair services** sub-category includes payments by Canadian residents to non-residents (imports) for repair work, including parts and other materials supplied by the repairing business, as well as receipts by Canadian businesses from non-residents (exports) for repair work performed on the non-residents' goods. The value of the goods themselves—the ones that are being maintained or repaired—are of course excluded from the valuation of the imported or exported maintenance and repair services.

For example, if a Canadian company representative travels to the U.S. to repair a machine the U.S. company purchased a few years earlier and the cost of the service is $10,000 including Canadian-sourced parts of $6,000 and labour of $4,000 then the Canadian balance of international payments would record exports of maintenance and repair services of $10,000.

There are two exceptions. First, construction maintenance and repair work is classified as construction services rather than general maintenance and repair services. Second, the repair of computer equipment is regarded as part of the telecommunications, computer and information services sub-category rather than the maintenance and repair services sub-category.

8.3.1.2.3.2 Construction services

Construction services pertain to the building, renovation, repair or extension of existing fixed assets in the form of buildings, engineered land improvements and other infrastructure works such as roads, bridges and dams. Related installation and assembly work is included as are management of construction projects, site preparation and specialized services such as painting, plumbing and demolition.

These services comprise work performed on construction projects by an enterprise that is non-resident from the perspective of the host country. Generally the work is of a short-term nature. The value of the construction service provided is equal to the full value of the construction project itself inclusive of all goods and services provided by the enterprise as inputs to the work and also inclusive of other costs of production and the operating surplus that accrues to the enterprise.

The acquisition of goods and services from within the host economy for use as intermediate inputs to a construction project by the enterprise undertaking the construction work is recorded under general merchandise imports. However, goods and services acquired from the home economy are treated as resident-to-resident transactions and as such are excluded from trade. Goods and services purchased from third economies are recorded under the appropriate general merchandise or service category for the economy of the enterprise doing the construction work—in other words, as imports of goods or services in the home economy of the construction enterprise.

For example, suppose a Canadian company undertakes construction work in the U.S. The construction project takes six months to complete. Over the course of the project the company brings in $1 million of construction materials from Canada, purchases $2 million of materials in the U.S. and imports $1 million of services from Mexico. The total value of the project is $10 million. These transactions would be recorded in the Canadian balance of international payments as $2 million of merchandise imports from the U.S., $1 million of services imports from Mexico and $10 million of construction services exports to the U.S.

Generally the construction contracts covered in international trade are of a short-term nature. If the external operations of a construction enterprise are substantial enough, they may be managed through a local site office and as such a **branch** may be identified as an institutional unit resident in the host economy. A branch is a kind of notional institutional unit or quasi-corporation (see Chapter 3) that is defined even though it is unincorporated. It is treated as a direct investment enterprise (see section 8.5.1). Conditions for establishing a branch within the international accounts include:

- either a separate set of accounts, including a balance sheet, exists for the unit identified as a branch or it could be created;
- the unit being identified as a branch is managing production of significant scale for one year or more, or intends to do so;
- the unit being identified as a branch purchases or rents business premises, recruits local staff and operates a bank account; and
- the unit being identified as a branch is subject to the income tax system and other legal requirements of the host economy.

For example, suppose a Canadian company undertakes construction work in the U.S. The construction project takes two years to complete and is managed by a foreign branch of the Canadian company. Over the course of the project the branch brings in $1 million of materials from Canada, purchases $2 million of goods from the U.S. and imports $1 million of services from Mexico. The total value of the project is $10 million. In the Canadian balance of international payments these transactions would be recorded simply as exports of goods $1 million. The U.S. balance of international payments would show imports of goods of $1 million from Canada and imports of services of $1 million from Mexico. The payment for construction services would be treated as if it were made to the branch office—treated as an institutional unit in the U.S.—which might then remit the profits back to the Canadian firm as primary income flows in the current account.

8.3.1.2.3.3 Insurance and pension services

Insurance and pension services cover provision of life insurance and annuities, non-life insurance, re-insurance, freight insurance, pensions, standardized guarantees and auxiliary services to non-residents by resident insurance companies and vice versa.

Insurance and pension services get special treatment in *SNA 2008* and *BPM6* (in the latter, see Appendix 6c, pp. 282 to 288). The services here are the financial management and administration services provided by insurance and pension funds. For insurance, the services component is calculated as gross premiums earned by the insurance companies plus premium supplements[12] minus claims payable, with adjustment for unusual claims volatility if necessary. For pensions the calculation is similar, but involves contributions instead of premiums and benefits rather than claims, plus an adjustment for changes in pension entitlements.

For example, suppose a U.S. property insurance company sold insurance policies in Canada in 2009. Suppose Canadians paid CAN$50 million in premiums to the company that year and the company earned an addition CAN$1 million in premium supplements. Suppose Canadians made claims on their policies in the amount of CAN$45 million that year. Assume there was no unusual claims volatility that year. In this example, Canada would be importing CAN$50 + CAN$1 – CAN$45 = CAN$6 million worth of property insurance services that year from that company.

The above calculation generates components that appear in the following places of the current account of the balance of international payments:

- Goods and services account: the services components
- Primary income account: investment income attributable to policy holders
- Secondary income account: net premium receivable which is equal to gross premiums receivable plus investment income minus the service component; also claims payable
- Financial account: change in insurance reserves

Life insurance policyholders make regular payments in return for an agreed sum, or an annuity, at a specified date in the future. This type of insurance is a form of saving combined with indemnification against early death. The insurance company must combine the saving aspect of a single policy with actuarial calculations on the insured population when determining the relationship between premiums and benefits. Life insurance policies redistribute income for a single policyholder across time periods while spreading the risk of early death across all policyholders.

Non-life insurance is designed primarily to spread property and casualty risks across policy-holders as a group. Typically the number of claimants is much smaller than the number of policyholders. All policyholders pay a premium each accounting period. Only those policyholders for whom an insured event occurs receive payment for claims.

Re-insurance allows insurance risk to be transferred from one insurance provider to another. The original insurers issue insurance policies in return for premiums and then pass on either a portion of the associated risk or the entire risk above a specified threshold. In effect, the insurance companies become insurance policyholders themselves, protecting against extraordinary events such as those related to catastrophic losses. Re-insurance is often cross-border in nature.

Freight insurance raises particular issues for the valuation of goods in the current account. It is extended to cover policyholders against theft, damage and loss of freight. The FOB valuation principle determines whether the insurance is included in the price of the merchandise to which freight insurance applies or is treated separately as an export or import of freight insurance services. Recall from section 8.3.1.2.2 that freight insurance premiums are included in the FOB price up to the border of the exporter while beyond the exporter's border, freight insurance is measured separately either as part of trade in services if provided by the exporter country or another economy, or as part of the importing country's domestic production.

BPM6 has the following to say about **auxiliary services** (p. 172): "Auxiliary insurance services consist of the provision of services that are closely related to insurance and pension fund operations. Included are agents' commissions, insurance brokering and agency services, insurance and pension consultancy services, evaluation and loss adjustment services, actuarial services, salvage administration services, and regulatory and monitoring services on indemnities and recovery services. These services are charged through explicit charges."

8.3.1.2.3.4 Financial services

The production of **financial services** is discussed in Chapter 4 (section 4.4.1.3). The topic here is the export and import of these services.

Included in this category are services provided by financial intermediaries and auxiliaries between residents and non-residents, except those provided by insurance and pension funds. Most often financial services are supplied by banks and other financial corporations.

Financial services may be charged for by explicit fees, margins on buying and selling transactions, asset management costs deducted from property income receivable in the case asset-holding entities or margins between interest payable and the reference rate on loans and deposits called financial intermediation services indirectly measured (FISIM).

Explicit charges include loan application fees, commissions and brokerage fees, account charges, early or late payment fees and the like. Financial market regulatory services charges are also in this sub-category.

Margins on transactions include those charged by dealers, market-makers, foreign-exchange bureaus and similar businesses. Typically these firms intermediate by both buying and selling within a given market. They buy at a lower price than they sell, with the difference being their total margin on transactions.

Asset management fees apply to institutional units who entrust their assets to financial enterprises for safekeeping and investment. Mutual funds, investment funds, hedge funds, holding companies and trusts are examples of such businesses. They charge the owners of the assets for the financial management services they provide. This is often done by deducting a percentage of the investment income earned.

For example, suppose an individual invests $100,000 in a mutual fund abroad that pays interest or dividend income each quarter. The individual receives $1,500 of income each period and the foreign fund manager retains $500 of the income earned in the period, as asset management fees. In the Canadian balance of international payments this would be recorded as property income received of $1,500 and financial service imports of $500. Note that the only directly observable flow is the $1,500 of investment income coming from the non-resident fund manager to the Canadian resident.

The remaining sub-category of financial services is intermediation services which are indirectly measured, or FISIM. A depositor might deposit funds in a bank and earn 2.0% interest, although if he could find another borrower of equivalent creditworthiness in the open market he might earn 3.5% instead. A borrower might come to the bank and borrow funds at 5.0%, although if he could find another lender in the open market he might be charged just 3.5%. The bank's revenue is the difference between the rate paid by the borrower and the rate received by the depositor, which is 5.0% – 2.0% = 3.0%. The bank earns this margin by intermediating between the depositor and the borrower, making it simpler and more economic for both to carry out their transactions via the bank rather than in the open market. The market rate, 3.5% in the example, is referred to as the reference rate. So for loans from financial corporations, the service charge is the difference between interest actually payable and the amount payable if the reference rate were used while for deposits it is the difference between the interest that would be paid if reference rate were used and interest actually paid.

The reference rate represents the pure cost of borrowing funds. It should include no service component, should reflect the risk and maturity structure of deposits and loans, and is likely to be different as between local currency transactions and other currency transactions.

