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OECD Benchmark Definition of Foreign Direct Investment
Fourth Edition


*Chapter 4*

# FDI Components, Accounts and Scope

## 4.1. Summary

148. This chapter describes the components, accounts and scope of foreign direct investment (FDI).

149. Chapters 2and 3 both emphasized how it is only voting power, usually derived from owning voting equity, which is used to determine whether a direct investment relationship exists. However, once the relationship exists, measures of the direct investment between enterprises resident in different economies covered in the Framework for Direct Investment Relationship (FDIR) include all immediate equity and debt positions and transactions between the related parties.

150. The first part of this chapter discusses the components of FDI which cover the types of financial instruments involved in direct investment transactions/positions. This is followed by a discussion of the accounts which represent the three measures concerning FDI, *i.e.* foreign direct investment positions, FDI financial transactions and FDI income. Each of these three measures includes detailed accounts that serve as building blocks for FDI. These building blocks can be arranged in different presentations that will be explained in this chapter. A fourth account referred as the "other changes" account provides the link between the financial transactions and the positions.

151. The third part of this chapter discusses the scope of FDI in terms of the presentation of aggregated *versus* detailed FDI statistics and the differences concerning their coverage, inclusions and exclusions.

## 4.2. FDI components

152. The main financial instrument components of FDI are *equity* and *debt instruments* (see Box 4.1). *Equity* includes *common and preferred shares* (exclusive of non-participating preference shares which should be included under debt), *reserves*, capital contributions and *reinvestment of earnings*. All cross-border positions and transactions in equity between FDI-related enterprises (see Chapter 3) are included in FDI. *Dividends*, distributed branch earnings, *reinvested earnings* and *undistributed branch earnings* are components of FDI income on equity.

153. Debt instruments include marketable securities such as bonds, debentures, commercial paper, promissory notes, non-participating preference shares and other tradable non-equity securities as well as loans, deposits, trade credit and other accounts payable/ receivable. All cross-border positions and transactions related to these instruments, between enterprises covered by an FDI relationship other than between related financial intermediaries are included in FDI. The interest returns on the above instruments are included in FDI income on debt.

154. Positions and transactions in financial derivatives between entities in a direct investment relationship should be excluded from direct investment.

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155. Direct investment assets and liabilities for both equity and debt can be further classified by the nature of the relationship between the resident and non-resident FDI counterpart to the FDI position or transaction.

- *Direct investment assets* can be ascribed to the following three categories:
  - *i)* investment by a resident direct investor in its non-resident direct investment enterprises;
  - *ii)* reverse investment by a resident direct investment enterprise in its non-resident direct investor(s);
  - *iii)* investment by a resident fellow enterprise in non-resident fellow enterprises.
- *Direct investment liabilities* can be ascribed to the following three categories:
  - *i)* investment of non-resident direct investor in resident direct investment enterprises;
  - *ii)* reverse investment of non-resident direct investment enterprises in resident direct investors;
  - *iii)* investment of non-resident fellow enterprises in resident fellow enterprises.

156. These three categories of assets and liabilities lead to the classes and sub-classes itemised in the account presentations that follow. These categories are useful for analysis. In the first category, the financing flows in the same direction as the influence or control, from the direct investor to the direct investment enterprise. This is in line with the core principle for direct investment that a direct investor acquires influence or control through the provision of financing.

157. In the second category *reverse investment*, financing flows in the opposite direction as the influence or control. This category reflects the reverse of the standard FDI financing flows as the direct investor uses its influence to have its direct investment enterprises provide equity or debt financing for its own operations (see Section 4.3 for further details). Such investments, defined as *reverse investments,* are limited to cases where the acquisition of voting power by a direct investment enterprise in its direct investor does not meet the 10% criterion for establishing a separate direct investment relationship in its own right.

158. The last category shows financing involving fellow enterprises that have no direct investment influence upon one another (*i.e.* the 10% voting power criterion is not met as there is not sufficient equity ownership in each other) but have a common parent.

159. Reinvested earnings and reinvestment of earnings are separately identified components of equity in the *FDI income account* and in the *FDI transactions account* respectively. These flows are identified only between the direct investment enterprise and its immediate direct investors (although the value of these flows should reflect income earned from directly and indirectly owned direct investment enterprises through the current operating performance concept, see Annex 6). In cases where the equity asset holder has less than 10% voting power (*reverse investment* and investment in fellow enterprises), reinvested earnings and reinvestment of earnings are not recorded.

160. In summary direct investment equity and debt are *a)* financing provided by a direct investor to a directly or indirectly owned direct investment enterprise or *b)* financing received from a directly or indirectly owned direct investment enterprise by a direct investor or *c)* financing provided by or to fellow enterprises.

Box 4.1. **Financial instruments related to foreign direct investment**

***Equity:*** Comprises: *i)* equity in branches; *ii)* all shares in subsidiaries and associates (except non-participating, preferred shares that are treated as debt securities and included under direct investment, debt instruments); and *iii)* other contributions of an equity nature. Ownership of equity is usually evidenced by shares, stocks, participations, depositary receipts or similar documents. Shares and stocks have the same meaning while depositary receipts are securities that represent ownership of securities by a depositary. This category includes proprietors' net equity in quasi-corporations, as well as shares and equity in corporations. It also includes preferred stocks or shares that provide for participation in the residual value on dissolution of an incorporated enterprise. Reinvestment of earnings comprises the claim of direct investors (in proportion to equity held) on the retained earnings of direct investment enterprises. Reinvestment of earnings represents financial account transactions that contribute to the equity position of a direct investor in a direct investment enterprise.

***Deposits:*** Typical forms of deposits include savings deposits, term deposits, transferable and non-transferable deposits in local or foreign currencies (see the SNA guidelines for a more specific definition of deposits).

***Debt securities:*** Include non-participating preferred shares, bonds, debentures, commercial paper, promissory notes and other non equity securities.

***Loans:*** Loans are financial assets that are created when a creditor lends funds directly to a debtor through an instrument that is not intended to be traded. This category includes all loans and advances (except accounts receivable/payable which are treated as a separate category of financial assets). It also covers the treatment of financial leases and repurchase agreements.

***Trade credit (receivables and payables)*** between FDI related enterprises. It represents short-term credit in the ordinary course of business by suppliers/buyers of goods and services. These credits are registered from the time the goods or services are provided until payment is received (or *vice versa*).

***Other accounts receivable/payable*** includes advances and deferred payments in respect of exchange of non-produced assets.

*Note:* Financial derivatives are not included in direct investment.

161. Within *reverse investment*, direct investment enterprises may raise loans which they on-lend to their direct investor, or may make loans to their direct investor from their own resources, so-called reverse investment. Such loans should be treated as direct investment debt and be included in the direct investment statistics. Similarly, loans involving fellow enterprises should be included under *debt* in direct investment statistics.

162. It is important to stress that all debt transactions and positions directly between two financial intermediaries within a direct investment relationship should be excluded from direct investment statistics (see Section 4.4.3 Banks and other financial intermediaries).

163. Direct investors may make loans to or borrow funds from their indirectly owned direct investment enterprises. An indirect ownership interest exists when a direct investment enterprise that is directly owned, in turn, has an equity holding in another non-resident direct investment enterprise, thereby making the first direct investment enterprise a direct investor in the second direct investment enterprise. In this example, the direct investor at the top of the ownership chain holds an indirect ownership interest in the

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enterprise at the bottom of the ownership chain. Transactions and positions between all these directly and indirectly owned enterprises should be included in direct investment if they meet the requirements of the FDIR (see Section 3.4.3).

164. Under the FDIR, if the indirect ownership in direct investment enterprises is not included in direct investment relationships, some transactions/positions between the direct investor and its indirectly owned direct investment enterprises may be excluded from the direct investment statistics as well as the corresponding earnings. Economies which do not require their companies to produce world-wide consolidated company accounts may have difficulties in obtaining information on all indirectly owned subsidiaries and associates in order to produce direct investment statistics according to FDIR.

165. A direct investment enterprise or a fellow enterprise may also have loans or balances due to or from fellow enterprises abroad. None of these related enterprises needs to hold a 10% or more voting power in the other as long as they have directly or indirectly a common parent.

166. As a result, financial transactions and positions between an enterprise and its fellow enterprise, both included in the FDIR, are part of FDI, even though there may be no equity participation between them. For example, B, a direct investment enterprise of A, may raise funds which, under instructions from A, it lends to C, another direct investment enterprise of A. Such transactions/positions should be considered direct investment between the economy of B and the economy of C, even though there is no equity participation between B and C. Similarly, if a resident direct investor, A, has a direct investment enterprise abroad, B, as well as a resident subsidiary, C, then C is, by definition, not a direct investment enterprise of A, but B and C are fellow enterprises within the FDIR covering A, B, and C. Therefore, transactions between B and C should be recorded as direct investment.

## 4.3. FDI accounts

167. The main accounts for presenting FDI statistics are *FDI positions*, *FDI transactions* and *FDI income*. These accounts are described below along with a description of other changes that may impact on the value of FDI positions and transactions.

168. Building on the three categories of assets and liabilities and the descriptions of the previous section, six classes of direct investment *assets* and six classes of direct investment *liabilities* can be defined that will serve as the building blocks for the presentations of FDI statistics described in this section. These building blocks are consistent with the information requirements of earlier editions of the *Benchmark Definition*. The classes of assets and liabilities in or to fellow enterprises are further subdivided into two sub-classes according to the residence of the ultimate controlling parent (UCP), *i.e.* the direct investor at the top of the control chain.

- *Direct investment assets*: (FDI assets = A1 + A2 + A3 + A4 + A5 + A6).
  - ❖ A1: Equity assets of direct investors in direct investment enterprises.
  - ❖ A2: Debt instrument assets of direct investors in direct investment enterprises.
  - ❖ A3: Equity assets of direct investment enterprises in their direct investors (reverse investment).
  - ❖ A4: Debt instrument assets of direct investment enterprises in their direct investors (reverse investment).

- ❖ A5: Equity assets in fellow enterprises abroad.
  - A5.1: If ultimate controlling parent is resident.
  - A5.2: If ultimate controlling parent is non-resident.
- ❖ A6: Debt instrument assets in fellow enterprises abroad.
  - A6.1: If ultimate controlling parent is resident.
  - A6.2: If ultimate controlling parent is non-resident.

