GCC COORDINATED FOREIGN INVESTMENT SURVEY (CFIS)

Guidelines on Use of Financial statements for validating or deriving information on foreign investment

(Chapter X of the Compilation Guide of the GCC-CFIS)

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Chapter X: Use of Financial statements for validating or deriving information on foreign investment

1. Among the sources available to compile FIS, survey of relevant enterprises together with their financial statements are the most important. Financial statements help to validate data reported by enterprises (a term used to denote single companies/branches or a group of related companies). These statements could also be used to obtain data when companies/enterprises do not respond to questionnaires.

2. This chapter will discuss the use of financial statements under the following topics:

A) Types of financial statements commonly used in the GCC countries;

B) A General Template of a Financial Statement and how to read it for the FI survey;

C) Correlation table between a financial statement and the GCC Coordinated FI survey questionnaire.

D) Distinction between the local enterprise group and global enterprise group;

E) Identification and exclusion from Financial Statements of data on FI position and financial flows between (1) residents on both sides, and/or (b) non-residents on both sides; that is, excluding resident to resident and non-resident to non-resident positions and flows.

F) Identification in the financial statement of data relevant to local enterprise group, or arriving from global enterprise group data and to local enterprise group data.

G) Completion of the questionnaire of GCC Coordinated FI survey in case of no response;

H) FIS data validation and verification using financial statements

A. Types of financial statements of financial statements commonly prepared/available/used in the GCC countries.

3. Financial statements consist of a related series of statements of a single business entity (branch, subsidiary, affiliate, holding company, parent company etc.) or that of related entities under common control with emphasis on certain aspects such as geographical or product specialization.

4. The most important of these financial statements is the balance sheet which portrays the financial position at a point of time (year, quarter or month end) of a single entity or that of a series of single entities that are under common control such as a conglomerate or enterprise. The balance sheet consists of two main sections, assets and liabilities. Liabilities are sub-divided into two main categories called Shareholders' Equity and other non- equity liabilities to both shareholders and third parties. Information on the term or maturity (short or long term) of the various assets and liabilities items could be derived from the balance sheet. Where the accounting definition of the term of a debt liability (short/long term) differs from that of BOP/IIP, adequate information is usually available from notes to the financial statements, to convert balance sheet data to conform to the BOP/IIP concepts. In a balance sheet any repayment on a long- term debt that is due in less than 12 months is classified as a short-term debt, whereas such repayments would be regarded as long-term according to BOP concepts. So, the Balance sheet will show an increase in short term and decrease in long term debt which is not due to financial transactions but to re-classification. According to BOP concepts, there would have been no change in short term or long - term positions due to the accounting treatment of re-classification of the debt from long-term to short term.

5. Foreign investments could be either inward, outward or both and consist of equity and debt. For BOP/IIP presentations, FI are also classified functionally as direct, portfolio, financial derivatives and other investments. Further, direct investment could be presented on a directional principle or on an assets/liabilities basis. All other functional classifications for BOP/IIP data purposes have always been presented on an assets/liabilities basis. Data to construct the BOP/IIP data come from both sides of the balance sheet. These will be explained in a later section (Derivation of BOP/IIP data from Balance Sheets). Balance sheets do not classify data on a functional basis. The BOP/IIP compilers need to extract the data from the balance sheet or notes to the financial statements and fit them into the functional classifications, maturity profiles of debt (as explained in the previous paragraph).

6. The relevance of the balance sheet to data required on the GCCSTAT questionnaire will be discussed in detail elsewhere in this chapter.

7. Another important financial statement is the Income or Profit/Loss Statement. This will have data on some current account items of BOP such as primary income (interest, dividends and reinvested earnings accruing on FDI) and flows related to changes in assets/liabilities related to FI, for example the counterpart entry in the financial transactions reflected in the direct investment income attributed to reinvested earnings.

8. Other data that could be obtained/derived from the Profit/Loss Statement or notes pertaining to it, both for BOP/ IIP data as well as for the activities of the MNCs as required by the CFIS of the GCCSTAT include profits/loss arising from the normal operations of companies in contrast to their comprehensive income. The difference between comprehensive income and income arising from normal operations relate to some of the factors other than financial transactions in the flows category which explains the change in stock positions of FI between two consecutive periods. Use of the data on profits from normal operations and comprehensive income for BOP/IIP data will be discussed in another section.

9. The other financial statements could be called subsidiary statements to the two main financial statements. These are the Statement on Retained Earnings and Sources and Uses of Funds.

10. The various financial statements referred to above could be presented by companies/enterprises either on a (a) Consolidated or (b) Unconsolidated basis.

11. Consolidated financial statements are prepared for a group of related companies, also known as enterprises. A case in point is the multinational corporations (MNC) which in addition to operating in two or more countries may also be a conglomerate with operations in more than one industry.