In the example just discussed, if the depositor deposited $100,000 in a foreign bank account and the borrower was lent $200,000 by a foreign bank, in the Canadian balance of international payments there would be annual imports of financial services equal to $100,000 × 0.015 = $1,500 in the form of FISIM services to the depositor and $200,000 × 0.015 = $3,000 in the form of FISIM services to the borrower.

Note that because of FISIM, adjustment is required for the interest received and interest paid in the primary income account. Actual interest payable by a borrower is partitioned between pure interest to be recorded in the primary income account and FISIM that is recorded in trade in services. Similarly, pure interest receivable by depositors (actual interest which excludes the value of services (FISIM)) is recorded in the primary income account and the implicit FISIM component is recorded in trade in services.

International FISIM flows are measured using information on international loans and deposits obtained from a variety of sources including Statistics Canada surveys of Canadian banks, the Bank of International Settlements, the Bank of England, the U.S. Federal Reserve and monthly reports of the Export Development Corporation.

At time of writing FISIM is measured with a single reference rate in domestic currency terms (Canadian dollars). However, there has been much international discussion about the desirability of identifying separate reference rates for borrowing and lending in different currencies. Doing so would help statisticians assure that the exports of FISIM from country A to country B, as measured in country A, are equal to the imports of the same FISIM as measured by country B after currency conversion. International discussions continue on this topic.

8.3.1.2.3.5 Telecommunications, computer and information services

Telecommunications services include the broadcast or transmission of sound, images, data or other information by telephone, telex, telegram, radio and television cable transmission, radio and television satellite, electronic mail, facsimile and so forth, including business network services, teleconferencing and support services. Mobile telecommunications services, Internet backbone services and online access services, including provision of access to the Internet, are also included. Excluded are the value of the content being transmitted and installation services for telephone network equipment (included in construction) and information services (included in other trade categories).

Computer services include hardware- and software-related services and data-processing services such as licenses to use software, maintenance and repairs of computers, data recovery services, web page hosting services and hardware and software consultancy services. Specifically excluded are charges for licenses to reproduce or distribute software, leasing of computers without an operator, computer training courses not designed for a specific user and non-customized packaged software all of which are included in other trade categories.

Information services include news agency services, database services such as data storage, dissemination of data and databases, web search portals, non-bulk subscriptions to newspapers and periodicals and downloaded content that is not software, audio or video. Measurement of these cross-border services is becoming more and more challenging as the amount of available on-line information-for-a-fee grows. Specifically excluded are bulk newspapers, downloaded software and downloaded audio and video which are included in other trade categories.

8.3.1.2.3.6 Charges for the use of intellectual property

Charges for the use of intellectual property include payments for the use of proprietary rights such as patents, trademarks, copyrights, industrial processes and designs including trade secrets and franchises. These rights can arise from research and development, as well as from marketing. Intellectual property charges also include payments for licenses to reproduce or distribute intellectual property embodied in produced originals or prototypes, such as copyrights on books and manuscripts, computer software, cinematographic works and sound recordings and related rights such as for live performances and television, cable and satellite broadcasts. Specifically excluded, in Canada, are outright purchases and sales of franchises and trademarks, which are recorded in the capital account.

8.3.1.2.3.7 Professional and management consulting services

Professional and management consulting services include legal, accounting, management consulting, managerial and public relations services as well as advertising, market research and public opinion polling services. Also included in this sub-category are services for the general management of a branch, subsidiary or associate provided by a parent enterprise or other affiliated enterprise.

8.3.1.2.3.8 Research and development services

Research and development services refer to the outright purchase or sale of the ownership rights to the results of research and development, such as patents, copyrights and information about industrial processes. Specifically excluded are charges for the use of the outcomes of research and development.

8.3.1.2.3.9 Technical, trade-related and other business services

Technical and other business services include agricultural, engineering, waste treatment, pollution remediation, operational leasing and a variety of other services.

Trade-related services refer to commissions on goods and services transactions payable to merchants, commodity brokers, dealers, auctioneers and commission agents.

Other business services include distribution services related to water, steam, gas and other petroleum products and air-conditioning supply, where these are identified separately from transmission services; placement of personnel, security and investigative services; translation and interpretation; photographic services; publishing; building cleaning; and real estate services. Also included are forfeited down payments not able to be associated with any other service. (See *BPM6*, p. 179.)

8.3.1.2.3.10 Personal, cultural and recreational services

There are two broad sub-categories of **personal, cultural and recreational services**, which are audiovisual and related services and other cultural and recreational services.

Audiovisual and related services refer to services related to the production of motion pictures, radio and television programs and musical recordings. Included are rentals of films and videotapes, fees received by actors, directors and producers[13] and charges for access to encrypted television channels such as cable and satellite services. Specifically excluded are mass-produced recordings and manuscripts on physical media, which are included in general merchandise trade, and charges or licenses to reproduce or distribute radio, television, film and music programming, which are included in charges for the use of intellectual property.

Other cultural and recreational services include other types of services such as those associated with museums, libraries and archives, other cultural, sporting and recreational activities, education services, health services and gambling.[14] Some examples are cross-border diagnostic laboratory services, correspondence courses, fees and prizes paid to athletes and the service component of lottery tickets. Specifically excluded are education and health services provided to non-residents who are present in the territory of the service provider, which are included in travel. Also excluded is the acquisition of other personal, cultural and recreational services by persons while outside their territory of residence, which are also included in travel.

8.3.1.2.4 Government services

There are three sub-categories of **government services**.

The first is goods and services supplied by and to enclaves such as embassies, military bases and international organizations. This includes, for example, visas and other services provided to residents of the host economy (exports) and office supplies, vehicles, repairs, rental of premises, electricity and so on purchased from the host economy (imports).

The second is goods and services acquired from the host economy by diplomats, consular staff and military personnel located abroad and their dependents. For example, if an embassy staff member or a member of her family purchases food and clothing in the host economy, this is an import of government services. Similarly if a diplomat sells his car at the end of his stay abroad this would be a Canadian export of government services and an import of government services by the host economy.

Finally, the third sub-category is services supplied by and to governments and not included in other categories of services, such as technical assistance on public administration when not classified to a specific service, payments for police-type services and the issue of licenses and permits to government agents to exercise some proper regulatory function. These services should, in principle, be classified to other specific services categories, but sometimes this is not possible.

8.3.1.3 Price and volume indexes for goods and services trade

The current and capital accounts, the financial account, the other changes in financial assets and liabilities account and the international investment position are all recorded at current market prices. Estimates at constant prices are not available, with the exception of the estimates for trade in goods and services. For these particular components of the current account, aggregate price indexes are available and they are used to produce associated trade volume indexes.[15]

Many of Canada's import and export price indexes are constructed using either domestic prices or U.S. prices adjusted for the movement in the Canada-U.S. exchange rate. The implication is that changes in exchange rates are reflected immediately and fully in import and export prices. Studies have shown this is not always the case and some prices tend to respond in a lagged manner. To address this problem an aggregate price adjustment is made to the 'other balance of international payments adjustments' price.

The measurement of trade-in-services prices is especially difficult, compared to trade-in-goods prices. However, the fact that a significant portion of goods trade is included in services trade by definition—in travel services, construction and government services—somewhat lessens this challenge.

8.3.2 The primary income account

The primary income account shows primary income flows between resident and non-resident institutional units. As explained in earlier chapters, primary incomes represent "the return that accrues to institutional units for their contribution to the production process or for the provision of financial assets and renting natural resources to other institutional units."[16] The compensation of employees and taxes and subsidies on products and production are income related to the production process. The returns associated with the ownership of financial assets (called investment income) and renting natural resources (rent) are property income consisting of dividends and withdrawals from income of quasi-corporations, reinvested earnings, interest and rents.

Primary incomes accrue in the first instance to producing units—corporations, households, governments and non-profit institutions serving households. From there they are allocated as labour compensation and taxes on products and production or property incomes to the institutional units providing financial assets and renting natural resources. The allocation of primary income focusses on institutional units in their capacity as recipients of income rather than as producers of primary income.

Table 8.2 shows primary income transaction flows broken down in two main categories, compensation of employees and investment income. The investment income flows, in turn, are reported separately for direct investment income, portfolio investment income and other investment income. Direct investment income flows are those coming from direct investment enterprises—enterprises for which an influential (10% ownership or more) or controlling (50% ownership or more) direct investor resides in another economy. This type of investment income includes not just dividends and interest, but also reinvested earnings (more on this below). Portfolio investment income flows, in contrast, are those associated with investors whose individual investment holdings are not considered influential (less than 10% ownership). Other investment income is a smaller residual category and includes interest on loans and investment income attributable to policyholders in insurance among other things.

Cross-border primary income flows are the link between the concept of gross domestic product and that of gross national income. GDP is linked to production which generates primary income, while the latter represents the income earned by residents or non-residents from ownership of labour, financial assets and natural resources. The difference between the GDP and GNI is equal to the difference between primary income receivable from non-residents and primary income payable to non-residents, described as net income from abroad.

8.3.2.1 Compensation of employees

Compensation of employees arises in the international accounts when the employer and the employee are resident in different economies. In Canada this could occur, for example, at the Windsor-Detroit border with the United States. Canadian residents might work in Detroit and U.S. residents might work in Windsor. It can also occur with seasonal and other temporary workers. For example, if Honduran residents come to work in Canada in seasonal jobs in the agriculture industry, their compensation would be considered as a primary income payment from a Canadian employer to a Honduran resident. As usual, the practical criterion for determining residency in whether the employees are domiciled for more than one year. Primary income flows between resident and non-resident institutional units can also occur when the embassy of one country, located in another country, engages local individuals as employees. The local employees are non-resident from the perspective of the country with the embassy.