- *Direct investment liabilities*: (FDI liabilities = L1 + L2 + L3 + L4 + L5 + L6).
  - ❖ L1: Equity liabilities of direct investment enterprises to direct investors.
  - ❖ L2: Debt instrument liabilities of direct investment enterprises to direct investors.
  - ❖ L3: Equity liabilities of direct investor to their direct investment enterprises (reverse investment).
  - ❖ L4: Debt instrument liabilities of direct investor to their direct investment enterprises (reverse investment).
  - ❖ L5: Equity liabilities to fellow enterprises abroad.
    - L5.1: If ultimate controlling parent is non-resident.
    - L5.2: If ultimate controlling parent is resident.
  - ❖ L6: Debt instrument liabilities to fellow enterprises abroad.
    - L6.1: If ultimate controlling parent is non-resident.
    - L6.2: If ultimate controlling parent is resident.

169. These building blocks are based on balance sheet entries of direct investors, direct investment enterprises and fellow enterprises.

170. Each of these classes can be also classified by the industrial activity and residence of the counterparties. Discussion of these dimensions is covered in Chapter 7.

171. These building blocks can be arranged in different presentations suitable for a variety of analytical requirements. Macroeconomic accounts, balance of payments and the national accounts present financial data primarily on an asset and liability basis. Thus, FDI data on this basis are useful when analysing direct investment in relation to other macroeconomic variables of the external sector of the economy. In addition, most FDI data are compiled as part of the balance of payments programs in each country, bridging macroeconomic accounts and other presentations of FDI statistics.

172. The *Benchmark Definition* also calls, as prescribed in its earlier editions, for the presentation of FDI statistics according to the directional principle which requires the rearrangement of some of these building blocks. Data presented on the basis of the directional principle are better suited for some types of analysis. In particular it is the preferred presentation for industry and country data described later in this *Benchmark Definition*. Under the directional principle, when the direct investment enterprise holds less than 10% of the voting power in its direct investor, any reverse investment (either equity or debt) from the direct investment enterprise to its direct investor is to be accounted for under outward or inward FDI (as appropriate) as opposed to the asset/liability equivalent.

173. Similarly, recording of transactions and positions between fellow enterprises under the directional principle (categories A5, A6 and L5, L6) is to be made as appropriate by transposing where necessary their asset/liability equivalents to provide the directional information. This generally results in overall outward and inward FDI statistics being lower

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in magnitude than those presented on an asset/liability basis (but cases can arise where the opposite occurs). In order to apply the directional principle as presented in the exhibits below, the recording of direct investment between fellow enterprises (*i.e.* where they are covered by the FDIR) is to be presented according to the residence of the immediate counterpart but the direction of the investment is to be determined according whether the ultimate controlling parent is a "resident" or a "non-resident" of the compiling economy. In other words, if the ultimate controlling parent is not a resident of the compiling economy, all transactions and positions between the fellow enterprises are classified as inward FDI. If the ultimate controlling parent is resident in the compiling economy, all transactions and positions between that fellow enterprises are classified as outward FDI. Once the direction of the transaction/position is determined, in either case, the geographical allocation should be made on the basis of the location of the immediate counterparts.

### *4.3.1. FDI positions*

174. For FDI positions, investment is disaggregated into equity and debt instruments; the accumulation of reinvestment of earnings (or the closing balance of retained earnings in proportion to the equity held) is not recorded separately in positions data as it is included in the overall calculation of "equity" when recorded at market value.

175. Exhibits 4.1 and 4.2 below are included to illustrate how these building blocks are used to construct the various measures of FDI that are required. These illustrations may be different to the standard and supplemental presentations for reporting FDI statistics which are described in Annex 2.

176. To illustrate the asset/liability approach, the six classes presented above are to be grouped as follows:

Exhibit 4.1. **FDI positions according to the asset/liability principle**

| Assets | Liabilities |
|---|---|
| Of *direct investors in direct investment enterprises* | *Of direct investment enterprises to direct investors* |
| **A1.** Equity | **L1.** Equity |
| **A2.** Debt instruments | **L2.** Debt instruments |
| *Of direct investment enterprises in direct investors (reverse investment)* | *Of direct investor to direct investment enterprises (reverse investment)* |
| **A3.** Equity | **L3.** Equity |
| **A4.** Debt instruments | **L4.** Debt instruments |
| *In fellow enterprises* | *To fellow enterprises* |
| **A5.** Equity | **L5.** Equity |
| A5.1. If ultimate controlling parent is resident | L5.1. If ultimate controlling parent is non-resident |
| A5.2. If ultimate controlling parent is non-resident | L5.2. If ultimate controlling parent is resident |
| **A6.** Debt instruments | **L6.** Debt instruments |
| A6.1. If ultimate controlling parent is resident | L6.1. If ultimate controlling parent is non-resident |
| A6.2. If ultimate controlling parent is non-resident | L6.2. If ultimate controlling parent is resident |

177. As mentioned already in this *Benchmark Definition*, two terms are used in presenting FDI statistics according to the directional principle: *Outward FDI* and *Inward FDI*. Outward FDI includes the net assets of resident enterprises exerting control or influence on non-resident enterprises (net assets of resident direct investors and net assets in fellow enterprises abroad when the UCP is resident). Inward FDI includes the net liabilities of resident enterprises controlled or influenced by non-resident enterprises (net liabilities of resident direct investment enterprises to direct investors and net liabilities to fellow

enterprises abroad when the UCP is non-resident). The components of outward and inward FDI are schematically shown as follows:

Exhibit 4.2. **FDI positions according to the directional principle**

| Outward foreign direct investment | Inward foreign direct investment |
|---|---|
| *Outward equity position:* | *Inward equity position:* |
| **A1.** Equity assets of DI in DIE | **L1.** Equity liabilities of DIE to DI |
| **– L3.** Equity liabilities of DI to DIE* (reverse investment) | **– A3.** Equity assets of DIE in DI* (reverse investment) |
| **A5.1.** Equity assets in fellow enterprises abroad *(if ultimate controlling parent is resident)* | **L5.1.** Equity liabilities to fellow enterprises abroad *(if ultimate controlling parent is non-resident)* |
| **– L5.2.** Equity liabilities to fellow enterprises abroad* *(if ultimate controlling parent is resident)* | **– A5.2.** Equity assets in fellow enterprises abroad* *(if ultimate controlling parent is non-resident)* |
| *Outward debt instruments position:* | *Inward debt instruments positions:* |
| **A2.** Debt instruments assets of DI in DIE | **L2.** Debt instruments liabilities of DIE to DI |
| **– L4.** Debt instruments liabilities of DI to DIE* (reverse investment) | **– A4.** Debt instruments assets of DIE in DI* (reverse investment) |
| **A6.1.** Debt instruments assets in fellow enterprises abroad *(if ultimate controlling parent is resident)* | **L6.1.** Debt instruments liabilities to fellow enterprises abroad *(if ultimate controlling parent is non-resident)* |
| **– L6.2.** Debt instruments liabilities to fellow enterprises abroad* *(if ultimate controlling parent is resident)* | **– A6.2.** Debt instruments assets in fellow enterprises abroad* *(if ultimate controlling parent is non-resident)* |

* Entered as a deduction in outward or inward FDI.

178. FDI asset positions under the asset/ liability principle are (generally) greater than FDI outward positions calculated according to the directional principle. In the same manner, FDI liability positions under the asset/liability principle are (generally) greater than the FDI inward positions calculated according to the directional principle. The difference between the two presentations is equal to the sum of the assets of residents in non-residents when the residents are controlled or influenced by non-residents (either directly in the case of reverse investments or ultimately for positions with fellow enterprises) and of the liabilities of residents to non-residents when the residents are exerting control or influence on non-residents (either directly in the case of reverse investments or ultimately for positions with fellow enterprises). Comparing the two presentations as follows:

179. The difference between the asset position and the outward FDI position is equal to:

$$(A1 + A2 + A3 + A4 + A5 + A6) – (A1 – L3 + A5.1 – L5.2 + A2 – L4 + A6.1 – L6.2)$$

which simplifies to

$$\mathbf{A3 + A4 + A5.2 + A6.2 + L3 + L4 + L5.2 + L6.2.}$$

- The difference between the liability position and the inward FDI position is equal to:

$$(L1 + L2 + L3 + L4 + L5 + L6) – (L1 – A3 + L5.1 – A5.2 + L2 – A4 + L6.1 – A6.2)$$

which simplifies to

$$\mathbf{A3 + A4 + A5.2 + A6.2 + L3 + L4 + L5.2 + L6.2.}$$

180. The net position (outward FDI *less* inward FDI and assets *less* liabilities) is the same for both presentations; *i.e.*, the difference between FDI assets and FDI liabilities is equal to the difference between outward FDI and inward FDI.

#### *4.3.1.1. Equity position*

181. Equity positions cover all components of shareholders' funds (proportionate to the percentage of shares held). They, therefore, include equity, contributed surplus, reinvestment of earnings, revaluations, as well as any reserve accounts (Exhibit 4.1,



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items A1 and L1). Reinvestment of earnings is not recorded for either reverse investment (items A3, L3) or for investment between fellow enterprises (items A5 and L5) where neither party holds 10% or more of the voting power in one another. The reason for not imputing reinvested earnings/reinvestment of earnings in these cases is that, as these parties do not have at least 10% of voting power in the other, none of them can exert influence over the earnings distribution policy of the enterprise. Reinvested earnings/ reinvestment of earnings apply only between a direct investment enterprise and its immediate direct investor.

182. As noted earlier, equity positions may arise from reverse investment, which occurs when a direct investment enterprise acquires an equity or debt claim on its direct investor without holding 10% or more of the voting power. In addition, as stated above, items A3, A5 and L3, L5 consist solely of equity capital, *i.e.*, reinvestment of earnings is excluded when the level of the equity investment is less than 10% of the voting securities of the direct investor. This exclusion would apply only if equity investment is recorded at book value. Since the *Benchmark Definition* recommends market value as the valuation of FDI positions, in principle this differentiation does not apply. In instances where a direct investment enterprise, holding less than 10% of the voting power in its direct investor, increases that voting power to 10% or more, the direct investment enterprise becomes, in its own right, a direct investor and a separate direct investment relationship is established with its direct investor. Similarly, when a fellow enterprise, holding less than 10% of the voting power in a non-resident fellow enterprise, increases that voting power to 10% or more, the acquiring enterprise becomes a direct investor in the foreign affiliate. How these transactions and the related changes in FDI positions are to be recorded is discussed further below (see Section 4.3.4.5).