12. Consolidated financial statements could be prepared at various levels such as:

(1) Global – At this level, the operations of a typical MNC will be reflected in one single set of financial statements that will consolidate the financial statements of its individual entities operating worldwide.

(2) Regional –This is a sub-set of a global consolidation. The regional level could be at the level of a Continent or an Economic Grouping of Countries such as the European Union or Gulf Cooperation Council of Countries.

(3) Sub-regional – This is a sub-set of a region such as the ASEAN within the Asian region, or the GCC within the Middle Eastern region.

(4) Individual country – A MNC could have many entities in an individual country. They may or may not be held by the same holding company in that country. They may have different holding companies which in turn may have reporting responsibilities to holding companies based in different regions based on the nature of their activities. Some of the entities may not be part of a country- based holding company but may report to an immediate parent company at the sub-regional or regional level and in some cases even to the ultimate controlling company. This may be the case for financing or administrative entities established in tax haven countries.

(5) In any country, a single entity or related group of entities may be ultimately controlled by non-residents or residents. That particular country is considered a host country for

the non-residents' controlled entities and home country for resident controlled companies. In the case of entities controlled by non-residents, they could have different types of financial statements related to (a) single entity in the host country (b) group of related entities in the host country (c) single or related entities consolidated on a sub-regional, regional or global basis. A resident controlled company similarly could have financial accounts according to a single entity, group of related entities and if it has overseas investments, on a sub-regional, regional and global basis.

(6) When the financial statements of a related group of enterprises in a country is consolidated, it is called local enterprise group's financial statement. If a global enterprise is a conglomerate, its various entities in a country may represent different industries and they may have different reporting relationships to host country, external intermediate or ultimate parent companies. In such cases, there will be more than one local consolidated financial statement. It is usual for the head entity of a nonresident controlled conglomerate in a country to consolidate those units that belong to its own enterprise structure in an industrial sector such as in manufacturing, mining or financial. If the nonresident controlled conglomerate has investments in more than one industrial sector in a country, there is likely to be parallel enterprise structures in that country represented by different parent companies at the investee country level. The units that belong to these parallel enterprise structures will be sister corporations or fellow enterprises to one another. A country parent company will consolidate all the controlled entities in its own organizational structure (more than 50% owned); report investments on an equity basis in all of its associates (those that are owned between 20% and less than 50%); and on a cost basis where ownership of companies is less than 20%. The method of reporting on global, sub-regional or individual country consolidation will follow the same basis – that is full consolidation, equity and cost basis. In the case of joint ventures (typically two companies each owning 50% ownership), each party will own or take responsibility for debt instruments, usually in proportion to their equity interest. In that case, each partner will include 50% of the assets/liabilities of the partnership company in its own financial statement. A separate financial statement will be available for the joint venture company as well.

(7) In addition to the above, enterprises will also have financial statements for individual companies/branches in their own enterprise structure. In the case of shipping companies, it appears to be a normal practice for companies to incorporate each ship as a separate entity, normally in a tax haven country or in countries where there are lax labor laws. Investments in a branch is denoted by the Head Office account which represents the net financial investments in a branch.

(8) The ultimate controlling interest of an enterprise group (whether domestic or non-resident) may reside with a corporation (represented by its Board of Directors), a powerful group of majority or minority shareholders, government, trust, non-profit organization, family, an individual or any combination of several owners. The residence of the ultimate controlling entity of an enterprise group may differ from the residence of the corporate entity at the apex of an enterprise group. For instance, the

corporate apex of a multinational enterprise may be in the United States or a tax haven country. However, the ultimate controlling interest of such an entity may be a resident of another country. This can be illustrated from the ultimate control of the global Zain (Kuwait) resident in Kuwait with investments in several countries. All the information given below on Zain (Kuwait) is gathered from publicly available data, principally through the google search engine. The following is the ownership structure of Zain (Kuwait) as of May 21, 2018:

Table 1 - Zain Shareholders: As of May 21, 2018

Ownership structure	**In percent to total**
Kuwait Investment Authority (KIA) - Kuwait	24.6%
Oman Telecommunications (Omantel) - Oman	21.9%
Nohoudh Development Trading & Contracting co. - Kuwait	5.05%
Public – Global portfolio investors	48.45%

According to the above ownership structure of Zain (Kuwait), its principal shareholder is KIA with ownership of 24.6%. The second biggest shareholder is Omantel with 21.9% ownership. The third principal shareholder is a distant third with ownership of 5.05%. The rest are portfolio shareholders spread globally. Hence no single shareholder has absolute controlling interest (50%+ ownership). This is typically a management-controlled company. The management is based in Kuwait. Does it mean its ultimate control is in Kuwait? In the case of Zain (Kuwait), it is not necessarily so for the following reasons:

- Although, KIA is the biggest shareholder, it is a passive investor. It does not participate actively in management decisions.
- Nohoudh Development's ownership is far too small to be part of a controlling group of shareholders.
- The global shareholders are too diversified and as such will not be able to act in concert as one group or a substantial group.
- Hence, it is the management that will control the company
- However, the management does not operate in a vacuum
- It in turn is influenced and controlled by the substantial shareholders who are KIA and Omantel
- Since KIA is a passive investor and may not necessarily have expertise in telecommunications, it will be content to let Omantel control the company for all practical purposes. Omantel will always have the tacit support of KIA.
- In the event of a major shareholder discontent with the management of Zain, KIA and Omantel will have 46.9% of shares and if they have Noboudh Development on its side, the combined group will have 51.55 % of shares. If it does not get Noboudh Development's support, KIA and Omantel could set out to obtain the proxies of about 3.2% of other owners to exercise effective control.
- In effect, Zain is effectively, a joint controlled company – KIA and Omantel

- However, for all practical purposes, Zain is effectively controlled by Omantel.
- If further prove of effective control is needed, Omantel, fully consolidates the world -wide operations of Zain. Hence, in its balance sheet, it shows the value of the non-Omantel shareholders of Zain. Usually, a company will consolidate the accounts of only companies in which it holds majority shares and calls the equity of the other shareholders as minority interest. However, when Omantel consolidates Zain, what should be minority interest becomes majority interest.
- Most importantly, Omantel is represented by five out of eight members on the Board of Directors of Zain since 2017 when it acquired an additional 10% of shares to bring up its total shares held to21.9 %.

(9) There are both public and private companies. Public companies are those whose shares are traded on various stock exchanges. They are obliged to publish their financial statements so that these are available to current and prospective shareholders. Private companies are not obliged to publish their financial statements although they are obliged to provide them to certain regulatory and other government agencies. In countries, where there are laws governing provision of statistics to a statistical agency, the private companies may be required to provide financial statements along with completing questionnaires requesting data on financial statistics.

(10) All the GCC countries have Sovereign Wealth Funds (SWFs). In the UAE, there are several. These are important vehicles for FI and to a smaller extent to domestic investments. Their domestic investments will not be considered as foreign, since they are residents to residents investment. Most of their investments excluding real estate investments appear to be portfolio or other investments. However, they do not disclose their financial data. In these cases, institutions responsible for data collection should addressed key people at the highest levels of government to obtain relevant data or use partner country data. Host countries will be able to collect data on investments made by foreign based SWFs in their own countries but not any data on their world-wide investment activities. However SWFs data are not made available to their home countries' statistical authorities.

B. General Template of a Financial Statement and how to read it for the FI survey

13. The following extract on financial statements is taken from Wikipedia (Free Encyclopedia). It describes in a very succinct manner, the four different kinds of financial statements.

Box 1: FINANCIAL STATEMENTS

(Source: https://en.wikipedia.org/wiki/Financial_statement)

"**Financial statements** (or **financial reports**) are formal records of the financial activities and position of a business, person, or other entity.

Relevant financial information is presented in a structured manner and in a form which is easy to understand. They typically include four basic financial statements accompanied by a management discussion and analysis:

1. A balance sheet or **statement of financial position**, reports on a company's assets, liabilities, and owners equity at a given point in time.

2. An income statement—or **profit and loss report** (**P&L report**), or **statement of comprehensive income**, or **statement of revenue & expense**—reports on a company's income, expenses, and profits over a stated period of time. A profit and loss statement provides information on the operation of the enterprise. These include sales and the various expenses incurred during the stated period.

3. A statement of changes in equity or **equity statement**, or **statement of retained earnings**, reports on the changes in equity of the company over a stated period of time.

4. A cash flow statement reports on a company's cash flow activities, particularly its operating, investing and financing activities over a stated period of time.

(Notably, a balance sheet represents a *single point in time*, where the income statement, the statement of changes in equity, and the cash flow statement each represent activities over a stated *period of time*.)

For large corporations, these statements may be complex and may include an extensive set of **footnotes to the financial statements** and **management discussion and analysis**. The notes typically describe each item on the balance sheet, income statement and cash flow statement in further detail. Notes to financial statements are considered an integral part of the financial statements".

14. Financial statements vary from very simple ones to very complex reports. FIS compilers will generally deal with only a very few complex reports, typically associated with reports of MNCs. However, the data derived from them could account for as much as about 80% of the value of any functional data such as the FDI in a country.