In order for compensation of employees to be recorded there must be an employee-employer relationship. This requires an agreement between a producing institutional unit and a person whereby the person works for the producing unit in return for remuneration, in cash or in kind, based on some objective indicator of the amount of work done. If the individual is contracted to produce a specific result there may be a service contract relationship rather than an employment relationship, as with consultants, in which case the associated transactions are exports or imports of services rather than flows of compensation of employees. Sometimes it may not be immediately clear whether the relationship is 'employer'-'employee' or 'service purchaser'-'service provider'. If necessary, a variety of indicators can be examined to make this determination.

Compensation of employees is recorded on an accrual basis. It is the amount of compensation that the employees become entitled to as a result of their work performed during the accounting period, regardless of any leads or lags that may exist in the actual payment of the compensation. If employees incur travel expenses and pay income taxes associated with their employment, these amounts should not be deducted from compensation as recorded in the primary income account. All the other guidelines applying to compensation of employees that are discussed in Chapter 5 apply similarly in the international accounts.

8.3.2.2 Investment income

Investment income accrues to an investor as a result of his or her ownership of a financial asset. This category of primary income flows can be presented using the functional classification (investment income from direct investment, from portfolio investment or from other investment) or the instrument classification (dividends, reinvested earnings, interest, investment income attributable to policyholders of insurance, standardized guarantees and pension funds). In this section investment income will be discussed according to the second classification, although the information is also available according to the functional classification. This is important as it permits the income statistics to be compared with the corresponding financial flow and international investment position statistics.

8.3.2.2.1 Dividends

If a resident institutional unit owns equity in a corporation that is resident in another economy, the owning unit may be entitled to dividend flows at the discretion of the corporation. These dividends appear in the primary income account in the accounting period in which the corresponding ‘ex dividend’ date occurs.[17] This date is the first day, following the announcement of the dividend, that the corporation’s shares trade on equity markets without the dividend. Prior to that date, if someone purchases the corporation’s shares they will be entitled to receive that dividend when it is eventually paid out.

8.3.2.2.2 Reinvested earnings

BPM6 defines retained earnings as follows (page 188): “Retained earnings of an enterprise shows the net earnings from production and primary and secondary income transactions before attributing reinvested earnings. It is equal to net operating surplus plus primary income, current transfers receivable, and change in pension entitlements, and minus primary income (excluding reinvested earnings payable to the enterprise’s direct investors and owners of investment funds) and current transfers payable.”

The international accounts treat the retained earnings attributable to investment funds and direct investment enterprises as if they were paid to the owners and then reinvested. “The rationale behind this treatment is that, because a direct investment enterprise is, by definition, subject to control or influence by a direct investor or investors, the decision to retain some of its earnings within the enterprise represents an investment decision on the part of the direct investor(s)” (*BPM6*, page 32).

Thus, as a simple example, suppose a direct investor in Canada had a direct investment enterprise in country A. Suppose that the enterprise had retained earnings of $100 million in a particular accounting period and the direct investor had an ownership position of 60% in the direct investment enterprise. In this situation, the international accounts would record imputed reinvested earnings of $60 million in the primary income account as receipts by Canada. The accounts would also record an imputed direct investment from Canada in country A of $60 million.[18]

8.3.2.2.3 Interest

Interest is paid to institutional units who own certain financial assets, namely deposits, bonds and other debt securities, loans and other accounts receivable. It is recorded on an accrual basis, continuously over time. Similar to dividends, interest can be paid on direct investment or portfolio investment. Primary income flows of interest are adjusted to reflect FISIM as discussed in section 8.3.1.2.3.4.

The fact that interest is recorded on an accrual basis in the international accounts, even though it is usually paid at discrete intervals depending on the specific contractual arrangements, means that offsetting entries must be made in the financial account. For example, if a household in Canada owns a bond from country A that pays $1000 interest at the end of each year, the interest income in the primary income account would be recorded as $250 per quarter during the year while the financial account would record investment income receivable of $250 in each of the first three quarters of the year and –$750 in the fourth quarter when the interest cash payment was actually made. The financial account would also show the cash receipt of $1000 in the fourth quarter.

8.3.2.3 Other primary income

8.3.2.3.1 Rent

According to *BPM6* (page 200): “Rent covers income receivable for putting natural resources at the disposal of another institutional unit. The party providing the natural resource is called the lessor or landlord, while the user is called the lessee or tenant. The terms under which rent is payable are expressed in a resource lease. A resource lease is an agreement whereby the legal owner of a natural resource that has an infinite life makes it available to a lessee in return for a regular payment recorded as rent.”

Rent payments are a form of primary income flows. However, most rent payments are made by resident units and for this reason do not appear in the international accounts. An example of a rent payment that would enter the international accounts might be a fishing operation that pays for temporary access to fishing rights in another country. Such payments are not significant in Canada and do not appear explicitly in its international accounts.

8.3.2.3.2 Taxes and subsidies on products and production

If a non-resident institutional unit paid taxes on products or taxes on production to a resident government, or received subsidies from that government, those tax payments or subsidy receipts would be recorded in the primary income account. Such trans-border payments of taxes and subsidies are not considered significant in Canada’s case. For example, the Goods and Services Tax does not apply on goods and services exported by Canada and import duties have been greatly reduced under various free trade agreements. However, it is possible some import duties and state and provincial tax payments across the Canada-U.S. border may become more prevalent in future as consumers engage increasingly in direct international purchases online.

8.3.3 The secondary income account

The secondary income account records current transfers, in cash or in kind, between resident and non-resident institutional units. These current transfers have the effect of redistributing income that would otherwise be available for consumption expenditure or saving by the donor units. In other words, net secondary income plus gross national income determine gross national disposable income.

As with all entries in the balance of international payments, a current transfer gives rise to two accounting entries for each party to the transaction, one in the current account and one in the financial account. If the transfer is in cash, the donor typically records a decrease in deposits and a transfer payable while the recipient usually records an increase in deposits and a transfer receivable. For current transfers in kind, the donor shows an export of goods or services and a transfer payable while the recipient records an import of goods or services and a transfer receivable.

Most current transfers are recorded at the time when economic ownership changes. However, for tax transfers the recording takes place when the tax liability is incurred—that is, when the activities, transactions or other events that give rise to the government’s tax claim occur—rather than when the funds are actually transferred.

BPM6 identifies two broad categories of current transfers: ‘personal transfers’ and ‘other current transfers’. Their composition is discussed below. Canada presents the secondary income account somewhat differently and with less detail, recording two aggregate components: ‘private transfers’ and ‘government transfers’.

8.3.3.1 Personal transfers

Personal transfers consist of current transfers between resident and non-resident households, regardless of whether the households are related or unrelated.[19] They also include the winning proceeds from lotteries and other gambling schemes. Of the total amount paid for the gambling services (by means of lottery tickets, slot machines, etcetera), a portion goes to the service provider as a service charge and is counted in the goods and services account. The remainder is paid out as prizes and these are considered to be current transfers from households to households or, in some cases, to NPISH units. If the payment is from a resident gambling scheme to a non-resident, or from a non-resident gambling scheme to a resident, the payment is considered to be a personal transfer.

The concept of **international remittances** is related to personal transfers, but is broader. It includes personal transfers but also several other types of international transaction flows: travel and transport related to employment of border and short-term workers (in the goods and services account), compensation of employees (in the primary income account), taxes and social contributions related to border and short-term workers plus social benefits and current transfers to NPISH units (in the secondary income account) and capital transfers between households and from households to NPISH units (in the capital account). International remittances are a large and important part of the balance of international payments in some countries. According to the World Bank,[20] worldwide remittances exceeded $430 billion in 2015 with the countries receiving the most being India, China, the Philippines, Mexico and Nigeria. International remittances are explained more fully in Appendix 5 of *BPM6*.

8.3.3.2 Other current transfers

Other current transfers (that is, current transfers other than personal transfers) comprise a variety of transactions, without quid pro quo, between resident and non-resident units.

8.3.3.2.1 Current taxes on income and wealth

Current taxes on income and wealth include taxes imposed by governments on the primary income, transfer receipts or assets of non-resident units. For example, seasonal or other temporary workers who are present in Canada for less than one year earn compensation as employees and typically pay income tax on their earnings. Those taxes are regarded as a transfer from non-residents to Canadian governments and are included as secondary income of governments. Similarly institutional units who own equity or fixed income assets in another country normally pay withholding tax on their dividend and interest income. Taxes on capital gains also fall in this category. Note that taxes on products and production are excluded from this category and are included, rather, in the primary income account. Also excluded are inheritance taxes, which are regarded as capital transfers.

8.3.3.2.2 Social contributions

Social contributions include contributions to social security schemes and pension arrangements in another economy for purposes of securing social benefits for the beneficiaries. They include the contributions both by employees directly and by employers on behalf of their employees. In the case of pension schemes the social contributions are calculated as the employees' actual contributions plus the employers' actual contributions plus the employers' imputed contributions plus contribution supplements (investment income payable by pension schemes on pension entitlements) minus service charges paid to pension administrators.

8.3.3.2.3 Social benefits

Social benefits include assistance payments or receipts, in cash or in kind, under social security and pension schemes. For example, someone who had lived in Canada for a long period of time and paid into the Canada Pension Plan (CPP) before moving to the United States would be entitled to collect CPP benefits even though resident in the U.S. The flow of payments in this example would be secondary income transfers from the Canadian government sector to a non-resident household. This category also includes benefits paid to households by governments or NPISH units that are not made under social insurance arrangements. Social benefits transfers are not large in Canada's balance of international payments, although they are more significant in some other economies.