183. It should therefore be emphasised that where a resident direct investment enterprise acquires a 10% or more voting power interest in its direct investor or in a fellow enterprise resident in a different economy, it is not treated as reverse (equity) investment in the first case but rather as a direct investment asset (item A1) in both cases, as the threshold of 10% of voting power has been reached to create a direct investor. Similarly, where a FDI enterprise holds 10% or more of the voting power of the resident direct investor or in fellow enterprises resident in different economies than itself, the investment should be recorded as direct investment liabilities (item L1) by the economies receiving the investment, as, by reaching 10% of the voting power in the resident enterprise, the non-resident enterprise itself becomes a direct investor.

#### *4.3.1.2. Debt instruments positions*

184. Inter-company accounts should be separately recorded for assets and liabilities. Debt positions include payables and receivables between enterprises in a direct investment relationship arising from loans, deposits, debt securities, suppliers' (trade) credit, financial leases, and non-participating preference (preferred) shares.[28] However, debt positions between FDI related financial intermediaries (such as commercial banks, savings institutions, credit unions, mutual funds or finance companies) are excluded from direct investment (though this exclusion does not apply if one of the parties is a holding company). The reason for this is that they are taken to represent "normal banking-type

28. Positions in derivative financial instruments are excluded, as they are not considered to be part of direct investment.

business", so that their very nature is quite different from that of other direct investment enterprises. Consequently, it is felt that the inclusion of debt instruments between such related financial intermediaries would produce misleading results.

185. For assets, positions should be recorded separately for the various debt instruments that:

- the resident direct investor holds in its direct investment enterprises;
- the resident direct investment enterprise holds on its direct investor(s);
- the resident fellow enterprises hold in other fellow enterprises abroad.

186. For liabilities, positions should be separately recorded for the various debt instruments that:

- the resident direct investment enterprise issues to its direct investor(s);
- the resident direct investor issues to its direct investment enterprise(s);
- the resident fellow enterprises issue to other fellow enterprises abroad.

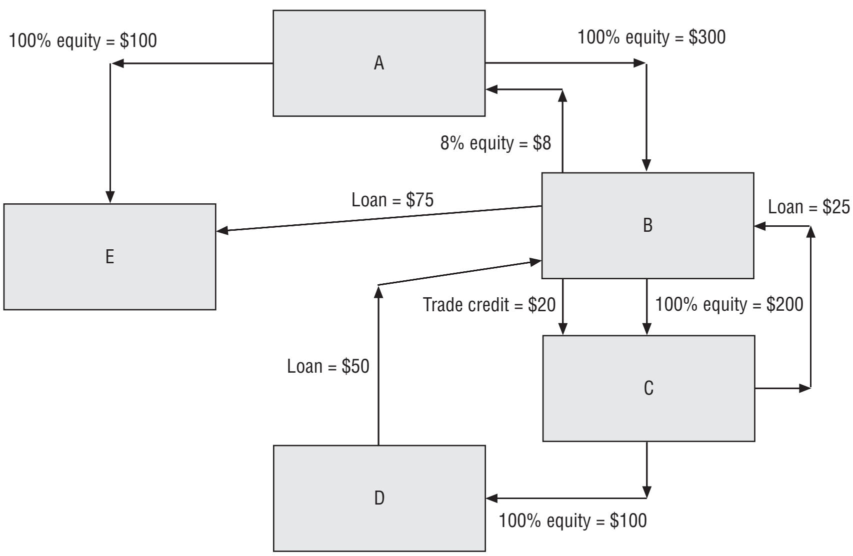
### *4.3.1.3. Changes in direct investment positions*

187. Direct investment positions may change either due to transactions or due to other changes. Transactions arise when parties of two different economies buy, sell, borrow, or lend to one another, and when a resident in one economy provides (or receives) something of value to (from) a resident in another economy by agreement. Other changes in direct investment positions resulting from changes in foreign currency exchange rates, debt being written off and other types of holding gains or losses are examples of items that should be recorded as appropriate in the Other Changes' account. See Section 4.3.4 for a further description of this category.

### *4.3.1.4. Reconciliation of presentations according to the "asset/liability " and the "directional" principles: A numerical example*

188. The numerical example in the figure below illustrates the differences in FDI presentations moving from the asset liability/principle to the directional principle:

**In this example each of the enterprises A through E is in a different economy:**



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**Taking B as the reporting economy:**

### Asset liability principle: *Net FDI liability position: $72*

| Assets | $303 | Liabilities | $375 |
|---|---|---|---|
| ***Of direct investors in direct investment enterprises*** | | ***Of direct investment enterprises to direct investor*** | |
| **A1.** Equity | | **L1.** Equity | |
| Equity in C | $200 | Equity from A | $300 |
| **A2.** Debt instruments | | **L2.** Debt instruments | |
| Trade Credit in C | $20 | | |
| ***Of direct investment enterprises in direct investor – Reverse investment*** | | ***Of direct investor to direct investment enterprises – Reverse investment*** | |
| **A3.** Equity | | **L3.** Equity | |
| Equity in A | **$8** | | |
| **A4.** Debt instruments | | **L4.** Debt instruments | |
| | | Loan from C | $25 |
| | | Loan from D | **$50** |
| ***In fellow enterprises*** | | ***To fellow enterprises*** | |
| **A5.** Equity | | **L5.** Equity | |
| **A6.** Debt instruments | | **L6.** Debt instruments | |
| **A6.2.** Loan to E | **$75** | | |

### Directional principle: *Net inward FDI position: $72*

| Outward foreign direct investment | 145 | Inward foreign direct investment | 217 |
|---|---|---|---|
| ***Outward equity position:*** | | ***Inward equity position:*** | |
| **A1.** Equity assets of DI in DIE | 200 | **L1.** Equity liabilities of DIE to DI | 300 |
| **– L3.** Equity liabilities of DI to DIE | | **– A3.** Equity assets of DIE in DI | **–8** |
| **A5.1.** Equity assets in fellow enterprises *(if ultimate controlling parent is resident)* | | **L5.1.** Equity liabilities to fellow enterprises *(if ultimate controlling parent is non-resident)* | |
| **– L5.2.** Equity liabilities to fellow enterprises *(if ultimate controlling parent is resident)* | | **– A5.2.** Equity assets in fellow enterprises *(if ultimate controlling parent is non-resident)* | |
| ***Outward debt instruments position:*** | | ***Inward debt instruments positions:*** | |
| **A2.** Debt instruments assets of DI in DIE | 20 | **L2.** Debt instruments liabilities of DIE to DI | |
| **– L4.** Debt instruments liabilities of DI to DIE | –25<br>–50 | **– A4.** Debt instruments assets of DIE in DI | |
| **A6.1.** Debt instruments assets in fellow enterprises *(if ultimate controlling parent is resident)* | | **L6.1.** Debt instruments liabilities to fellow enterprises *(if ultimate controlling parent is non-resident)* | |
| **– L6.2.** Debt instruments liabilities to fellow enterprises *(if ultimate controlling parent is resident)* | | **– A6.2.** Debt instruments assets in fellow enterprise *(if ultimate controlling parent is non-resident)* | **–75** |

- The same component entries appear in both accounts but the entries shown as negative amounts in the directional table correspond to the relevant positive entries on the opposite side of the asset/liability table.
- Gross values of assets and liabilities are presented.
- In both presentations net FDI is the same ($72).

*Under the directional principle:*

- The reverse investment asset position with A effectively reduces the the aggregate headline inward FDI position of B (it is netted out).
- There is a negative inward FDI debt liability position into E resulting from the recording of loans with fellow enterprises (as the ultimate controlling parent of "B" is non-resident). This also reduces the aggregate headline inward FDI position of B.

- The outward FDI position is effectively reduced as a result of the recording of the reverse investment loans from C and D (as in the preceding edition of the *Benchmark Definition*).

*Under the asset/liability principle:*

- There is an asset position with A that contributes to the gross total.
- There is a liability position with C that contributes to the gross total.
- The notion of inward and outward FDI is replaced by the notion of FDI asset and FDI liability.

### *4.3.2. FDI financial transactions*

189. Direct investment transactions are all transactions between direct investors, direct investment enterprises, and/or other fellow enterprises. In the case of transactions the Equity Asset and Liability classes A1 and L1 are further subdivided into two sub-components:

A1: Equity assets of direct investors in direct investment enterprises

A1.1. Equity transactions

A1.2. Reinvestment of earnings

L1: Equity liabilities of direct investment enterprises to direct investor

L1.1. Equity transactions

L1.2. Reinvestment of earnings

190. It is recommended that separate figures be collected and published for transactions in equity capital, reinvestment of earnings and debt for both direct investment assets and direct investment liabilities.