Box 2. Consolidated Statement, Profit or Loss, Year-End 2018 and 2017

XYZ Corporation

Any Currency '000

Financial Items	**Note**	**2018**	**2017**
Revenue	**18**	**1,087,774**	**1,137,547**
Cost of Sales		(266,764)	(259,945)
Gross Profit		**821,010**	**877,602**
Operating and Administrative Expenses	19	(308,174)	(373,797)
Depreciation and Amortization	12,13	(222,307)	(212,751)
Provision for impairment – trade and other receivables	5	(1,296)	(5,303)

Operating Profit		**289,233**	**285,751**
Interest income		5,992	7,243
Investment Income	20	(3,925)	(5,863)
Share of results of Associates and Joint Ventures	8,9	(30,781)	(29,297)
Other income/expenses		(22,793)	(4,832)
Finance costs		(32,598)	(29,029)
Loss from currency revaluation		(42,044)	(22,119)
Net monetary gain	32	(30,781)	-
Profit before Corporate Social Responsibility Projects		193,865	201,854
Income tax and Board Remuneration	21,22	(35,130)	(35,736)
Profit for the Year		**158,735**	**166,118**
Attributable to :			
Shareholders of the Company		156,702	154,314
Non-controlling interests		2,033	11,804

Box 3. Consolidated Statement – Profit or Loss and other Comprehensive income

Year Ended 2018 and 2017
XYZ Corporation

Any Currency '000

Financial Items	**2018**	**2017**
Profit for the year	158,735	166,118
Other comprehensive income (Items that may be re-classified subsequently to profit and loss account)		
Exchange differences on translating foreign operations	(342,525)	(73,395)
Net unrealized loss/gain on available for sale investments	847	(5,269)
Net loss transferred to consolidated statement of profit or loss on sale of available for sale investment (net of impairment loss)	4,083	2,618
Cash flow hedges	96	1,715
Total comprehensive income for the year	(178,764)	(91,787)
Comprehensive income attributable to:		
Shareholders of the company	(181,723)	73,742
Non-controlling interests	2,959	18,045
Total	(178,764)	91,787

Box 4. Consolidated Statement of Financial Position at 31 December 2018

Year Ended 2018 and 2017
XYZ Corporation

Any Currency '000

Financial Items	Note	2018	2017
ASSETS			
Current assets			
Cash and bank balances	4	208,752	359,799
Trade and other receivables	5	450,386	406,581
Inventories	6	16,418	27,593
Investment securities at fair value through profit/loss	7	964	1,164
Total		676,520	795,137
Non-current assets			
Investment securities available for sale	7	22,134	26,598
Investment in associates and joint ventures	8,9	190,396	219,902
Dues from associates	10	381,661	350,673
Other assets	11	15,598	15,880
Property and equipment	12	798.156	901,679
Intangible assets and goodwill	13	1,007,237	
Total		2.415,182	2,700,044
Total assets		3,091,702	3,495,181
LIABILITIES AND EQUITY			
Current liabilities			
Trade and other payables	14	570,920	761,758
Due to banks	15	219,154	213,330
Total		790,074	975,068
Non-current liabilities			
Due to banks	15	830,193	751,569
Other non-current liabilities	16	48,953	40,454
Total		879,146	792,023
Equity		1,422,482	1,728,090
Attributable to Company shareholders		1,265,129	1,542,692
Share capital	17	432,706	432,706
Share premium		1,707,164	1,707,164
Treasury shares		(567,834)	(567,834)
Various reserves		(878,413)	(538,539)
Retained earnings		571,503	510,641
Non- controlling interest		157,353	185,398
Total Liabilities And Equity		3,091,702	3,495,181

C. Correlation table between a financial statement and the GCC Coordinated FI Survey questionnaire

Correlation between Section 1 of the CFIS and the Financial Statement

15. Section 1 deals with identification information about the reporting entity. Information given in this section gives clues to what a compiler may expect to find in the rest of the questionnaire and to what extent they are borne out by the information in the rest of the questionnaire and or in the financial statement.

16. Section 1.1.1 – Requests the name of the company. In most cases, the name may be a clue to the principal activity of the company. For instance, if the name is ABC Manufacturing Company, a correlation may exist with 1.2 which requests information on the principal activity of the company. In most cases, the principal activity would be identified as manufacturing. However, a company, originally starting out as a manufacturing company, may have subsequently become largely a trading company. However, the name may not have been changed to reflect the new reality. Hence, in spite of its name, the principal activity will be identified as wholesale/retail trade. If it is a global trading company, one would expect to find payables to/receivables from non-residents including its non-resident parent company and fellow enterprises abroad. The main Balance Sheet will not differentiate among direct investors and others but notes to the FS will identify separately, positions with related parties. Again related parties may be residents or nonresidents.