8.3.3.2.4 Net premiums on non-life insurance and standardized guarantees

When institutional units purchase non-life insurance or standardized guarantees, they pay in the form of premiums and premium supplements (investment income accruing from premiums paid in advance). Some of these amounts are retained by the service providers as service fees and the remainder, referred to as net premiums, are eventually paid out to satisfy claims against the insurance or guarantee policies. When these net premiums are paid between residents and non-residents they are treated as a form of secondary income transfer. For example, if a Canadian household purchased a non-life insurance policy from a corporation in the U.S., the net premium that it paid to the corporation during an accounting period would be considered a secondary income transfer from a resident household to a non-resident institutional unit.

The term 'standardized guarantees' refers to guarantees against creditors defaulting in probabilistic conditions that have characteristics similar to non-life insurance. As with non-life insurance, only a relatively small proportion of those acquiring the guarantees actually end up making claims. Often these guarantee schemes are offered by governments, though private corporations also provide such arrangements. The deposit insurance scheme operated by the Canada Deposit Insurance Corporation is an example of such a scheme. Mortgage loan insurance offered by the Canada Mortgage and Housing Corporation is another.

8.3.3.2.5 Non-life insurance claims and calls under standardized guarantees

Similar but opposite to the previous section, when institutional units make claims against non-life insurance policies or standardized guarantee schemes, the amounts paid out between residents and non-residents are treated as a form of secondary income transfer. For example, if a Canadian household made a claim against a non-life insurance policy acquired from a corporation in the U.S., the claim payout it received from the corporation during an accounting period would be considered a secondary income transfer from a non-resident institutional unit to a resident household. In relatively rare circumstances where large non-life insurance claims result from a catastrophe, some part of the claims may be recorded as capital transfers rather than current transfers.

8.3.3.2.6 Current international cooperation

It is common for the governments and NPISH units of developed countries to provide secondary income transfers to governments in less developed countries for various reasons. In some cases these are one-time current transfers intended to provide assistance during specific emergencies related to floods or other natural disasters. In other instances they are ongoing transfers, other than for capital purposes (which are treated as capital transfers), to assist with economic development in those countries. Payments to cover the salaries of technical assistance staff resident in the countries they are assisting also fall into this category. Canadian institutional units seldom if ever receive transfers of this kind, but the Government of Canada and various Canadian NPISH units do make transfers abroad of this type.

In fiscal year 2014-2015, for example, Canada provided international assistance disbursements totalling $5,842 million according to the Statistical Report on International Assistance, Fiscal Year 2014-2015.[21] Not all of this amount is considered to be current international cooperation transfers, however. For example, the total includes the provincial costs of refugees in Canada.

BPM6 notes that concessional loans to developing countries—for example, economic development loans with a zero rate of interest—could also, in principle, be considered as a form of secondary income transfer, but as yet no adequate means has been devised to calculate the transfer portion of such transactions. It recommends that information about concessionary loans be provided as supplementary information pending the development of international standards for such loans.

8.3.3.2.7 Miscellaneous current transfers

The **miscellaneous current transfers** category includes a variety of additional kinds of current transfers that are not encompassed by the other categories. Membership dues and donations to NPISH units are one example. Fines imposed on institutional units by courts of law or other government bodies are another. Additional examples include payments of compensation and gifts or donations of a current nature.

8.4 The capital account

The capital account records receipts and payments of a capital nature. These include capital transfers receivable and payable between residents and non-residents and the net acquisition of non-produced non-financial assets.

Table 8.2 shows total receipts and payments in the capital account in 2009. Receipts were $248 million and payments $1,066 million, implying a balance on capital account of –$819 million. These are relatively small amounts given that total current account receipts were $511 billion that year and total current account payments $557 billion. The capital account typically plays a minor role in Canada’s international accounts.

8.4.1 Capital transfers

Capital transfers are encountered in earlier chapters. They involve the provision of resources for capital purposes by one transactor without anything of economic value being supplied as a *quid pro quo*. To quote *BPM6* (p. 209): “Capital transfers are transfers in which the ownership of an asset (other than cash or inventories) changes from one party to another; or that oblige one or both parties to acquire or dispose of an asset (other than cash or inventories); or where a liability is forgiven by the creditor. Cash transfers involving disposals of noncash assets (other than inventories) or acquisition of noncash assets (other than inventories) are also capital transfers. A capital transfer results in a commensurate change in the stocks of assets of one or both parties to the transaction without affecting the saving of either party." Note that capital transfers can be in cash or in kind. If they are in kind, a market value equivalent estimate is assigned to them for purposes of the accounts.

8.4.1.1 Debt forgiveness

One common form of capital transfer is debt forgiveness.[22] This occurs when a resident institutional unit cancels all or part of a debt obligation of a non-resident institutional unit. For example, under the 'Heavily Indebted Poor Countries' initiative led by the World Bank and the International Monetary Fund, Canada and other Paris Club creditor countries have committed to providing comprehensive debt relief to the world's poorest and most indebted countries. Canada has forgiven debt as part of this initiative and these amounts are treated as capital transfers and as corresponding transactions in the financial account.

8.4.1.2 Assumptions of debt under guarantees

One-off guarantees and other assumptions of debt, if and when activated, are also capital transfers. If the debt assumer receives a liability from the debtor consequent to assuming the debt, such as a promise of reimbursement, this is regarded as a financial account transaction.

8.4.1.3 Capital taxes

Capital taxes are another form of capital transfer. They include taxes, levied at infrequent intervals, on assets or net worth. Taxes on wealth that are levied at frequent intervals, such as property taxes, are current transfers. Capital taxes also include levies on assets transferred such as estate or inheritance taxes and gift taxes. They do not include taxes on sales of assets.

8.4.1.4 Non-life insurance claims

Cross-border non-life insurance claims are also classified as capital transfers if they are exceptionally large or unusual. In the event of cross-border reinsurance claims resulting from large or unusual events they would be classified as capital transfers. In the Canadian international accounts all such claims are treated as current transfers.

8.4.1.5 Transfers to finance investment

Sometimes governments, NPISH units or international organizations make cash transfers or transfers in kind to institutional units in other countries to finance all or part of the costs they incur by acquiring fixed assets. Such transfers are often tied to specific investment projects and they are classified as capital transfers.

8.4.1.6 Compensation for extensive damage

Finally, capital transfers also include major non-recurrent payments in compensation for extensive damage, such as from oil spills, or serious injury not covered by insurance policies. Large gifts and legacies such as those made to non-profit institutions (hospitals, universities) are also regarded as capital transfers.

8.4.2 Acquisitions of non-produced non-financial assets

Acquisitions of non-produced non-financial assets include natural resources and contracts, leases and licenses. The purchase of land in a foreign country by the Canadian government for purposes of constructing an embassy or military base is an example of an acquisition of natural resource assets. Contracts, leases and licenses are also recognized to be economic assets that might be traded internationally. For example, a Canadian company might purchase transferable rights to exploit natural resources abroad, or options to purchase goods in other countries or sub-leases of operational leases outside Canada. This kind of international transaction is not very common since the contracting, leasing or licensing enterprise generally has a presence in the country.[23]

8.5 The financial account

The financial account records transactions in financial assets and liabilities that occur between residents and non-residents. It measures the sources and uses of funds embodied in financial instruments. Transactions in financial instruments have a direct impact on the international investment position by creating, extinguishing or modifying financial assets and liabilities (see section 8.7). In turn, financial assets and liabilities generate investment income flows, which are recorded in the current account (see section 8.3.2). The financial account for 2009 is shown in Table 8.8.

Table 8.8
Financial account, 2009

	2009
	millions of dollars
Net lending / net borrowing, from financial account	**-47,564**
Net acquisition of financial assets	97,623
Direct investment assets	42,769
Canadian portfolio investment	8,732
Canadian portfolio investment, foreign debt securities	-7,186
Canadian portfolio investment, foreign money market instruments	1,844
Canadian portfolio investment, foreign bonds	-9,029
Canadian portfolio investment, foreign equity and investment fund shares	15,918
Official international reserves	11,617
Other Canadian investment	34,504
Other Canadian investment, loans	17,481
Other Canadian investment, currency and deposits	17,946
Other Canadian investment, trade credits and advances	-256
Other Canadian investment, other accounts receivable	-668
Net incurrence of liabilities	145,189
Direct investment liabilities	23,448
Foreign portfolio investment	112,726
Foreign portfolio investment, Canadian debt securities	86,480
Foreign portfolio investment, Canadian money market instruments	681
Foreign portfolio investment, Canadian bonds	85,799
Foreign portfolio investment, Canadian equity and investment fund shares	26,246
Other foreign investment	9,013
Other foreign investment, loans	-11,990
Other foreign investment, currency and deposits	13,185
Other foreign investment, special drawing rights	8,825
Other foreign investment, trade credits and advances	-588
Other foreign investment, other accounts payable	-419
Discrepancy (net errors and omissions)	**-556**

Source: Statistics Canada, table 36-10-0472-01.

Most transaction entries in the current and capital accounts are mirrored by corresponding entries in the financial account. For example, if the Government of Canada sends a Canada Pension Plan cheque to a non-resident, that payment would be recorded as a payment in the secondary income account and also as a reduction in resident currency and deposits assets in the financial account. However, the reverse is not generally true: many entries in the financial account are **not** mirrored by entries in the current and capital accounts. For example, a resident might purchase a U.S. government bond which would result in an increase in that resident's debt securities assets and a decrease in his currency and deposits assets, with no effect on the current or capital accounts. Another example would be if a resident corporation issued and sold new equity to non-residents, thereby increasing its currency and deposit assets and also increasing its equity liabilities.