191. For transactions, the asset/liability principle is schematically shown as follows:

Exhibit 4.3. **Foreign direct investment transactions according to the asset/liability principle**

| Transactions in assets | Transactions in liabilities |
|---|---|
| ***Of direct investors in direct investment enterprises*** | ***Of direct investment enterprises to direct investors*** |
| **A1.** Equity | **L1.** Equity |
| **A1.1.** Equity transactions | **L1.1.** Equity transactions |
| **A1.2.** Reinvestment of earnings | **L1.2.** Reinvestment of earnings |
| **A2.** Debt instruments | **L2.** Debt instruments |
| ***Of direct investment enterprises in direct investors- Reverse investment*** | ***Of direct investors to direct investment enterprises – Reverse investment*** |
| **A3.** Equity | **L3.** Equity |
| **A4.** Debt instruments | **L4.** Debt instruments |
| ***In fellow enterprises*** | ***To fellow enterprises*** |
| **A5.** Equity | **L5.** Equity |
| **A5.1.** If ultimate controlling parent is resident | **L5.1.** If ultimate controlling parent is non-resident |
| **A5.2.** If ultimate controlling parent is non-resident | **L5.2.** If ultimate controlling parent is resident |
| **A6.** Debt instruments | **L6.** Debt instruments |
| **A6.1.** If ultimate controlling parent is resident | **L6.1.** If ultimate controlling parent is non-resident |
| **A6.2.** If ultimate controlling parent is non-resident | **L6.2.** If ultimate controlling parent is resident |

192. To illustrate the directional principle for transactions, the FDI elements are schematically shown as follows:

Exhibit 4.4. **Foreign direct investment transactions according to the directional principle**

| Outward foreign direct investment | Inward foreign direct investment |
|---|---|
| ***Outward equity transactions*** | ***Inward equity transactions*** |
| **A1.** Equity assets of DI in DIE | **L1.** Equity liabilities of DIE to DI |
| **A1.1.** Equity transactions | **L1.2.** Equity transactions |
| **A1.2.** Reinvestment of earnings | **L1.2.** Reinvestment of earnings |
| **– L3.** Equity liabilities of DI to DIE(reverse investment)* | **– A3.** Equity assets of DIE in DI (reverse investment)* |
| **A5.1.** Equity assets in fellow enterprises abroad *(if ultimate controlling parent is resident)* | **L5.1.** Equity liabilities to fellow enterprises abroad *(if ultimate controlling parent is non-resident)* |
| **– L5.2.** Equity liabilities to fellow enterprises abroad* *(if ultimate controlling parent is resident)* | **– A5.2.** Equity assets in fellow enterprises abroad* *(if ultimate controlling parent is non-resident)* |
| ***Outward debt instruments transactions*** | ***Inward debt instruments transactions*** |
| **A2.** Debt instruments assets of DI in DIE | **L2.** Debt instruments liabilities of DIE to DI |
| **– L4.** Debt instruments liabilities of DI to DIE (reverse investment)* | **– A4.** Debt instruments assets of DIE in DI (reverse investment)* |
| **A6.1.** Debt instruments assets in fellow enterprises abroad *(if ultimate controlling parent is resident)* | **L6.1.** Debt instruments liabilities to fellow enterprises abroad* *(if ultimate controlling parent is non-resident)* |
| **– L6.2.** Debt instruments liabilities to fellow enterprises abroad* *(if ultimate controlling parent is resident)* | **– A6.2.** Debt instruments assets in fellow enterprises abroad* *(if ultimate controlling parent is non-resident)* |

* Entered as a deduction in outward or inward FDI.

193. As explained in the section on foreign direct investment positions, the presentation of outward foreign direct investment transactions is different to that for foreign direct investment assets. Similarly, the presentation for inward foreign direct investment transactions is different to that for foreign direct investment liabilities. These differences essentially involve transposing reverse transactions and transactions between fellow enterprises in the two presentations (see Section 4.3.1).

### *4.3.2.1. Equity and reinvestment of earnings*

194. Transactions by a direct investor in the equity of its direct investment enterprises include both reinvestment of earnings and other equity transactions [Exhibits 4.3 and 4.4, items A1 (A1.1, A1.2) and L1 (L1.1, L1.2)]. Transactions by a direct investment enterprise in the equity of its direct investor (reverse investment; items A3 and L3) or in the equity of a fellow company (items A5 and L5) do not include reinvestment of earnings.

### *4.3.2.2. Equity transactions*

195. Equity increases result from a direct investor's establishment of a new direct investment enterprise, through:

*a)* its initial acquisition of equity that represents a 10%-or-more voting power interest in an existing enterprise;

*b)* its acquisition of an additional voting share ownership interest in an existing enterprise which takes the accumulated holding to at least the 10% voting power threshold; and

*c)* from its equity contributions to an existing direct investment enterprise.

196. Equity decreases result from:

*a)* the liquidation of a direct investment enterprise;

*b)* the partial or total sale of an ownership interest in a direct investment enterprise; and

*c)* the return of capital contributions;

*d)* liquidating dividends, which are considered to be a withdrawal of equity rather than a distribution of income.

197. For a given category of equity transactions (items A1, A3, A5 and L1, L3, L5), decreases in assets are deducted from increases in assets to derive the net transactions in assets within a given period, and similarly for liabilities. Equity transactions exclude changes in equity that result from the reinvestment of earnings, which constitute a separate sub-component of the accounts.

198. Equity transactions may arise either from transactions between a direct investor and its direct investment enterprise (such as contributed surplus or liquidations), or from transactions between a direct investor and a third party [such as purchases (sales) of stock in a direct investment enterprise by a direct investor from (to) an unaffiliated third party]. Note that these third-party transactions may need to be based on the records of the direct investor rather than on the records of the direct investment enterprise, because the data on these transactions may not be available from the records of the direct investment enterprise.

### *4.3.2.3. Reinvestment of earnings*

199. Reinvestment of earnings of direct investment enterprises (items A1.2 and L1.2) reflects earnings accruing to direct investors (that is, proportionate to the ownership of equity) during the reference period less earnings declared for distribution in that period. Earnings are included in direct investment income because they are deemed to accrue to the direct investor, whether they are reinvested in the direct investment enterprise or remitted to the direct investor. However, reinvested earnings are not actually transferred to the direct investor but rather increase the direct investor's investment in its direct investment enterprise. Therefore, an entry that is equal to that made in the direct investment income account but that flows in the opposite direction is made in the direct investment financial transactions account. In the direct investment income account, this form of income is referred to as "reinvested earnings". However, in the direct investment transactions account, "reinvestment of earnings " is the term that is used, to more clearly differentiate between the income and financial transactions (see the discussion of reinvested earnings in the direct investment income account for more details, Section 4.3.3: Direct investment income).

### *4.3.2.4. Debt instrument transactions*

200. For each category of debt instrument, decreases in assets are deducted from increases in assets to derive the net transactions in assets within a given period, and similarly for liabilities. Transactions in debt instruments between enterprises in a direct investment relationship should be recorded separately as shown in Exhibits 4.3 and 4.4 (items A2, A4, A6, L2, L4, L6). However, just as debt positions between FDI related financial intermediaries (such as commercial banks, savings institutions, credit unions, mutual funds or finance companies) are excluded from direct investment, so are the related transactions.

- *For debt instrument assets*, included are transactions that increase or decrease:
  - *i)* the resident direct investor's debt instrument claims on direct investment enterprise (A2);

*ii)* the resident direct investment enterprise 's debt instrument claims on direct investors (A4);

*iii)* other resident fellow enterprises ' debt instrument claims on fellow enterprises abroad (A6), distinguishing whether the ultimate controlling parent is resident (A6.1) or non-resident (A6.2).

- For debt instrument *liabilities*, included are transactions that increase or decrease:

*i)* the financial obligations of a resident direct investment enterprise to direct investors (L2);

*ii)* the financial obligations of a resident direct investor to direct investment enterprises (L4);

*iii)* the financial obligations of other resident fellow enterprises to fellow enterprises abroad (L6) distinguishing whether the ultimate controlling parent is non-resident (L6.1) or resident (L6.2).

201. When a direct investor lends funds to its direct investment enterprise, the level of the direct investor's assets claim (receivables) on the enterprise increases. Subsequently, when the direct investment enterprise repays the principal owed to its direct investor, the level of the direct investor's receivables from the enterprise is reduced. Similarly, when a direct investor borrows funds from its FDI enterprise, the level of the direct investor's liabilities (payables) to the enterprise increases and when the direct investor repays the principal, the level of the direct investor's payables is reduced. The same would be applicable to fellow enterprises.

202. Increases in the resident's receivables from, or reductions in the resident's payables to, its foreign direct investor or fellow enterprises abroad give rise to outflows on inter-company debt accounts. Reductions in the resident's receivables from, or increases in the resident's payables to, its foreign direct investor or fellow enterprises abroad give rise to inflows.

203. The net change in inter-company debt includes changes in the value of financial (or capital) leases between direct investors and their related enterprises abroad. Financial leases are treated as loans. A financial lease is a contract under which a lessee contracts to pay rentals for the use of a good for most or all of its expected economic life. The rentals enable the lessor over the period of the contract to recover most or all of the costs of goods and the carrying charges. While there is not a legal change of ownership of the good, under a financial lease the risks and rewards of ownership are, *de facto*, transferred from the legal owner of the good, the lessor, to the user of the good, the lessee. For this reason, under statistical convention and standard accounting rules, the total value of the good is imputed to have changed ownership. So, the debt liability at the inception of the lease is defined as the value of the good and is financed by a loan of the same value, a liability of the lessee. The loan is repaid through a series of payments (which comprise a blend of the accrued interest since the last payment and principal payment elements) and any residual payment at the end of the contract (or alternatively, by the return of the good to the lessor).

204. Direct investors may make loans to or borrow funds from their indirectly owned direct investment enterprises. An indirect ownership interest exists when a direct investment enterprise that is directly owned, in turn, owns an enterprise that also qualifies as a direct investment enterprise of its own direct investor. In this example, the direct investor at the top of the ownership chain holds an indirect ownership interest in the enterprise at the bottom of the ownership chain. The *Benchmark Definition* recommends that such

transactions be included in direct investment and allocated to the country of the indirectly owned direct investment enterprises (see Chapter 3 for a description of the FDIR).

205. Enterprises which are fellow enterprises may make loans to or borrow funds from other fellow enterprises. The *Benchmark Definition* recommends that such transactions be included in direct investment and allocated to the economies of the counterpart fellow enterprises. Loans made by enterprises included in the FDIR in economy A to fellow enterprises in economy B should be included in direct investment assets for compiling economy A and as direct investment liabilities for compiling economy B.

### *4.3.3. Direct investment income*

206. Direct investment income is part of the return on the direct investment position; that is, it is the return on equity and debt investment. Direct investment income consists of earnings on equity investment (for example, a resident direct investor's share in the net income or earnings of its direct investment enterprises) plus income on debt between direct investors and direct investment enterprises and between fellow enterprises. Direct investment income payables are calculated in a similar way. Direct investment income is recorded as it accrues. However, as debt instruments involving FDI-related financial intermediaries are excluded from direct investment, so is the debt income between them (see also Section 4.4.3).