17. Some companies will have two or more owners. It is likely that one or more partners may be non-residents and in which case this would be an in-scope company for the survey. In some cases, especially in petroleum and natural gas companies, associated with production sharing or development sharing agreements, the partners will report only their share of financial transactions/positions and not that of the other partners. So an indication of partnership in PSAs and DSAs should alert the compilers to perhaps some non-resident partners.

18. Section 1.5 – If information is submitted correctly in this section, there will not be any non-resident equity in 1.5.1. There will be 100% foreign ownership in 1.5.2, most of it FDI and others significant FPI. In 1.5. 3, there is likely to be some FPI and perhaps FDI. In 1.5.4. and 1.5.5 there could be some FDI and FPI.

19. Section 1.6 – This is an important section that determines the type of financial statements needed for use in compilation of FIS.

20. 1.6.1 refers to a single company without subsidiaries and associates in either the reporting country or abroad. So, it will have only a single financial statement for itself. This is a purely domestic owned company without any inward/outward FDI but may have inward/outward FPI/FOI.

21. 1.6.2 The holding company could be domestically owned or a foreign direct investment enterprise. It may be a subsidiary of an immediate parent company with an

ultimate controlling company. The holding company could present its financial accounts in various ways. It could provide (a) non-consolidated financial statements, (b) consolidate the subsidiaries and associates in the country of its residence (LEG) or (c) consolidate its subsidiaries and associates directly related to it through ownership on a global-wide basis (GEG). The intermediate and the ultimate holding companies may follow the same pattern of reporting. These different types of financial statements are normally not relevant for the compiler of FIS in the host countries. Financial statements of companies that are at the apex of global enterprise groups, often refer to their investments on a geographical basis, either by a geographical region or even by single countries in the event of significant investments. **In the event a subsidiary of a MNC in a host country does not respond to the FIS questionnaire or provide its own financial statements, then the financial statements of the intermediate or ultimate controlling company should be looked at to see whether there are any references there to the value of investment by the enterprise group in the host country.** Whether a company responds to a survey or not, all relevant companies should be encouraged to submit their financial statements. They serve the purpose of validating reported data. In the event of non-response to questionnaires, the major FIS data (if not all the details) can be derived from financial statements. For instance, administrative data on share ownership could be applied to obtain FDI and FPI equity investments. In the event some companies do not provide financial statements, compilers in some instances have alternative sources to obtain them. **Some countries require all companies to deposit their financial statements with designated governmental ministries or agencies (e.g. Nigeria and the Philippines). There is a requirement for companies whose shares are traded on stock exchanges to publish their financial statements and additionally also in newspapers. Regulatory agencies such as the central banks and others that regulate insurance and other financial institutions and utilities and taxation authorities also have access to financial statements**. Statistical agencies should explore all these avenues to obtain relevant financial statements to compile data on inward and outward FI.

22. 1.6.3 refers to the branch of a foreign company in the reporting country. A branch does not have a legal existence of its own. It is part of another company. However, for statistical, taxation and other purposes (e.g. keeping track of its operations), branch financial accounts are available. A branch may not be able to enter into financial or business contracts or raise funds for operations on its own. The Head Office assumes responsibility for the financial transactions of a branch. **So, essentially the branch and the head office maintain an account which is called the Head Office Account.** The net asset position in that account in favor of the Head Office would represent FDI in the host country and net liability position, negative FDI. Rather than survey the branches with a separate questionnaire, the Head Office/Home Office Account data is requested in line 8 of Section 4 (Shareholders' Equity). Please note that there are no shareholders in a branch. It is an intrinsic part of an entity. Line 4.8 would enable branches to report the net Head Office Account. Without that line, the branches would return the questionnaire marked "not applicable" since there are no shareholders in a branch. In practice, a branch is like a wholly owned subsidiary. But unlike a subsidiary, a branch does not have any shareholders since it is part of another entity. A branch has no legal existence but for statistical purposes, it is considered as a separate entity.

23. 1.7.1 refers to the ultimate controlling parent of an entity. An ultimate controlling parent (UCP) is an investor or individual) at the top of the ownership chain and is not controlled by another investor. An undisputed UCP is one who owns 50%+ voting shares of an entity. However, many enterprises, especially those whose shares are traded on the stock market, effectively control an entity with less than 50% voting shares since the ownership is diversified. In some cases, even a minority shareholder will be able to control an entity because of certain special circumstances. An instance of that is the UCP of Zain (Kuwait) which is described elsewhere in the chapter. **Most financial statements do not customarily give information on share ownership.** In some cases, an event like a significant acquisition of shares by a person that could affect control of an entity may prompt it to refer to share ownership as in the case of Zain (Kuwait). **Sources of share ownership are government entities that register commercial entities, stock exchanges, investment promotion agencies and regulatory organizations and most importantly through surveys of FI**. Data on UCP is useful for policy makers as in some instances it is not the direct investor (immediate parent) but the UCP who influences the activities of a foreign direct investment enterprise. Historically, very few countries have collected data based on ultimate control. Hence, there is some interest to collect FIS on ultimate control. Currently, information on UCP is used to determine the direction of FDI of fellow enterprises in some instances.