The transactions in the financial account are presented on a net basis, unlike in the current and capital accounts where they are shown on a gross basis. This means that, on the asset side, acquisition of assets is netted against disposal of assets and, on the liability side, incurrence of liabilities is netted against redemption of liabilities. A plus sign denotes an increase in net investment and a negative sign a decrease in net investment.

For example, suppose the following transactions took place in a given accounting period:

- Mr. A purchased CAN$10,000 worth of bonds in the U.S.
- Mr. B purchased CAN$20,000 worth of bonds in the U.S.
- Mr. C purchased CAN$25,000 worth of bonds in Europe
- Mr. A sold CAN$15,000 worth of bonds in the U.S.
- Mr. D sold CAN$35,000 worth of bonds in Japan

This would be recorded in the financial account of Canada's balance of international payments as CAN$5,000 net investment in foreign bonds.

The currency (unit of account) in which a financial asset or liability is denominated is **not** relevant for determining the residence of the asset or liability holder. For example, if a Canadian resident opens a saving account at a Canadian bank and deposits U.S. dollars in the account this is not an international transaction. Rather, it is a domestic transaction involving foreign currency. When internationally traded assets and liabilities are denominated in a currency other than the Canadian dollar they are converted, for purposes of the international accounts, to Canadian dollar equivalents using prevailing exchange rates during the period. For this reason, fluctuations in exchange rates play a very important role in the BOP and IIP.

The classification system used in the financial account is based primarily on functional categories (direct investment, portfolio investment, reserve assets and other investment). However the financial account also provides statistics based on financial instrument categories (equity and investment fund shares, debt instruments such as bonds and money market instruments and other financial assets and liabilities such as loans, deposits and trade and non-trade credits). The different types of financial instruments in use in Canada are discussed in Chapter 6.

8.5.1 Direct investment

Among the major functional categories of financial asset acquisition, **direct investment** often receives special attention because, when compared to the other categories, it is most closely associated with the gaining of power and influence in other economies. Direct investment is closely associated with the phenomenon of **globalization**.

The concept of direct investment is a behavioural notion in that it purports to measure the investment by a resident enterprise, **a direct investor (DI)**, that has been made with the intent of having a significant influence in the affairs of a non-resident enterprise, a **direct investment enterprise (DIE)**, or vice versa. This concept is difficult to apply in practice. Canada retains, as prescribed by international standards, a rule of 10 per cent minimum ownership of voting equity when identifying a direct investment relationship.

The connection between the direct investor and the direct investment enterprise is referred to as a **direct investment relationship**. All enterprises that are under the control or influence of the same direct investor are considered to be part of a single direct investment relationship. In this context, **control** requires more than 50 per cent of the voting power in the enterprise while **influence** requires that the direct investor own equity equivalent to between 10 and 50 per cent of the voting power.

The determination of whether or not a direct investment relationship exists in a particular case can get rather complicated because control and influence can be exercised indirectly, through the control of a chain of other enterprises, as well as directly. The Framework for Direct Investment Relationships (FDIR) provides a disciplined structure of rules for identifying the extent and type of direct investment relationships.[24]

The direct investment flows that are recorded in the financial account include all transactions that occur directly between enterprises in different economies that are in a direct investment relationship. Direct investment flows into Canada are referred to as **inward direct investment**, or **Foreign Direct Investment in Canada (FDIC)**, while direct investment flows from Canada to other countries are called **outward direct investment**, or **Canadian Direct Investment Abroad (CDIA)**.

In this context, a **subsidiary** is defined to be a direct investment enterprise over which the director investor can exercise control, owning more than 50% of the voting equity of the DIE. **Branches**[25] which are normally wholly owned unincorporated enterprises are treated as subsidiaries. An **associate** is a direct investment enterprise over which the direct investor can exercise significant influence, owning between 10 and 50% of the voting equity, but not control. The **affiliates** of any enterprise consist of its direct investor(s), both immediate and indirect, its direct investment enterprises, whether subsidiaries, associates or subsidiaries of associates, both immediate and indirect, and its **fellow enterprises** which is to say those enterprises that are under the control or influence of the same immediate or indirect investor, with neither being an immediate or indirect investor in the other.

Direct investment covers all transactions in equity and debt between the direct investor and its direct investment enterprise. Equity comprises equity capital and reinvested earnings; debt comprises both long and short-term debt except for banks where these intercompany debt transactions are excluded and presented in 'other investment'.

Direct investors can be business enterprises, investment and pension funds, households, government organizations, international organizations, non-profit institutions serving households, estates or trustees. Direct investment enterprises by definition cannot be governments, households or international organisations.

When a direct investment enterprise lends funds to or acquires equity in its own immediate or indirect direct investor, **reverse investment** is said to have occurred as long as the direct investment enterprise does not own equity with 10 per cent or more of the voting power in the direct investor. In 2015 the financial account main presentation was modified to show these reverse investments based on an **asset-liability principle** (that is, on a gross basis) as opposed to a **directional principle** (that is, on a net basis) as had been the case previously in Canada. The difference between the two foreign direct investment conceptual presentations resides in the classification of reverse investments such as (1) Canadian affiliates' claims on foreign parents and (2) Canadian parents' liabilities to foreign affiliates. Under the asset/liability presentation,(1) is classified as assets and included in direct investment assets and (2) is classified as liabilities and included in direct investment liabilities. New terminology was introduced to represent this concept: **Canadian direct investment abroad** is now referred to as **direct investment assets** in the new presentation while **foreign direct investment in Canada** was renamed **direct investment liabilities**. Under the former directional principle presentation, (1) is still classified as foreign direct investment in Canada and (2) is classified as Canadian direct investment abroad. However when two enterprises each have 10 per cent or more of the voting power in the other, two **distinct direct investment relationships** are created as was the case previously.

International purchases and sales of land and any buildings on the land, or expenditures on natural resource exploration and development, are treated as direct investment flows. Recall that by the conventions of *SNA 2008* and *BPM6*, non-residents cannot directly own land and other capital assets. In such cases a notional resident institutional unit is created to own the assets and the non-resident is deemed to own the equity in the notional unit. Thus in principle, when a household in another country purchases a real asset in Canada, such as a house, while continuing to reside outside Canada, a notional enterprise is created in Canada to own the asset and the non-resident is deemed to own the equity associated with this notional institutional unit. In practice, presently available data sources do not permit such international transactions by households to be well identified.

Section 8.3.2.2.2 discusses the role of reinvested earnings as an imputed transaction flow in the current account. The counterpart to this transaction in the financial account is a corresponding imputed direct investment transaction flow.

Most of the data used to derive direct investment transactions originate from economic surveys of Canadian companies that are asked to consolidate all of their Canadian operations and accordingly are referred to as Canadian enterprises. A number of administrative and other data sources are also used from the Bank of Canada, the financial press, electronic business publications and company reports. Information collected by Statistics Canada under the authority of the *Corporations Returns Act*, which identifies ownership information on corporations, is also used to help identify the frame of enterprises involved in direct investment transactions.

Foreign direct investment statistics not only serve as a major input to the balance of international payments and the international investment position, but are also released as an annual stand-alone product showing inward and outward foreign direct investment positions by country and industry.

Detailed foreign direct investment statistics published annually by Statistics Canada also feed the coordinated direct investment survey[26] in which many countries including Canada participate, under the leadership of the International Monetary Fund. This database is used by many countries to assess foreign direct investment positions (and indirectly transactions) vis-à-vis what has been collected by counterpart countries. Canada's detailed foreign direct investment statistics are also provided to the financial directorate of the Organization for Economic Cooperation and Development and to the United Nations.

8.5.2 Portfolio investment

Portfolio investment embodies the notion of marketability, that is, of financial instruments that can be traded (bought or sold) on organized financial markets after they have been issued. In the Canadian statistics, portfolio investment covers transactions in stocks and bonds (both Canadian and foreign) and in Canadian money market instruments between Canadian residents and non-residents. However, it excludes the following: security transactions which are part of direct investment, as described section 8.5.1, foreign security transactions which are part of Canada's official international reserves (see section 8.5.3) and repurchase and reverse repurchase agreements on securities, which are classified as 'other investment' (section 8.5.4).

Transactions in securities comprise new issues, trade in outstanding securities (both sales and purchases), retirements of debt securities when they come to maturity and interest accrued on debt but not paid (inclusive of amortization of discounts or premiums and coupon interest).

Data on portfolio investment transactions, both by Canadian residents in other countries and by non-residents in Canada, are collected monthly via the international transactions in securities survey. This survey operates through questionnaires sent to agents, brokers and other intermediaries and also to a number of major institutional investors such as pension funds. Respondents to this survey send detailed transaction-level data to Statistics Canada that enable the compilation of a wealth of information related to international transactions in securities. Other administrative sources are used such as the Bank of Canada and commercial databases.

The coordinated portfolio investment survey,[27] administered by the International Monetary Fund, is also used to confront domestic holdings with the country of the issuer. While the survey is about stocks rather than flows, much is revealed about transaction flows by looking at the difference between successive holdings as reported in this survey.

An extensive and detailed system is used to process data on Canadian bonds and money market instruments. In the system, each Canadian issuer is identified by name, sector (federal government, private company name and so on) and industrial classification; each security held abroad is listed with the dates of issue and of maturity, the currency of issue, the interest rate, the timing of payments of interest and so on. Because the system is extensive in terms of the details maintained, it is used to derive a number of variables such as position, new issues, market values as well as interest and retirements. This all-encompassing system processes not only flows but also positions and investment income statistics. This system is being revamped to enhance functionality in order to meet evolving data demands, including those associated with the G-20 'data gaps' initiative.[28]

8.5.3 Official international reserves

Canada's **official international reserves** consist of foreign currency assets held by the Exchange Fund Account[29] plus Canada's reserve position at the International Monetary Fund.[30] These reserves are available for purposes of potential intervention in currency exchange markets, meeting balance of international payments financing needs and other related purposes. The reserve assets are of such a nature that they are readily acceptable as a means of payment by the central banks of other countries. They are denominated in convertible foreign currencies and they are readily and unconditionally available for use at any time. They may consist of currency and deposits, debt and equity securities, monetary gold, Canada's reserve position with the International Monetary Fund, Special Drawing Rights[31] holdings and other claims. By convention, official international reserves are usually expressed at market value in U.S. dollar terms, although their value is converted to Canadian dollars when they are recorded in the international accounts.