207. Direct investment earnings measure earnings from current operations. Therefore, this amount should be calculated before recognition of holding gains and losses and extraordinary items. Operational earnings of the direct investment enterprise should be reported after deducting provisions for depreciation and for corporate taxes charged on these earnings by the government in the host economy. Depreciation should, in principle, be measured at current replacement cost, particularly if market values are available for stock figures. If data on depreciable assets and on depreciation are available only on a book value or historical cost basis, those values should be adjusted wherever possible to a current replacement cost basis. Compilers should base the estimates of direct investment earnings, and of direct investment positions, on a current market value basis. If market values are unavailable, FDI data at book value should be adjusted to estimates of market value.

208. The earnings of direct investment enterprises reported using the "Current Operating Performance Concept " (COPC) should exclude:

- *i)* any gains or losses arising from valuation changes, such as inventory write-offs, write-downs, or write-ups;
- *ii)* gains or losses on plant and equipment from the closure of part or all of a business;
- *iii)* writing-off of intangible assets, including goodwill, due to unusual events;[29]
- *iv)* writing-off of research and development expenditures capitalised in a prior period;
- *v)* provisions for losses on long-term contracts;
- *vi)* exchange rate gains and losses incurred by the direct investment enterprise both from its trading activities and from its holdings of foreign currency assets and liabilities;
- *vii)* unrealised gains or losses from the revaluation of fixed assets, investments and liabilities;

29. The standard amortization of intangible assets is, however, included as an expense under the COPC.

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*viii)* realised gains or losses made by the enterprise from the disposal of assets or liabilities.

209. The exclusion of realised and unrealised holding gains and losses is applicable to all direct investment enterprises, including those such as banks and securities dealers for whom the making of such gains is an important or even the main part of their business. This promotes consistency with the calculation and treatment of earnings in the national economic accounts, as prepared pursuant to *SNA* guidelines.

210. Some countries apply the *All-inclusive concept* to measure the earnings where income is estimated after allowing for all items (including capital gains and losses). This method is not recommended by the *Benchmark Definition*. However, because many countries base their earnings data on all-inclusive basis, they are encouraged to provide supplemental data on holding gains and losses and other extraordinary items.

211. Direct investment income should be separately shown for assets and for liabilities. Income on direct investment assets should be recorded as positive amounts under income receivables, and income on direct investment liabilities should be recorded as positive amounts under income payables. When, during a reference period, a direct investment enterprise pays a dividend that is larger than the earnings from current operations during that period (or where it incurs an operational loss), negative reinvested earnings will result. The latter should be recorded as a negative credit for income on direct investment assets and as negative debit for income on direct investment liabilities. All income credits on reinvested earnings (whether negative or positive) should have an equal and opposite entry in the *FDI transactions account* (under "outward FDI, reinvestment of earnings"). Similarly, all income debits on reinvested earnings (whether negative or positive) should have an equal and opposite entry in the *FDI transactions account*, under "inward FDI, reinvestment of earnings".

212. For direct investment income under the asset/liability principle, elements are schematically shown as follows:

Exhibit 4.5. **Foreign direct investment income according to the asset/liability principle**

| Receivables | Payables |
|---|---|
| ***Of direct investors from direct investment enterprises*** | ***Of direct investment enterprises to direct investors*** |
| **A1.** Earnings on equity | **L1.** Earnings on equity |
| **A1.1.** Distributed earnings | **L1.1.** Distributed earnings |
| **A1.2.** Reinvested earnings | **L1.2.** Reinvested earnings |
| ***A2.*** Interest (on debt instruments) | ***L2.*** Interest (on debt instruments) |
| ***Of direct investment enterprises from direct investors – Reverse investment*** | ***Of direct investors to direct investment enterprises – Reverse investment*** |
| **A3** Distributed earnings | **L3** Distributed earnings |
| **A4.** Interest (on debt instruments) | **L4.** Interest (on debt instruments) |
| ***From fellow enterprises abroad*** | ***To fellow enterprises abroad*** |
| **A5.** Distributed earnings | **L5.** Distributed earnings |
| **A5.1.** If the ultimate controlling parent is resident | **L5.1.** If the ultimate controlling parent is non-resident |
| **A5.2.** If the ultimate controlling parent is non-resident | **L5.2.** If the ultimate controlling parent is resident |
| **A6.** Interest (on debt instruments) | **L6.** Interest (on debt instruments) |
| **A6.1.** If the ultimate controlling parent is resident | **L6.1.** If the ultimate controlling parent is non-resident |
| **A6.2.** If the ultimate controlling parent is non-resident | **L6.2.** If the ultimate controlling parent is resident |

213. To illustrate the directional principle for direct investment income, elements are schematically shown as follows:

Exhibit 4.6. **Foreign direct investment income according to the directional principle**

| Income on outward foreign direct investment | Income on inward foreign direct investment |
|---|---|
| ***Income on outward equity*** | ***Income on inward equity*** |
| **A1.** Earnings on equity | **L1.** Earnings on equity |
| **A1.1.** Distributed earnings | **L1.1.** Distributed earnings |
| **A1.2.** Reinvested earnings | **L1.2.** Reinvested earnings |
| **– L3.** Distributed earnings of DI to DIE (reverse investment)* | **– A3.** Distributed earnings of DIE from DI (reverse investment)* |
| A5.1. Distributed earnings from fellow enterprises abroad (*if ultimate controlling parent is resident*) | L5.1. Distributed earnings to fellow enterprises abroad (*if ultimate controlling parent is non-resident*) |
| – L5.2. Distributed earnings to fellow enterprises abroad* (*if ultimate controlling parent is resident*) | – A5.2. Distributed earnings from fellow enterprises abroad* (*if ultimate controlling parent is non- resident*) |
| ***Interest on outward debt instruments*** | ***Interest on inward debt instruments*** |
| ***A2.*** Interest receivable from DIE | ***L2.*** Interest payable to DIs |
| **– L4.** Interest payable by DI to DIE (reverse investment)* | **– A4.** Interest receivable by DIE from DI (reverse investment)* |
| **A6.1.** Interest receivable from fellow enterprises (on debt instruments) *(if ultimate controlling parent is resident)* | **L6.1.** Interest payable to fellow enterprises (on debt instruments) *(if ultimate controlling parent is non-resident)* |
| **– L6.2.** Interest payable to fellow enterprises (on debt instruments)* *(if ultimate controlling parent is resident)* | **– A6.2.** Interest receivable from fellow enterprises (on debt instruments)* *(if ultimate controlling parent is non-resident)* |

* Entered as a deduction in outward or inward FDI.

### *4.3.3.1. Direct Investment Income on equity*

214. Once a direct investment relationship exists, direct investment earnings are based on the direct investor 's percentage share (based on their equity share) in the current earnings of the given direct investment enterprise.

215. Direct investment income on equity (Exhibits 4.5 and 4.6, items A1 and L1) – or direct investment earnings – is the return of the direct investor on the equity component of the direct investment position. For investment by a direct investor in its direct investment enterprise [Exhibits 4.5 and 4.6, items (A1.1, A1.2) and (L1.1, L1.2)] it consists of "distributed earnings " and "reinvested earnings ". For investment by a direct investment enterprise in its direct investor (A3 and L3) or investment between fellow enterprises (items A5 and L5), income on equity consists only of distributed earnings as reinvested earnings are not included. The reason for this is that the direct investment enterprise does not hold 10% or more of the voting power in its direct investor. Consequently, the enterprise is not considered able to influence the savings and distribution policies of the direct investor or fellow enterprise. If, however, the direct investment enterprise does hold 10% or more of the voting power in its direct investor, it then becomes a direct investor in its direct investor, and reinvested earnings are attributed to it.

216. Earnings exclude currency exchange gains and losses and other holding gains and losses, whether or not such gains and losses are included in net income for financial accounting, tax, or other purposes. However, these earnings include the impact of changes in foreign currency exchange rates on the operating revenues and expenses of direct investment enterprises, because these are not due to holding gains and losses. This treatment is intended to make income and earnings correspond to the current operating performance of the relevant enterprises in the ownership chain, in accordance with international guidelines.


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217. Direct investment earnings are measured before deduction (or gross) of withholding taxes on distributed earnings and interest. Withholding taxes are viewed as being levied on the recipient of the distributed earnings or interest to which the taxes are applied, and thus as being paid across borders even though, as an administrative convenience, the tax payments are actually made by the firm whose disbursement gave rise to them. Thus, foreign withholding taxes on distributed earnings and on interest received by a resident direct investor are recorded as if they were paid by the direct investor, not by the direct investment enterprise. Similarly, the resident economy's withholding taxes of the reporting country on interest payments by resident direct investors or resident direct investment enterprises are recorded as if they were paid by the non-resident, not by the resident.

218. When a direct investment ownership chain exists, direct investment earnings should reflect income from direct and indirect enterprises. All earnings from an ownership chain are geographically allocated to the enterprises directly owned. However, these earnings should include the claims of directly owned enterprises' on the earnings of enterprises below them in the ownership chain, proportionate to the immediate direct investor 's ownership of shares. For example, if A (resident in Country A) owns 100% of B (resident in B), which, in turn, owns 100% of C (resident in C), B's FDI earnings will include all of the earnings from its current operations, including its investment income, which, by definition, includes all of C's reinvested earnings (as C is 100% owned by B, B will be deemed to receive all of C's reinvested earnings as reinvested earnings). As a consequence, the reinvested earnings receivable by A from its ownership of all the shares in B will include C's reinvested earnings. Therefore, A does not need to seek the information on C's reinvested earnings directly from C, in order for that income to be measured correctly, but it is recommended that the compiler of direct investment data in Country A makes sure that B understands that it should report C's reinvested earnings, even though it is an imputed transaction. (In instances, where the direct investors do not hold 100% of the equity in an immediate direct investment enterprise, their reinvested earnings receivable should be in accordance with the proportion of the shares they own (see Annex 6 on reinvested earnings for another example of calculation of reinvested earnings along a chain of related enterprises). The compiler will often find that the information required in order to determine a direct investor's share of the reinvested earnings of indirectly owned direct investment enterprises becomes more difficult to determine once its share of indirect ownership falls below 50%. In that instance, it is recommended that it be impressed upon respondents to direct investment surveys of the importance that this information be collected.