24. 1.7.2 refers to information on immediate direct investor who is defined as someone owning 10% or more of the voting shares of an entity. In most cases it is the entities that are effectively controlled that are consolidated in the financial statements of a controlling entity. If not effectively controlled, an entity will be considered as an associate if 20% and 50% of its shares are held by it. Investment in that associate will be represented on an equity basis and not fully consolidated. Transactions and ownership positions in those associates are referred to as that in **related entities** in notes to the financial statements. **They may or may not be individually identified or their residency disclosed.** In any case this information can be used by compilers as leads to get data that otherwise may not be available. Follow ups could be made with company officials to find out the names and residency of such associates.

25. Section 2 requests data on financial assets (claims) on non-residents. Section 3 requests data on financial liabilities to non-residents. These two sections have been designed to meet the data requirements as specified in *BPM6* to report claims on and liabilities to non - residents on an assets and /liabilities basis. But the cells in these sections can be cross arranged to obtain data on the directional principle for FDI as was specified in *BPM5*. **GCCSTAT and policy makers require FDI data on the directional principle (*BPM5* concept) whereas for compilation of BOP and IIP data, the assets/liabilities presentation is used.** All other functional classifications of financial instruments (portfolio, financial derivatives and other investments) have always been presented on an assets/liabilities basis whether one followed *BPM5* or *BPM6* concepts. **The switch to presenting FDI on an assets/liabilities basis was to enable the presentation of all functional classifications of financial instruments on a gross assets and / liabilities basis in the IIP statistical tables rather than present FDI on a net basis (according to the directional principle) and all other functional classifications on a gross assets/liabilities basis.** However, some users of FDI data require them on the directional basis which is more appropriate to analyze inward and outward FDI. GCCSTAT requires FDI data for analytical purposes on a directional

basis. For compilation of BOP/IIP data, the central banks of the GCC countries (as also compilers of BOP/IIP data in other countries) require data on the assets/liabilities basis. **IMF's CDIS Survey collects data on FDI on the directional principle**. The principal purpose of the CDIS survey is to obtain data on the geographical dispersion to enable data reconciliation between partner countries especially when large discrepancies exist and thereby reduce global discrepancies in reported data by home and host countries.

26. Both Sections 2 and Section 3 have other subsidiary sections which are required for various data facets which are difficult to be represented in a single section. As expertise in FI data collection developed in many countries, more surveys were developed focusing on certain important data facets. Such developments evolved gradually from the days of highly abridged single surveys on FI. At the time of the introduction of *BPM6*, while some countries had highly sophisticated surveys on FI (some with more than 10 principal surveys to cover various aspects of FI both inward and outward investments and to take account of required data periodicity such as annual and quarterly), other countries had none and depended on the reporting by commercial banks of international transactions to the central banks for compilation of BOP data or on estimates based on other data sources, primarily administrative data and the media. **The approach of the GCCSTAT was to have one omnibus survey that would cover all the requirements for FI data by both BOP/IIP data compilers as well as policy makers.** This was indeed a difficult challenge. Among other advantages, it ensured that scarce statistical resources were concentrated on a single survey rather than on several surveys. As requirements for quarterly data arose, three GCC countries have developed surveys for them. Two of them collect quarterly data on all functional classifications of FI data both inwards and outwards while the other collects data on inward FDI only. **Having one omnibus annual survey to collect data on inwards and outwards FI has certain disadvantages.** Both compilers and respondents need to fully grasp the concepts of FI and how they are to be reported on the questionnaire. Since the financial data are extracted from the financial statements of the respondents, the latter need to know the concepts of FI (both according to *BPM5 and BPM6)* so that they could provide the appropriate requested data. However, in practice, this does not happen. **Corporate financial officials simply do not have the time to learn BOP/IIP concepts (with all the exceptions to commonly accepted accounting terms) to report data correctly. Data collectors and compilers may not have sufficient accounting knowledge to effectively communicate with data providers. Hence, it is unavoidable that data collectors and compilers need some basic accounting knowledge to communicate effectively with data providers.**

27. Section 2 and its associated Sections 6, and parts of 8 and 9 are on outward FI except for the data on reverse investments associated with direct investment liabilities. Section 3 and its and its associated Sections 4, 5, 7 and parts of 8 and 9 are on inward FI except for the data on reverse investments associated with direct investment assets.