Some countries have enormous official international reserves—notably China which, at the end of 2016, had approximately US$3 trillion. Other countries with relatively large reserves include Japan, Switzerland and Saudi Arabia, although none of these approach the size of China's reserves. Canada's official international reserves were US$82 billion on March 31, 2016 consisting of US$67 billion of securities, US$5 billion of deposits, US$8 billion of Special Drawing Rights at the IMF and US$2 billion in Canada's reserve position with the IMF. Note that Canada no longer held gold in its official international reserves at the end of fiscal year 2015-2016.

The nature and composition of Canada's official international reserves are also discussed in Chapter 6, section 6.5.1.

8.5.4 Other investment

The **other investment** category in the financial account records the net acquisition of financial assets and the net incurrence of liabilities by residents vis-à-vis non-residents in the form of loans, currency and deposits, trade credits and advances and other accounts receivable or payable. In the case of the net incurrence of liabilities, the allocation of Special Drawing Rights to Canada, as an International Monetary Fund member, is also shown, with a corresponding entry under Special Drawing Rights in reserve assets.

Transactions in domestic currency in circulation between resident holders and non-residents are recorded in liabilities while transactions by resident holders with non-residents in foreign-issued currency are transactions in assets. Transactions in domestic liabilities between non-residents and transactions in foreign assets between residents are, of course, not recorded in the balance of international payments.

Table 8.8 shows the financial account for Canada in 2009 and Table 8.9 lists some additional tables with further statistics on items in the financial account. In 2009, Canada had net borrowing of $47,564 million from non-residents, according to the financial account. As shown in Table 8.2, net borrowing was $47,009 million based on the current and capital accounts so net errors and omissions were –$556 million. The net borrowing reflected the net acquisition of $97,623 million in financial assets and the net incurrence of $145,189 million in liabilities. The asset accumulation was the result of $42,769 million in net direct investment abroad, $8,732 million in net portfolio investment abroad, an $11,617 million buildup of official international reserve assets and net other Canadian investment abroad of $34,504 million. The net incurrence of liabilities was attributable to $23,448 million of net foreign direct investment in Canada, $112,726 million of net foreign portfolio investment and $9,013 million of net other foreign investment.

Table 8.9
Financial account, other breakdowns

Table number	Table title	Frequency	Availability
36-10-0471-01	Balance of international payments, financial account	annual	1981 to date
36-10-0025-01	Balance of international payments, flows of Canadian direct investment abroad and foreign direct investment in Canada	quarterly	First quarter 2007 to date
36-10-0026-01	Balance of international payments, flows of Canadian direct investment abroad and foreign direct investment in Canada, by North American Industry Classification System	quarterly	First quarter 2007 to date
36-10-0442-01	Balance of international payments, direct investment conceptual presentations	quarterly	First quarter 1990 to date
36-10-0027-01	Balance of international payments, Canadian chartered bank transactions in assets and liabilities booked in Canada with non-residents	quarterly	First quarter 1981 to date
36-10-0028-01	International transactions in securities, portfolio transactions in Canadian and foreign securities, by type of instrument and issuer	monthly	January 1988 to date
36-10-0029-01	International transactions in securities, portfolio transactions in Canadian and foreign securities, by type of instrument and issuer	quarterly	First quarter 1981 to date
36-10-0030-01	International transactions in securities, portfolio transactions in Canadian and foreign securities, by geographic area	monthly	January 1988 to date
36-10-0031-01	International transactions in securities, portfolio transactions in Canadian bonds, by type of issuer and transaction	monthly	January 1988 to date
36-10-0032-01	International transactions in securities, portfolio transactions in Canadian bonds, by currency of issue and type of transaction	monthly	January 1988 to date
36-10-0033-01	International transactions in securities, portfolio transactions in Canadian equity and investment fund shares, by type of transaction	monthly	January 1988 to date
36-10-0034-01	International transactions in securities, portfolio transactions in foreign bonds, by currency of issue	monthly	January 2005 to date
36-10-0035-01	International transactions in securities, loans under repurchase agreements, assets and liabilities, by type of instrument	monthly	January 1995 to date

Source: Statistics Canada.

8.6 The other changes in financial assets and liabilities account

The financial account together with the **other changes in financial assets and liabilities account** determine the change in the international investment position between the opening and closing of an accounting period. The latter account records ‘other flows’, which is to say changes in financial positions that are attributable to factors other than international transactions. In the financial account, transactions are recorded involving two accounting entries for each of the two parties to a transaction, while in the other changes in financial assets and liabilities account other flows involve just one entry for each party.

The other changes in financial assets and liabilities account includes the effects of revaluations and other changes in volume. It displays several kinds of other flows affecting financial assets and liabilities such as those attributable to:

- holding gains and losses due to exchange rate changes and other price changes,
- changes due to institutional units altering their economy of residence,
- reclassifications, including monetization and demonetization of gold bullion,
- changes in model assumptions relating to insurance reserves, pension entitlements and provisions of standardized guarantee schemes,
- unilateral debt cancellations and write-offs by a creditor, and
- uncompensated seizures of financial assets by governments.

As an example of how holding gains are treated in the account, suppose at the beginning of a period a Canadian investor holds 100 units of a U.S. exchange traded fund valued at US$10 dollars per unit for a total holding value of US$1,000. At the beginning of the period the Canadian dollar is at par with the U.S. dollar (CAN$1 = US$1). Suppose further that the Canadian investor purchases 10 more units of the fund during the period and that the unit purchase price increases to US$15 per unit. Moreover the Canadian dollar’s value decreases relative to the U.S. dollar during the period such that it costs CAN$1.10 to purchase US$1. In this example the investor’s position (assets held) at the beginning of the period is CAN$1,000 = US$1,000. At the end of the period the position is CAN$1,815 = US$1,650. Financial transactions, as recorded in the financial account, are CAN$165 = US$150. There are no other changes in volume during the period, but other changes in assets due to revaluation are CAN$650 = US$500. Thus the change in position between the end and beginning of the period, CAN$815 = US$650, is explained by the change in the financial account, CAN$165 = US$150, plus the change in the other changes in financial assets and liabilities account, CAN$650 = US$500. The revaluation change can be decomposed as CAN$100 due to exchange rate changes and CAN$550 due to other price changes.

In the Canadian balance of international payments, the effects of exchange rate valuations are calculated on a very detailed basis for every functional category and instrument that are denominated in foreign currencies.[32]

In Canada, the top-level aggregates of the other changes in financial assets and liabilities account are shown in table 36-10-0454-01, where they are derived by subtracting the financial account and the opening international investment position from the closing international investment position. In future the account will be made more explicit with a breakdown of its main component parts. This account is the mirror image of the other changes in assets account of the non-resident sector, which is discussed in Chapter 6.

8.7 The international investment position

Canada’s **international investment position (IIP)** is the statistical statement that presents the stock of financial assets and liabilities of its residents vis-à-vis non-residents. It records, at an instant in time, the value of the financial assets of residents that are claims on non-residents (including gold bullion held as reserve assets) and the value of liabilities of residents to non-residents. The difference between these asset and liability stocks is the Canada’s net international investment position.

As explained previously, the change in the IIP between the beginning and end of an accounting period is equal to the sum of financial transaction flows recorded in the financial account and other flows shown in the other changes in financial assets and liabilities account (refer to Figure 8.2). The IIP is based on the same general principles with respect to valuation, timing, units and the concept of residence that apply to the rest of the international accounts and SNA 2008 more generally.

The IIP can be viewed as a subset of the national balance sheet and is also discussed in Chapter 6.[33] It provides statistical information that is valuable for many kinds of analysis such as:

- monitoring Canada's external asset and debt position,
- assessing Canada's general economic relationships with the rest of the world,
- evaluating potential currency or debt maturity mismatches as between Canadian foreign assets and liabilities,
- examining the global geography of international assets and debts,
- studying the relationship between domestic and foreign sources of financing,
- calculating average rates of return on foreign assets and liabilities by instrument class, and
- reviewing Canada's balance of international payments sustainability and vulnerabilities.

Table 8.10 shows the IIP for 2009 (that is, as of December 31, 2009). Total assets were $2,067,092 million, total liabilities were $2,288,731 million and Canada's net international investment position was –$221,639 million, indicating a net indebtedness by Canadian residents to non-residents of that absolute amount. When a country's foreign assets are greater than its foreign liabilities that situation is referred to as a net asset position. In the opposite circumstance, with liabilities greater than assets, it is referred to as a net liability position or net debt position.