#### *4.3.3.2. Distributed earnings*

219. Distributed earnings (items A1.1, A3, A5 and L1.1, L3, L5) consist of dividends and distributed branch profits. Dividends include those to shareholders, both common and participating preferred stock, whether voting or non-voting, according to the contractual relationship between the enterprise and these various types of shareholders, before deduction for withholding taxes. Dividends exclude liquidating dividends and bonus shares (which are dividends in the form of additional shares of stock). Liquidating dividends are excluded because they are a return of equity rather than a remittance of earnings (liquidating dividends are included instead as transactions in the direct investment equity). Distributed earnings can be paid out of current or past earnings and

may result in negative reinvested earnings if the distribution of dividends exceeds total earnings in a particular reference period. Bonus shares are excluded because they are a capitalisation of retained earnings – a substitution of one type of equity (capital stock) for another (retained earnings). In an accounting sense, they reduce the amount of retained earnings available for distribution but leave total owners' equity unchanged.

#### *4.3.3.3. Reinvested earnings*

220. Reinvested earnings of direct investment enterprises (items A1.2 and L1.2) reflect earnings on equity accruing to direct investors less distributed earnings, proportionate to the percentage ownership of the equity owned by the direct investor(s). As noted in the discussion of "reinvestment of earnings", reinvested earnings are included in direct investment income because the earnings of the direct investment enterprise are deemed to be the income of the direct investor (proportionate to the direct investor's holding of equity in the direct investment enterprise), whether they are reinvested in the enterprise or remitted to the direct investor. However, because reinvested earnings are not actually distributed to the direct investor but rather increase the direct investor's investment in its affiliate, an entry that is equal to that made in the direct investment income account but of opposite sign is entered in the direct investment transactions account. In the direct investment income account, this transaction is referred to as "reinvested earnings".

#### *4.3.3.4. Direct Investment income on debt*

221. Direct investment interest payables (on liabilities) and interest receivables (on assets) are separately recorded. Thus, interest receivables comprise interest accruing to residents (direct investors, direct investment enterprises and fellow enterprises) on their debt receivables, and interest payables comprise interest accruing to non-residents (direct investment enterprises, direct investors and fellow enterprises) on debt payables.

222. No direct investment interest receivables or payables are recorded when both parties are related financial intermediaries (such as commercial banks, savings institutions, credit unions, mutual funds or finance companies).

223. Interest includes the interest component of transactions under financial leases between enterprises in a direct investment relationship, assuming the outstanding capitalized value of such leases is included in the debt component of the direct investment position at discounted value.

224. The interest component of direct investment income reflects accruals of interest on debt in the current period (*i.e.* interest accrued), whether or not paid.[30] Interest receivable and payable should be compiled separately. Interest receivable by direct investors from their direct investment enterprises, receipts from direct investment enterprises from their direct investors and receipts from fellow enterprises are included. Payables are calculated in an analogous manner.

225. Interest accruals on marketable securities should be calculated under the debtor basis, not the creditor basis. Under the debtor basis, interest accruals on fixed interest rate

30. Accrual accounting records flows at the time economic value is created, transformed, exchanged, transferred or extinguished. This means that flows which imply a change of economic ownership are entered when ownership passes and services are recorded when provided. In other words, the effects of economic events are recorded in the period in which they occur, irrespective of whether cash was received or paid or was due to be received or paid (*SNA 2008*, paragraph 3.94 and *GFSM 2001*, paragraph 3.25).

 

securities reflect the amount of interest that the debtor is contractually obligated to pay, and changes in market interest rates since the debt was issued are not taken into account. In contrast, under the creditor basis, interest accruals on fixed interest rate securities reflect market interest rates in the current period, not the interest rates in effect at the time(s) that the debt securities were originally issued.

226. Interest on debt accrues continually over the life of the debt and adds to the principal. Thus, actual payments of the debt (as opposed to accruals) are investment transactions and not income. Therefore, they should be recorded in the *FDI transactions account*.

227. At inception, future cash flows are determined in the relevant currency. Interest expressed in foreign currency is to be converted into the domestic currency units at the mid-point market exchange rate for the periods in which the interest accrues.

### *4.3.4. Other changes*

228. As described in Section 4.3.1.3 a direct investment position can change due to transactions and to other changes, where other changes consist of valuation changes and volume changes. Valuation changes can further be considered to consist of exchange rate changes and other price changes. Exchange rate changes generally reflect the impact on the position of exposure of the instrument to a currency other than that in which the accounts are compiled. Other price changes reflect all other changes in the market value of the instrument as expressed in the compilation currency.

229. The other changes account is an important component of direct investment statistics as it allows transactions to be reconciled with positions. As such, it provides a method of validating and testing the consistency of transactions and positions. While other changes can be measured residually, it is through direct measurement of this account (and its components) that the improvements to quality of transactions and positions are made possible. The standard and supplemental reporting to the OECD (see Annex 2) does not involve the reporting of the other changes account.

#### *4.3.4.1. Valuation changes*

230. Chapter 5 describes methods for identifying the market value of a position or a transaction. Valuation changes reflect changes in the market value of a position.

#### *4.3.4.2. Exchange rate changes*

231. "Exchange rate changes" reflect the impact that changes in exchange rates have on instruments that are denominated in a currency other than that in which the accounts are compiled. Equity is considered to be denominated in the currency of the economy in which the enterprise is resident. As a result, all equity liabilities of an economy are considered to be denominated in the local currency and if the accounts are compiled in the local currency, the exchange rate changes for equity liabilities will be zero. Debt securities are denominated in the currency in which they are to be redeemed except in the case where the principal is indexed to another currency. When the principal of a debt security is linked to another currency, the debt security is treated as though it were denominated in that currency. In all other cases, reference should be made to the contractual arrangements of the debt position to determine in which currency it is denominated.

232. Exchange rate changes may be referred to by enterprises as realised or unrealised exchange rate or foreign exchange gains or losses. These impacts should not be included in the earnings of an enterprise when calculating income flows.

233. It should be noted that operating revenues and expenses denominated in units of a foreign currency will also translate into different amounts, expressed in the compilation currency, solely as a result of exchange rate changes. However, these impacts should be included in direct investment earnings in the current period, because they result from actual on-going operations in the current period rather than from holding gains.

234. Transactions are converted to the compilation currency at the rate prevailing when they took place, and positions are converted at the rate prevailing on the reference date. The mid-point between the buying and selling rates should be used at the time of transaction (for transactions) and at the close of business on the reference date for positions. The impacts of changes in the exchange rate on this conversion are recorded as exchange rate changes.

235. If the accounts are compiled in the local currency, and the local currency appreciates against the currency of denomination of a financial instrument, exchange rate changes will reflect a decrease in the value of the instrument in the local currency. This is the case whether the instrument is an asset or a liability.

#### *4.3.4.3. Other price changes*

236. "Other price changes" reflect all changes to the market value of an instrument as expressed in the compilation currency that are not exchange rate changes or attributable to transactions. For the asset holder, these changes may be referred to as holding gains or losses. Other price changes reflect the change in the market value of an instrument in the currency in which it is denominated. This market price change is then converted to the currency of compilation and may also give rise to exchange rate changes if the exchange rate changes over the period during which the market price change occurred (see Section 4.3.4.4).

237. Other price changes may be recorded under any of the recommended methods for valuing unquoted equity in terms of current period prices. For example, if positions are revalued under the "Net Asset Value, including goodwill and identified intangibles" method, much or most of the change in the direct investment equity position may be recorded in this account.

238. Another example of a change that will be recorded as an other price change' is when a direct investor sells its direct investment enterprise for more (or less) than the value recorded in the direct investment position. The amount received from the sale of the enterprise is recorded as a financial inflow in the direct investment accounts compiled by the country of the direct investor; the difference between the financial inflow/outflow and the value of the direct investment enterprise in the position must be attributed as an other price change so as to remove from the position the full value of the affiliate that has been sold.

239. A direct investment enterprise may have assets or liabilities expressed in a currency other than its local currency. Changes in exchange rates will have an impact on the value of the direct investment enterprise's assets and/or liabilities. These changes are likely to impact on the market valuation of the direct investment enterprise itself. The change in

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the asset value of the direct investment enterprise to its direct investor is recorded as an "other price change".

240. Similarly, external factors can influence the market value of a debt position. If the credit rating of the issuer of a debt instrument is changed, then this may have an impact of the value of the debt instrument.

241. If equity listed on resident markets is generally increasing in value, this will be reflected in an increase in the value of equity liabilities; while if equity listed on non-resident markets is generally increasing in value, this will be reflected in an increase in the value of equity assets.

242. Where debt positions between related enterprises are in the form of debt securities, the market value of these positions will be affected by changes in interest rates. If resident interest rates are generally increasing, this will be reflected in a decrease in the value of debt securities issued in the local economy; while if non-resident interest rates are generally increasing, this will be reflected in a decrease in the value of debt securities issued abroad. To determine the impact of these changes on the values of positions, it is necessary to understand whether debt security assets/liabilities between related enterprises are issued locally or abroad.

#### *4.3.4.4. Recording valuation changes*

243. It is not unusual for positions to change due to both exchange rate changes and other price changes. It is analytically useful to separate the causes of the changes in valuation.

244. For instruments denominated in a currency other than that in which the accounts are compiled, the opening position (or position at creation) is converted to the compilation currency at the exchange rate prevailing at the time, and similarly for the closing position (or position when extinguished). The difference between these two values consists of both exchange rate changes and other price changes.

245. The other price changes should be calculated in the currency of denomination. This is converted to the compilation currency using a mid-point exchange rate. The mid-point exchange rate is calculated as the mid-point between the exchange rate at the start of the period (or at the time when the position was created if this was during the period) and the exchange rate at the end of the period (or at the time when the position was extinguished if that occurred during the period).

246. The exchange rate changes can then be calculated as the difference between the total valuation change and the other price change.

247. Under the International Financial Reporting Standards (IFRS), enterprises may keep their books in a currency other than the local currency or the currency in which the accounts are compiled. The IFRS refer to this currency as the currency of account. When these enterprises report information to the compiling authority, it will need to be converted to the domestic currency (or the compilation currency). Exchange rate changes are calculated as the impact of changes in the exchange rate between the currency in which an instrument is denominated and the currency in which the accounts are compiled; other valuation changes identified during the conversion process should be recorded as price changes, regardless of movements in the exchange rates used in the conversion.