28. The rest of this section on the questionnaire will focus on the type of data that is requested and how available data in the financial statements will help to validate reported data as well as to estimate data for non-responses.

29. Section 2 is on “Financial Assets (Claims) on Non-residents”. It requests data on the reporting countries’ investments abroad (assets) by resident enterprises whether they are controlled by the reporting country or by non-residents. Data are required by financial instruments and investments in related and unrelated parties. This enables to compile (a) FDI related equity investments abroad in direct investment enterprise (DIE)– 2-A-1 (b) adjustments necessary for inward FDI for reverse investment- 2-A- 2 (c) either equity FDI abroad in fellow enterprises or adjustments necessary for inward FDI depending on the ultimate control of the reporting enterprise – 2-A-3 and (d) portfolio investments abroad – 2-A-4

30. Data for the above should be reported according to the consolidated financial statement of the Local Enterprise Group (LEG) as reported in Section 11 of the questionnaire. Section 11 is very important. Very often, if an enterprise has many subsidiaries and associates, there is likely to be one or more holding companies at the top of the companies operating in the reporting country. The questionnaires should therefore be directed to the holding companies which should be requested to file a consolidated financial statement for their investees. **However, not all holding companies especially the non-resident controlled holding companies will consolidate the accounts of their investees. Hence, investments held abroad by the operating companies and associates will not be reported. In those cases, the questionnaire should be sent to the operating companies.**

31. Section A will comprise total for one or several investees. The data reported in Sections A – I, will all be on the book values of the reporting entity (the investor). **According to BOP/IIP data compilation conventions, the values should reflect those in the books of the investees**. **That would necessitate additional response burden on both respondents and compilers.** Further, compilation of FIS is a relatively new statistical work in the GCC countries and hence there are staff constraints, that is the number of experienced and trained staff to do compilation. **Also, the focus in the GCC countries is on inward FI because of special circumstances. Much of the investments abroad is by the Sovereign Wealth Funds (SWFs) and expats resident in the GCC countries. GCC based SWFs with perhaps two exceptions are not willing to disclose their data to statistical agencies or central banks.** The statistical issue associated with the SWFs is not peculiar to those in the GCC countries. It is so in the case of the SWFs in other countries as well. Although, investments abroad by SWFs based in investor countries are difficult to track by the statisticians of those countries, it is less difficult for statisticians in the investee countries to track inward investments. For this reason, in countries where SWFs are active, investee countries will have better knowledge of their investments than the investor countries. This is so since in the investee countries, the data are collected from the investee enterprises and not from the investor SWFs. **There are commercial data bases that track the origins ad destinations of SWFs’ investments through media information and other sources. It would be cheaper for compilers to use such sources to the alternative of employing their own resources to obtain this data.** Data gaps that exist for outward investments between investor countries and the corresponding amounts for inward investments for investee countries could be partly resolved through partner country data reconciliation exercises where substantial differences exist. The data collected by IMF’s CDIS and CPIS could be of some help in identifying substantial data inconsistencies. **However, GCC compilers do not resort**

to either of these alternatives. However, GCC compilers do not resort to either of these alternatives.

32. In 2. A.1. since investments data are required to be submitted for the local enterprise group (LEG) and not on a regional or global consolidated basis for the reporting entity, FDI equity should be reported either on an equity or cost basis. Equity basis would be for all entities in which the reporting entity has over 20 percent of the value of common shares. Equity basis means the cost of the original investment plus the share of the investor in the rest of the equity account (mainly retained earnings but also reserves) since the acquisition of its investment. Any investment with less than 20% ownership of common shares will be shown at cost. **Enterprises consider investments of less than 20% of equity as essentially portfolio investments, some of which are held for short term trading purposes only. According to BOP/IIP concepts, ownership of more than 10% in the equity of a company is considered FDI. More detailed information on these investments may or may not be disclosed in the notes to the financial statements of the companies.** If such information is disclosed, it is mostly on their investments in associates (over 20% ownership of equity) rather than on investments held at cost. The investments reflected in 2.A.1 are made by both companies ultimately controlled in the reporting countries as well as by nonresident controlled companies with operations in the reporting country.

33. 2.A.2. **represents equity investments made by DIE in the reporting country in their parent companies abroad. This represents a foreign asset for the reporting company and hence is appropriate in a statement that represents FDI on a strictly assets/liabilities basis. However, on a directional principle, this data will be deducted from reported inwards FDI by the reporting entity. It is highly unlikely that any data will be reported for this cell since it is on very rare occasions that a subsidiary or associate makes an investment in its parent company.**

34. 2.A.3. represents equity investments abroad in fellow enterprises. These investees are part of the family of enterprises of the investor group. **By definition, a fellow enterprise is one in which the investor (a member of the family of the investor group) has an equity investment that ranges from 0% to less than 10%. If the equity investment reaches 10% or more, it is considered a DIE and not a fellow enterprise.** Again, it is not usual to find equity investments in fellow enterprises. However, it is more likely to find investments related to debt instruments related to trade and debt financing for investments in fellow enterprises which is described elsewhere in this chapter.