Table 8.10
International investment position, 2009

	2009
	millions of dollars
Total assets	**2,067,092**
Direct investment assets	979,409
Direct investment assets, equity	..
Direct investment assets, debt instruments	..
Canadian portfolio investment	645,272
Canadian portfolio investment, foreign debt securities	142,772
Canadian portfolio investment, foreign money market instruments	4,631
Canadian portfolio investment, foreign bonds	138,140
Canadian portfolio investment, foreign equity and investment fund shares	502,501
Official international reserves	57,129
Other Canadian investment	385,281
Other Canadian investment, loans	99,433
Other Canadian investment, currency and deposits	223,581
Other Canadian investment, trade credits and advances	7,169
Other Canadian investment, other accounts receivable	55,098
Total liabilities	**2,288,731**
Direct investment liabilities	953,379
Direct investment liabilities, equity	..
Direct investment liabilities, debt instruments	..
Foreign portfolio investment	940,629
Foreign portfolio investment, Canadian debt securities	570,506
Foreign portfolio investment, Canadian money market instruments	32,923
Foreign portfolio investment, Canadian bonds	537,583
Foreign portfolio investment, Canadian equity and investment fund shares	370,123
Other foreign investment	394,723
Other foreign investment, loans	64,434
Other foreign investment, currency and deposits	299,354
Other foreign investment, special drawing rights	10,224
Other foreign investment, trade credits and advances	7,619
Other foreign investment, other accounts payable	13,091
Canada's net international investment position	**-221,639**

.. not available for a specific reference period

Source: Statistics Canada, table 36-10-0485-01.

The presentation of the IIP in the table is by functional category—direct investment, portfolio investment, official international reserves and other investment—as recommended in *BPM6*. This classification also aligns with that of the financial account and the primary income account, thereby facilitating the calculation of investment-flow-to-stock ratios and income-to-stock ratios. IIP statistics can also be obtained with a variety of other breakdowns—by region, by industry for direct investment, by sector, by currency of issue, by maturity for debt instruments, by book versus market value—as shown in Table 8.11.

Table 8.11
International investment position, other breakdowns

Table number	Table title	Frequency	Availability
36-10-0008-01	Canadian direct investment abroad and foreign direct investment in Canada by country	annual	1987 to date
36-10-0009-01	Canadian direct investment abroad and foreign direct investment in Canada by North American Industry Classification System and region	annual	1999 to date
36-10-0469-01	Canada's gross external debt position by sector, book and market values	quarterly	Fourth quarter 2002 to date
36-10-0361-01	Canadian portfolio investment abroad at market value by country	annual	1997 to date
36-10-0368-01	Canadian portfolio investment abroad at market value by country	quarterly	First quarter 2013 to date
36-10-0443-01	Direct investment conceptual presentations	quarterly	First quarter 1990 to date
36-10-0474-01	International investment position book value	annual	1981 to date
36-10-0485-01	International investment position book and market values	quarterly	First quarter 1990 to date
36-10-0038-01	Portfolio and other investment in Canada by sector, book value	annual	1981 to date
36-10-0039-01	Portfolio and other investment in Canada by sector, book and market values	quarterly	First quarter 1990 to date
36-10-0486-01	Foreign portfolio investment in Canadian bonds and Canadian money market instruments, by geographic region	monthly	January 1991 to date
36-10-0475-01	Foreign portfolio investment in Canadian bonds and Canadian money market instruments, by currency of issue and sector	monthly	January 1991 to date
36-10-0444-01	Foreign portfolio investment in Canadian debt securities by remaining maturity and sector	monthly	January 2007 to date
36-10-0446-01	Canada's gross external debt position by currency	quarterly	Fourth quarter 2002 to date
36-10-0454-01	Change in Canada's international investment position, market value	quarterly	First quarter 2015 to date

Source: Statistics Canada.

The proper valuation of financial assets and liabilities in the IIP is sometimes a challenge. The aim is to value them at current market prices and this is readily done for listed equity and debt instruments that are regularly traded in financial markets. Non-negotiable financial instruments such as loans, deposits and accounts payable or receivable are recorded at their nominal values. However, for unlisted direct investment enterprises, private equity, joint ventures, listed but illiquid companies and unincorporated enterprises the determination of the current market valuation can be quite problematic.

In 2012, market value estimates of foreign direct investment were introduced in Canada's international accounts and market value aggregates became the main measure for the compilation of the international investment position.

A most widely-accepted methodology for creating market value estimates[34]—the market capitalization approach—was developed to produce market value estimates for foreign direct investment. This amounts to using capitalization ratios (market value over book value) derived from listed companies and applying these to the book value equity estimates of unlisted companies, with exceptions for specific cases such as small companies or companies in particular sectors. Moving equity to a market value basis provides a more accurate picture of the value of assets and liabilities of the international investment position. The switch from a book value to a market value measure has, in recent years, tended to move the net international investment position toward a larger net asset position.

8.8 Historical balance of international payments statistics

Canada's balance of international payments statistics program has existed for a long time, longer in fact than any other part of the Canadian system of macroeconomic accounts. This is discussed in Chapter 2.

The presentational format of the international accounts changed in 2012 to bring them in line with *SNA 2008* and *BPM6*. Unfortunately it was not possible to carry the changes back to the start of the time series in 1926. However, the old time series are still accessible and the tables in which they are available are listed in Table 8.12. As can be seen there, many annual current, capital and financial account time series are available from 1926 to 2011 and the quarterly statistics are available from 1946 forward. Annual international investment position statistics are also available on the old presentational format from 1926 to 2011.

Table 8.12
Selected historical balance of payments statistics

Table number	Table title	Frequency	Availability
36-10-0043-01	Balance of international payments, current account (archived)	annual	1926 to 2011
36-10-0045-01	Balance of international payments, current account (archived)	quarterly	First quarter 1946 to second quarter 2012
36-10-0047-01	Balance of international payments, current account, seasonally adjusted (archived)	quarterly	First quarter 1946 to second quarter 2012
36-10-0044-01	Balance of international payments, capital and financial account (archived)	annual	1926 to 2011
36-10-0046-01	Balance of international payments, capital and financial account (archived)	quarterly	First quarter 1946 to second quarter 2012
36-10-0048-01	Balance of international payments, current account, goods (archived)	annual	1946 to 2011
36-10-0049-01	Balance of international payments, current account, goods (archived)	quarterly	First quarter 1961 to second quarter 2012
36-10-0002-01	Balance of international payments, current account, investment income, by type and sector	annual	1926 to date
36-10-0055-01	Balance of international payments, flows of Canadian direct investment abroad and foreign direct investment in Canada, by category of transactions (archived)	annual	1946 to 2011
36-10-0058-01	International transactions in securities, portfolio transactions, net and gross sales and purchases, by type and sector (archived)	annual	1952 to 2011
36-10-0073-01	International investment position (archived)	annual	1926 to 2011
36-10-0075-01	International investment position, foreign portfolio investment in Canadian bonds and Canadian money market, by sector (archived)	annual	1955 to 2011
36-10-0076-01	International investment position, portfolio and other investment in Canada, by sector (archived)	annual	1926 to 2011
36-10-0079-01	Balance of international payments, flows of Canadian direct investment abroad and foreign direct investment in Canada, by industry and type of transactions (archived)	annual	1946 to 1993
36-10-0082-01	Net official financing from the official international reserves and the foreign currency borrowings of the Government of Canada (archived)	annual	1927 to 1996
36-10-0083-01	International investment position, capital employed in non-financial industries by country of ownership (archived)	annual	1926 to 1993
36-10-0095-01	International investment position, capital employed in non-financial industries, by country of control (archived)	annual	1926 to 1993

Source: Statistics Canada.

Annex A.8.1 Globalization and foreign affiliate statistics

Canadian companies are increasingly engaged in the global economy and as a result there is a growing demand for more detailed information on their international activities. As Canadian businesses expand across national borders and foreign businesses expand their activities in Canada, both through foreign direct investment, this brings a number of policy-related challenges on issues such as outsourcing jobs, competitiveness and export performance and how these relate to foreign affiliate sales.

Foreign affiliate statistics (FATS)[35] shed light on these issues by going beyond the traditional realm of cross-border foreign direct investment statistics to articulate the activities and financial positions of Canadian majority-owned affiliates operating abroad and foreign majority-owned affiliates operating in Canada.

FATS are an extension of statistics on foreign direct investment. They provide additional insight into the impact of foreign direct investment on economic agents in national economies in terms of earnings, productivity, employment, trade and foreign exposure resulting from an inter-connected global economy. They are not part of the balance of international payments as such because they are not, at least not primarily, about economic relationships between residents and non-residents. Rather, they are about the effects of those relationships, in terms of jobs, earnings and other variables.

There are two dimensions of FATS: First, there are activities and positions of foreign majority-owned affiliates in Canada, known as **inward** FATS; and, second, there are activities and positions of Canadian majority-owned affiliates abroad, known as **outward** FATS. In order to be consistent with the international practice for measuring FATS,[36] only the data for Canadian majority-owned foreign affiliates (MOFAs) and foreign majority-owned domestic affiliates (MODAs) are included. Sales and employment figures of such majority-owned affiliates are fully attributed—that is, there is no adjustment for less than 100 per cent ownership.

Selling goods or services through foreign majority-owned affiliates is a means for Canadian companies to market their products internationally and for foreign firms to market their products in Canada. In the case of goods, the products sold by majority-owned affiliates may be produced in Canada or produced abroad.

Statistics related to MOFAs are needed in relation to the negotiation and monitoring of trade and investment agreements. The statistics are also needed to meet Canada's statistical obligations to international organizations, such as the Organization for Economic Co-operation and Development. Canada has had a partial program of foreign affiliate statistics related to outward FATS since 2000.

For outward FATS, information is collected by Statistics Canada's annual Survey of Activities of Canadian Majority-Owned Affiliates Abroad. This survey currently measures sales of goods and services, employment and assets of Canadian MOFAs abroad and is conducted in conjunction with the Canadian Investment Abroad survey questionnaire. On the other hand, inward FATS statistics are a recent addition to the international accounts. The data are compiled by linking a variety of survey and administrative data[37] about each particular foreign majority-owned affiliate in Canada.

The FATS statistics are available in seven tables, as summarized in Table 8.13.