### 4.3.4.5. *Volume changes*

248. The volume of financial assets and liabilities for an economy can change due to either transactions or other changes in volume. The causes of other changes in volume include debt cancellation and write-offs, liquidations, uncompensated seizure, and reclassifications.

**Debt cancellation and write-offs**

249. Changes in claims resulting from debt cancellation or write-offs are treated as volume changes and are not treated as financial transactions. Specifically, a creditor may recognise that a financial claim can no longer be collected from the debtor and may remove the claim from its balance sheet. Debt cancellations and write-offs are unilaterally determined by the creditor as well as by courts, arbitrators and related out-of-court settlements; unilateral cancellation of a financial claim by a debtor (debt repudiation) is not recognised. Debt forgiveness and debt assumption are both treated as financial transactions.

250. Debt forgiveness usually involves the intention by the creditor to convey a benefit to the debtor. Debt assumption (including one-off guarantees) usually involves a third party with which there may be transactions.

251. Partial write-offs (write-downs) of debt assets by creditors are not considered to change the volume of financial claims of the creditor on the debtor. Partial write-offs are treated as a revaluation of the claim and are classified as other price changes. If a bankruptcy process results in all debt being written off, then the loss is recorded as a volume change; if the bankruptcy process results in even a token return to the creditor, then the debt is reduced as a valuation change with a transaction to extinguish the debt. The nature of the underlying loss is similar and the distinction may not be practical or analytically useful. As a result, a simplifying convention may be to treat these cases in the same way as full write-offs.

**Liquidations and failed exploration activities**

252. When a direct investment enterprise is liquidated, the equity investment in the enterprise is often written off by the direct investor and removed from its balance sheet. This situation is treated as a volume change as the equity claim is considered to have disappeared. The treatment is analogous to the write-off of debt. If there is a partial return to the direct investor, then this should be treated as a valuation change with a transaction to extinguish the claim. As with debt write-offs, it may not be practical or analytically useful to make this distinction, and these cases may be treated in the same way as where there is no return.

253. Mineral exploration activities present a special case of equity write-offs. The purchase of a mineral exploration licence is a sufficient criterion to recognise a notional unit within the economy where the mineral exploration is to take place. As activity takes place and equipment is purchased or provided to the exploration operations, a branch is considered to be established. The provision of equipment is recorded as a transaction reflecting the injection of equity in the branch. Valuation changes may also occur dependent on the expectations of a find. If the exploration fails to identify a viable resource discovery and the operator walks away' from the activities, the investment in the branch is extinguished through a volume change. This is a borderline case – where there are assets that are sold, the appropriate treatment is to revalue the investment to the value received

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for the assets and then extinguish the investment through a transaction reflecting the sale of the assets and withdrawal of equity.

**Uncompensated seizure**

254. Direct investment enterprises may also be subject to seizure by national governments on occasion (for example where a government decides to nationalise certain industries within its jurisdiction without compensation). This extinguishes the equity that the direct investor has in the enterprise in the economy, with the equity position being reduced to zero through a volume change.

**Reclassification**

255. A reclassification entry is necessary when a financial instrument changes its characteristics without there having been a cross-border transaction.

256. For direct investment, a common issue is how to treat an existing equity position when a further purchase is made to take the total position to one that represents at least 10% of the voting power in an organisation. The original equity position is reclassified to direct investment through a volume change to include it in the direct investment equity position. Similarly, any pre-existing debt positions are reclassified to direct investment debt positions through a volume change. When voting power is reduced, equity and debt positions are removed from direct investment through volume changes. It should be recognised that there does not need to be any transactions for voting power to cross the 10% threshold – for example, a position can increase in proportion due to share buybacks; while positions can decrease due to the issue of additional shares.

257. The migration of persons can also result in reclassifications of direct investment. When a person changes residence, this is considered to be a reclassification of his/her residence – any direct investment assets which they hold which are resident in the economy to which the person has moved are reclassified out of the direct investment position as a volume change (as the position has become one between two residents of the same economy). Assets with which the person is in a direct investment relationship in their former place of residence are reclassified into the direct investment position as a volume change.

258. On occasion, land can change from being part of one economy to being considered part of another economy, whether through mutual agreement or annexation, or be considered to be a new economy. This may create or extinguish direct investment positions that residents of either economy had with residents of the area of land that changed jurisdiction. The creation and extinction of the direct investment positions is treated as a volume change.

259. A similar situation arises with the change of membership in country groups. For example, the European Union has increased its membership on a number of occasions. This can result in the positions between the country group and the new member being extinguished (for statistics for the country group as a whole), positions between the country group and other countries being created. Conceptually, these should be treated as volume changes. An alternative approach is to treat the country group as if it had always consisted of its current membership and to revise historical series associated with the country group.

## 4.4. Scope of FDI

### *4.4.1. Standard content of FDI statistics*

260. The scope of direct investment covered in this *Benchmark Definition* was reviewed to take into account the economic and financial developments over the past decade or so[31] which may directly or indirectly impact the measurement of the FDI activity. As described in Section 2.4.2, there are two standard (core) presentations of direct investment statistics, both of which represent breaks from historical series:

- Aggregate FDI statistics for assets and liabilities by instrument (equity, debt).
- Detailed FDI statistics under the directional principle by *i)* geographical allocation; and *ii)* industry classification (each category broken down by instrument (equity, debt).

261. Investors apply a large variety of financing structures as markets evolve and as they put in place new instruments. The growing complexity of the measurement of the direct investment activity was accelerated with the expansion of globalisation and its effects. As a consequence, users indicated that international standards should be revisited to respond to the need for more and more sophisticated statistics for analytical research and for policy making. Against this background, the traditional FDI statistics had to be expanded and tailored for new data requirements.

#### *4.4.1.1. Aggregate FDI statistics (asset/liability principle)*

262. The analytical presentation of FDI statistics showing non-resident assets and liabilities of direct investors and direct investment enterprises is a new feature of the *Benchmark Definition*. It complies fully with the overall presentation of macro-economic statistics. Conceptually, these data are in line with the balance of payments and the international investment position statistics[32] as well as the national accounts presentation of the institutional sectors of the economy. Direct investment measured in terms of assets and liabilities constitute the basis for compiling FDI statistics from which other presentations can be derived provided that additional relevant pieces of information are included in national data collection systems.

263. Aggregate FDI statistics include all types of enterprises (operational direct investment entities as well as Special Purpose Entities (SPEs) following the relationship identified by the FDIR (see also Chapter 3) and all types of transactions/positions (including pass through funds and capital in transit). These statistics are compiled according to first counterparty (*i.e.* immediate investor or immediate direct investment enterprise). The identification of counterpart residency information is not required for aggregate data dissemination but constitutes to a large extent the fundamental basis for data compilation. Industry classification is not required for these data either. Aggregate FDI statistics on this same asset and liability basis should also be provided separately for resident SPEs.

31. The *Benchmark Definition, 3rd edition* was published in 1996.
32. The asset/liability approach constitutes a break in series from previous aggregate data compilation of balance of payments and international investment position. Linkages between the two data sets are provided in Chapter 4.

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### *4.4.1.2. Detailed FDI statistics (directional principle)*

264. As from its first edition, the *Benchmark Definition* recommends that countries compile and disseminate detailed FDI statistics broken down by *i)* geographical allocation; and *ii)* industry classification. Such statistics provide a further refinement to an aggregate statistical framework which is traditionally used for balance of payments and international investment position presentations. It allows FDI analyses by source and destination country/industry which cannot be achieved by aggregate data. Current standards for detailed FDI statistics have refined further the directional principle as compared to the previous version of the *Benchmark Definition*. The revised directional principle reflects the guiding principle of FDI which is influence (or control) of the direct investor over the direct investment enterprise (see Section 4.3 FDI accounts).

265. Recourse to complex financing structures by multinational enterprises (MNE) in their cross-border investments is more and more frequent. Funds transmitting through intermediate entities of different types are common practice. Such investment patterns distort the analysis of the source and destination of FDI and may lead to undesirable statistical and analytical results when they are recorded strictly according to the immediate counterparty.[33] Moreover, they result in the overstatement or multiplication of direct investment transactions (also referred as the "inflation" of FDI data) both at the country and at regional or global levels. Countries hosting the intermediate entities (SPEs or other entities acting on behalf of the parent), observe artificially high investment statistics. These pass-through investments have no real immediate economic impact such as job creation, productivity gains etc. on the host economy. To circumvent such problems,[34] the present edition of the *Benchmark Definition* recommends, while preserving consistency of geographical (industrial) breakdowns provided by different countries, that compilers exclude SPEs resident in their economies when presenting FDI statistics on a directional basis. However, compilers are at the same time asked to provide in a separate column and on the same basis the transactions and positions of resident SPEs according to the geographical and industrial classifications. Chapter 7 provides more information on the geographical and industry classification of FDI data presented according to the directional principle.

266. For the standard presentation of FDI under the directional principle, the exclusion of SPEs was limited only to resident entities even if it is recognised that it would be more meaningful to exclude non-resident SPEs as well. Due to difficulties compilers currently may encounter in achieving this, the alternative option of "looking through" non-resident SPEs is recommended only on a supplemental basis and is subject to further priority research (see Section 4.4.2.1).

267. This standard presentation of FDI statistics excluding resident SPEs, considered by users as more suitable for FDI analysis, constitutes one of the main focuses of this *Benchmark Definition*. Relative to the previous edition of the *Benchmark Definition* it represents a substantial improvement of the analysis of FDI figures broken down by country and industry. Obviously, in view of the complexity of the global network of FDI relationships and the many aspects to it, some issues still need to be further investigated and will remain on the agenda for future research.

33. This approach was recommended in earlier versions of the *Benchmark Definition*.
34. It should be noted that MNEs also pass funds through their operating affiliates. However, these structures can be very complicated and require further research (see Annex 13).

268. Extensive research has shown that a variety of (overlapping) definitions of SPEs exist. As there is no single universal definition of SPEs, it is left to individual countries to identify such entities according to their own definitions or descriptions. Countries that have not yet adopted a definition of SPE (which is the case in a large majority of countries) may be assisted by the criteria listed in Chapter 6.