Table 8.13
Foreign affiliate statistics

Table number	Table title	Frequency	Availability
36-10-0470-01	Activities of Canadian majority-owned affiliates abroad, by countries	annual	2011 to date
36-10-0440-01	Activities of Canadian majority-owned affiliates abroad, by North American Industry Classification System	annual	2011 to date
36-10-0445-01	Activities of foreign majority-owned affiliates in Canada, by countries	annual	2010 to date
36-10-0447-01	Activities of foreign majority-owned affiliates in Canada, by North American Industry Classification System	annual	2010 to date
36-10-0451-01	Activities of foreign majority-owned affiliates in Canada, employment at establishment level, by province and the North American Industry Classification System	annual	2010 to date
36-10-0011-01	Foreign affiliate trade statistics, Canadian operations abroad, by North American Industry Classification System (archived)	annual	1999 to 2012
36-10-0012-01	Foreign affiliate trade statistics, Canadian operations abroad, by countries (archived)	annual	1999 to 2012

Source: Statistics Canada.

Statistics Canada's FATS program is relatively new and continues to develop and expand. The end goal is to produce additional variables and update on-going annual estimates for inward FATS that are tied to trade in goods and services as well as research and development, employment and financial characteristics in support of global production measures. For outward FATS, in addition to sales in goods and services, employment and total assets of the foreign affiliates, the introduction of other variables, such as value added will be evaluated. A broader framework is also being envisaged, to include Canadian parent enterprises and to link to trade by enterprise characteristics.

Annex A.8.2 International accounts releases and their linkages to other CSMA releases

The international accounts are disseminated through eight regular statistical releases which are:

- Monthly merchandise trade statistics
- Monthly international transactions in securities
- Quarterly balance of international payments
- Quarterly international investment position
- Annual international trade in services statistics
- Annual Canadian portfolio investment survey
- Annual foreign direct investment statistics
- Annual foreign affiliate statistics

These releases are tightly integrated with those for the other components of the CSMA. In particular, the monthly merchandise trade statistics and the quarterly balance of international payments align with the quarterly income and expenditure accounts and the annual supply and use accounts. The monthly international transactions in securities release and the quarterly balance of international payments also are consistent with the quarterly financial flow accounts. The quarterly international investment position statistics are fully consistent with the quarterly national balance sheet accounts.

Notes for chapter 8

1. Art Ridgeway participated on the committee from Canada. The manual is available free on the Internet and can be easily found by an Internet search for *BPM6*.

2. Note however that the current account balance was positive between 1999 and 2008.

3. *BPM6* observes (p. 133) that: “Despite the lending-oriented terms, net lending/net borrowing is a balance that takes into account equity, financial derivatives, and monetary gold, as well as debt instruments. Also, net lending includes reduction of liabilities and net borrowing includes reduction in assets.”

4. Steven Mozes and Diane Oberg, “U.S.-Canada Data Exchange, 1990-2001”, technical paper available on the Internet at https://www.census.gov/foreign-trade/aip/uscanada.pdf.

5. The Canada Revenue Agency requires that corporations file a T106 form when they engage in non-arm’s-length transactions with non-residents. The information on these forms is valuable for purposes of determining market valuation equivalent valuations.

6. **Allocated gold** is gold that is owned outright by the institutional unit. It may be stored for safekeeping in a bank, but it is not owned by the bank and is therefore safe from the bank’s potential insolvency. **Unallocated gold** is not the investor’s property. Rather, the investor owns a legal claim against another institutional unit to supply a given amount of gold on demand. If that other institutional unit goes bankrupt it may be unable to fulfill its liability

7. Concerns about survey respondent burden and survey cost preclude the collection of very detailed information.

8. The one year rule for travel services does not apply to students and medical patients. Their expenditures are included in travel services for the entire length of their stay outside their own economy.

9. In other words, business travel services exclude any purchases business travelers may make on behalf of the enterprises they represent. Purchased goods for resale or for use as intermediate inputs or for use as capital assets are included in goods trade.

10. Consumer durable goods and other purchases for own use valued in excess of the Customs threshold are excluded from travel services and included in goods trade.

11. Figure 5.1 entitled “Conventions for cross-border trucking of Canadian exports and imports of goods” on page 36 in the Statistics Canada publication *Canada’s Balance of International Payments and International Investment Position: Concepts, Sources, Methods and Products* provides a detailed picture of how transportation services are valued in Canada’s international accounts.

12. Purchasers of insurance typically pay their premiums in advance of the period during which the insurance applies. The insurance companies invest the premiums and earn investment income which is due to the policyholders. The policyholders, in turn, allow the insurance companies to retain these amounts as ‘premium supplements’.

13. If the persons receiving the payments are employees of the entity making the payments this is treated as compensation of employees rather than as trade in services.

14. Gambling includes a transfer element as well as a service element.

15. Quarterly volume indexes are available for both goods and services in table 36-10-0104-01. More detailed monthly and quarterly price and volume indexes for merchandise trade are available in tables 12-10-0003-01, 12-10-0004-01, 12-10-0006-01 through 12-10-0010-01 and 12-10-0087-01.

16. *BPM6*, page 183.

17. As a practical matter it may sometimes be difficult to allocate dividends to the accounting period when they become ‘ex dividend’. In such circumstances they are recorded in the period when they are paid.

18. This imputation in Canada’s international accounts is not present in Canada’s Financial Flow Accounts, so a reconciliation between the two is provided at the end of table 36-10-0578-01. For a discussion of reservations about this imputation see Arthur Ridgeway, “Dividends and Retained Earnings of Foreign Direct Investors: BOP and SNA Treatment in Canada,” a paper presented to the IMF Balance of Payments Committee, December 2003.

19. When migrants bring their own assets from their old economy to their new one this is not recorded as a transfer, but rather is recorded in the other changes in financial assets and liabilities account.

20. World Bank Group, *Migration and Remittances: Recent Developments and Outlook,* Migration and Development Brief 26, April 2016*.*

21. Global Affairs Canada, Statistical Report on International Assistance, Fiscal Year 2014-2015, available online at https://www.international.gc.ca/development-developpement/assets/pdfs/2014-15StatisticalReport-eng.pdf.

22. Debt forgiveness is to be distinguished from debt write-offs. The latter involves the involuntary cancellation of debt due to bankruptcy or other events. Debt write-offs are recorded in the other changes in financial assets and liabilities account as other (non-transaction) flows.

23. *SNA 2008* and *BPM6* also recognize marketing assets such as trademarks and corporate goodwill as types of non-produced non-financial assets in the capital account. However, these are not currently recognized in the Canadian capital account.

24. See Organization for Economic Cooperation and Development, *OECD Benchmark Definition of Foreign Direct Investment*, fourth edition, Annex 4. This volume is often referred to as *BD4*.

25. A branch is defined in section 8.3.1.2.3.2 in the context of trade in construction services.

26. For more information about the survey see International Monetary Fund, *Coordinated Direct Investment Survey Guide – 2015*, 2015, available free on the International Monetary Fund website.

27. For detailed information about the Coordinated Portfolio Investment Survey see International Monetary Fund, *Coordinated Portfolio Investment Survey Guide*, available free on the Internet.

28. The G-20 'Data Gaps' initiative was a result of a meeting of Group-of-20 finance ministers and central bank governors in April 2009. The purpose of the meeting was to review lessons learned from the international financial crisis in 2008. It was decided at the meeting to call upon the International Monetary Fund and the Financial Stability Board to identify major financial and economic information gaps needing to be filled. A set of 20 recommendations on the enhancement of financial and economic statistics were subsequently made.

29. The Exchange Fund Account is held in the name of the Minister of Finance. The status of the account is reported annually. See for example *Report on the Management of Canada's Official International Reserves, April 1, 2015 – March 31, 2016*, Government of Canada, catalogue number F1-31E-PDF, 2016.

30. IMF members are each assigned a quota, which must be deposited with the IMF. A country's reserve position at the IMF is the difference between that quota and the IMF's holdings of that country's currency.

31. Special Drawing Rights are a monetary reserve currency created by the International Monetary Fund in 1969. They are intended to add to international liquidity and are used by countries to supplement their other foreign exchange reserves. An SDR is a defined basket of national currencies. The contents of the basket and the weights of the currencies are changed from time to time. As of the end of 2016 the basket included the U.S. dollar (41.73%), the European euro (30.93%), the Chinese Renminbi (10.92%), the Japanese yen (8.33%) and the British pound (8.09%).

32. For a detailed example of exchange rate calculations see: *Canada's Balance of International Payments and International Investment Position, Concepts, Sources, Methods and Products*, Statistics Canada catalogue 67-506-X, 2000, p. 98. For a detailed explanation of the calculation of revaluations see also *BPM6*, paragraph 9.28, p. 146 and Box 9.1, p. 148.

33. Again, the non-resident sector part of the balance sheet accounts, as discussed in Chapter 6, records the assets of non-residents that are claims on Canadian residents and the liabilities of non-residents to Canadian residents. This is the mirror image of the IIP, which records the claims of Canadian residents on non-residents and the liabilities of Canadian residents to non-residents.

34. *BPM6* discusses these and other valuation methods on pp. 122 to 124.

35. *BPM6* refers to Activities of Multinational Enterprises (AMNE) statistics, which are closely related to but broader in scope than FATS. See appendix 4, pp. 269 to 271.

36. In addition to *BPM6*, see also *Recommendations Manual on the Production of Foreign Affiliates Statistics*, 2007 edition, Eurostat and the European Commission, Luxembourg, 2007.

37. It is a striking advantage of Statistics Canada's highly integrated business survey system that data for a particular business enterprise, on a wide variety of variables collected by numerous different surveys and administrative data systems, can be readily combined to paint a picture of that enterprise's activities without there being a need for additional survey collections.