269. The directional principle, in addition, involves the deducting of some building blocks of the FDI accounts as presented in Section 4.3. Under this presentation any reverse investment (equity or debt) from the direct investment enterprise in its direct investor is to be deducted from the inward FDI when the direct investment enterprise holds less than 10% of the voting power in its direct investor. Data on the directional principle is also to be applied between fellow enterprises (see section 4.3). The recording of direct investment between fellow enterprises is to be presented according to the residence of the immediate counterpart but the direction of the investment is to be determined according to whether the ultimate controlling parent is a resident or a non-resident of the compiling economy. In other words, if the ultimate controlling parent is not a resident of the compiling economy, all transactions and positions between the fellows are classified as inward FDI. If the ultimate controlling parent is resident in the compiling economy, the transactions and positions are classified as outward FDI.

### *4.4.2. Supplemental FDI series*

#### *4.4.2.1. FDI looking through non-resident SPEs (directional principle)*

270. Compilers are strongly encouraged to provide on a supplemental basis a breakdown of FDI by country and industry that is obtained by looking through immediate non-resident counterparts that are SPEs. Due to the fungibility of funds and the use of SPEs as financial turn-tables for different destinations/countries – an outward flow may split beyond the SPE – it may not (always) be possible to look through non-resident SPEs in an unambiguous way. Compilers are therefore encouraged to intensify bilateral exchanges of information with compilers of countries hosting SPEs.[35] Some bilateral asymmetries may remain, but these would seem less serious than distortions of geographical breakdowns, in which countries with many SPEs would, for instance, give the wrong impression of being overly attractive as a location for direct investment or overly active in investing in developing countries, for instance.

271. Where considered necessary compilers are also encouraged, at least once a year, to provide FDI statistics according to the criteria of the *Benchmark Definition*, 3rd edition[36] *i.e.* to include all resident enterprises in compiling these FDI statistics irrespective of whether they are SPEs or not.

#### *4.4.2.2. FDI by type: Mergers and acquisitions (directional principle)*

272. International standards for compiling FDI statistics described in earlier editions of the *Benchmark Definition* have focused mostly on types of financing, types of enterprises, types of transactions, etc. For the first time, a methodology was put together to construct

35. The allocation of inward amounts to outward destinations may still require some rules of thumb, which countries are asked to clarify in meta-data.

36. According to the former 3rd edition of the *Benchmark Definition*, the basis for data reporting was the directional principle which was then primarily concerned with reverse investments by direct investment enterprises in direct investors.

statistical series by types of FDI which is largely determined by the purpose of direct investment. FDI statistics encompass mainly four types of operations that qualify as FDI:

*i)* purchase/sale of existing equity in the form of mergers and acquisitions (M&A);

*ii)* greenfield investments;

*iii)* extension of capital (additional new investments); and

*iv)* financial restructuring.

273. While M&A transactions imply the purchase or sale of existing equity, greenfield investments refer to altogether new investments (*ex nihilo* investments). Extension of capital relates to additional new investments as an expansion of an established business; conceptually and in terms of economic impact, it is similar to greenfield investments. Financial restructuring refers to investment for debt repayment or loss reduction.

274. Direct investment will have, all other aspects being equal, a different impact, in particular, on the "host" economy depending on the type of FDI. It is generally considered that cross-border investments in the form of M&As will not involve significant changes in the performance of economic variables such as production, employment, turnover, etc., unless the acquired enterprise is subject to significant restructuring. On the other hand, new investments, greenfield investments and extension of capital, are likely to add new dimensions to the economic performance of the host economy and to the earnings of the direct investor.

275. Moreover, to measure the impact of FDI in host and home economies, users need detailed analytical information: FDI by type broken down by partner country and by industry (see also Chapter 2). This novel feature of FDI statistics is at the centre of arguments which have led to the revision of the *Benchmark Definition*, *i.e.* to align international standards to economic and financial developments since the last edition. To avoid any confusion, it should be clear to the reader that the statistics of M&As shown as an "of which" category of FDI are not identical to what is generally referred to as "M&A statistics" by private commercial sources compiled and disseminated outside the context of FDI statistics. It is more appropriate to call the former "M&A transactions" and the latter M&A statistics as the scope and the coverage of the two data sets differ but they remain complementary.

276. In the current edition of the *Benchmark Definition* a primary focus is to compile and disseminate on a supplemental basis FDI showing M&A type transactions, *i.e.* purchase/sale of existing FDI equity by non-residents. The examination of greenfield investments, extension of capital, and financial restructuring is deferred to the research agenda as they require further research which could not be completed in time for the publication of the present edition. However, after deducting M&A equity transactions from total FDI equity, users would be able to obtain, as a residual, "other types" of investments (for equity transactions). Compilers are also asked in their presentation of FDI for M&As to identify all relevant transactions (for both influence and control relationships – equity share 10%-100%) and to distinguish separately those involving control relationships (*i.e.* equity share more than 50%).

277. M&A as a sub-category of FDI refers to cross-border financial transactions which qualify as FDI according to the criteria described earlier. These data do not relate to FDI positions as it would be superfluous to distinguish the stock of FDI by type. Breakdowns by type of FDI have analytical significance mostly at the time of the initial decision of the

investor and for the related transaction but not in subsequent periods. Compilers are strongly encouraged to provide “M&A type transactions” as an “of which” item of total inward and outward FDI equity transactions. More specifically, data relate only to FDI financial flows in the form of equity but *exclude* reinvested earnings and debt instruments (inter-company loans). Box 4.2 describes the recommended components of the data to be compiled.

278. Furthermore, Annex 9 provides the details on how to record M&A transactions as a part of FDI equity transactions. This annex also provides a comparison of “M&A transactions” as a part of FDI and “M&A statistics”.

### Box 4.2. **Components of M&A transactions**

| | |
|---|---|
| ***Foreign direct investment*** | |
| ***Inflows:*** *Gross* investments and divestments by non-residents | |
| Investment in equity | Divestment in equity |
| *Of which:* | *Of which:* |
| Acquisition of existing stake in resident companies by non-residents | Sale of existing stake in resident companies by non-residents |
| *i)* partner country and | *i)* partner country and |
| *ii)* industry | *ii)* industry |
| ***Outflows:*** *Gross* investments and divestments by residents | |
| Investment in equity | Divestment in equity |
| *Of which:* | *Of which:* |
| Acquisition of existing stake in non-resident companies by residents | Sale of existing stake in non-resident companies by residents |
| *i)* partner country and | *i)* partner country and |
| *ii)* industry | *ii)* industry |
| *Memo items:* Total of which M&A under control | |
| *i)* partner country and | |
| *ii)* industry | |

*Note:* The above presentation relates to the conceptual framework by country allocation and by industry classification. For data dissemination, data may be disseminated at higher level of aggregation if limited by confidentiality.

#### *4.4.2.3. FDI according to Ultimate host/investing country*

279. This *Benchmark Definition* recognizes additional user needs for information, to the extent meaningful definitions allow, on the economic distribution of direct investment capital, as well as on the countries that ultimately control direct investment enterprises. These needs have grown in recent years, as ownership structures have become more complex and as it has become more common for direct investment enterprises to be owned through intermediate entities such as holding companies and regional management centres.

280. While these needs are clear-cut, the means of addressing them sometimes are far more complex. *Conceptual* difficulties may arise, for example, when funding provided to an enterprise by a direct investor is co-mingled with other funding obtained by the enterprise before being further invested in other enterprises. In addition, practical difficulties may arise in collecting detailed information on ownership chains leading to a foreign-owned enterprise in the compiling economy. In the light of these difficulties, this *Benchmark Definition* provides recommendations only for the allocation of inward investment positions for the compiling economy to the countries where the investors controlling these

positions are established. Allocation of outward positions, across ultimate host countries (including intermediate countries in longer investment chains), remains on the research agenda. At this stage, research work has not progressed enough to reallocate outward investment in an unambiguous way across different entities down the FDI ownership chain.[37]

281. Details of the recommendations for allocating inward direct investment positions to ultimate investing countries are given in Chapter 7 as well as compilation guidance in Annex 10.

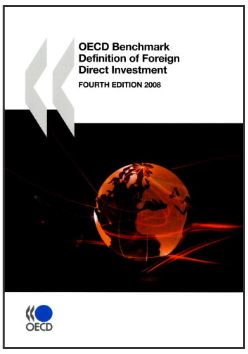
### 4.4.3. Banks and other financial intermediaries

282. The *Benchmark Definition* recommends that, in the case of banks and other affiliated financial intermediaries, all inter-company flows and positions – with the exception of those pertaining to equity investment – with related financial intermediaries should be excluded from direct investment flows. Deposits and other amounts lent by a parent bank or other financial intermediary to its direct investment enterprise located abroad that is also a financial intermediary, and deposits and other borrowings taken from such offices, should also not be classified as direct investment.

### 4.4.4. Financial leases

283. Wherever an operator (the lessee) acquires an asset under a financial (or capital) lease (as distinct from an operating lease), the legal owner of the assets (the lessor) should be regarded as making a loan to the lessee that the lessee uses to buy the assets. If this arrangement is between a direct investor and its direct investment enterprise, the loan should be included in direct investment, and be treated according to the provisions of this *Benchmark Definition*, in the same way that a conventional loan would be regarded and treated. The SNA states that a financial lease arrangement is to be taken as presumptive evidence that a change of ownership is intended. A change of ownership is imputed because the lessee assumes all rights, risks, rewards, and responsibilities of ownership in practice and, from an economic point of view, can be regarded as the *de facto* owner. The financial lease essentially is a method of financing the purchase of the good by the lessee (as opposed to taking out a loan for the purchase). During the life of the financial lease, the lessor expects to recover most or all of the cost of the goods and carrying charges.

37. Attempts to allocate investments to ultimate host countries are hampered by difficulties related to the inter-changeability of money – linking specific sources of funding with specific uses – and by the fact that direct investments made by intermediate enterprises in ownership chains may reflect not only funding provided by direct investors, but also funding that these enterprises may, in turn, have obtained from other sources, such as local owners or lenders. Consequently, more work needs to be done to determine whether it is possible to develop reallocation schemes of outward investments.

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