35. 2.A.4. **represents any equity investment made in investees other than those mentioned in 2.A.1 - 2.A.3. By definition, the equity investments reported in 2.A.4 need to be less than 10% and the investees should not be part of the family of enterprises of the investor.** All such investments will be reported in a single line on the assets side of the balance sheet of the reporting entity. There is not likely to be any further details provided in the notes to the financial statements of the value of individual stock, geographical dispersion or industrial characteristic. Therefore, to obtain information on geographical or industrial characteristics, contacts need to be made with the respondents where the amounts are large. If

the amounts are small, they could be classified to the “other” category in geographical and industrial characteristics.

36. Section B is on investment abroad in debt securities. Debt securities are part of debt instruments. They are differentiated from other debt instruments because they are securitized while other debt instruments are not. Debt securities are tradable financial instruments whereas other debt instruments are not.

37. Sections B 1-4 are the same as Section A 1-4 where the direction of investment, the investees and functional classification of investments are concerned. The only difference between the two sections is that Section A is on equity securities whereas Section B is on debt securities. **Balance sheets may report investments in debt securities separately from equity securities. They may report their values at cost or at current market prices. It is not likely to find more details on these investments in notes to the financial statements except if the amounts are substantial and if there are any concerns about these investments in terms of tradability or safety of investments.**

38. Section C. Currency and deposits assets. These transactions are usually between two financial entities or at least one of them would be a financial entity. These financial transactions should be treated as other financial investments, even in the case of transactions between two related deposit taking entities such as commercial banks. Functionally, there are no direct or portfolio investments associated with these investments. The compilers should classify all data reported in Section C as short term foreign other investments (FOI) abroad.

39. Section D is on loan assets and is different from Section B since these are not tradable financial instruments. Therefore, they are categorized as other debt instruments and not as debt securities. Otherwise, Sections D 1-4 are the same as Section A 1-4 for non-financial corporations where the direction of investment, the investees and functional classification of investments are concerned. **Notes to the financial statements are likely to have more details on these investments. If they do, they will show investments in D 1 – 3 under the heading, investments with related parties without differentiating the counter parties as residents of the reporting country or nonresidents**. In the event of substantial loans, the notes will specify the name of the counter parties, residency etc. From these, they could be identified as residents or nonresidents. If differentiation between residents and nonresidents could not be made from the notes, then contact with company officials could be made to get appropriate information. For financial corporations, the categories D 1-4 are considered as foreign other investments. The compilers need to note that the functional classification of loan assets are different in the case of financial and non-financial entities.

40. **Loan assets would be shown as short and long term. There is an important distinction in this classification between the financial statements and the BOP/IIP concepts. A financial statement will treat all loans due within 12 months as short term. These apply to installment payments made on long term loans as well. Any installment payment due within 12 months will be classified as short term. In BOP/IIP, any loan with original maturity of over one year is classified always as long term, including**

installment payments due within 12 months. Using the notes, compilers should adjust the short/long term classification in the financial statements.

41. Section E - Insurance, pension and standardized guarantee scheme assets should be treated the same as data reported in Section C, in that they are treated as other foreign assets and there are no direct or portfolio related investments.

42. Section F - Trade credit and advances assets. The treatment of F 1-4 should be the same as in D except the maturity profile of these investments are short term. **There is likely to be details pertaining to these in the notes to the financial statements which are useful to identify the counter parties and destinations of investments.**

43. Section G - Other accounts receivables. Same treatment as for Section F and **similar information likely to be found in the notes to the financial statements.**

44. Section H - Financial derivatives are based on other underlying financial instruments. At the time of striking a contract between two parties, derivatives have zero values for either party. Over a period, one party "is in the money" (assets) and the other party is not (liabilities). During the life of a derivative, the value and the designation between assets and liabilities could oscillate for either party. An entity may enter into several financial derivatives contracts and at any given point of time, they will be classified as assets or liabilities. Periodic changes will be reflected as other changes in stock positions and not as financial transactions in the financial statements.

45. Section I - Employee stock options are a sub-set of financial derivatives.

46. The questionnaire format of Section 3 is the mirror image of Section 2. Whereas Section 2 requires data on assets abroad, Section 3 requires data on liabilities to non-residents.

Changes in stock Positions – Sections 2 and 3.

47. Both Sections 2 (Assets) and 3 (liabilities) request beginning and end of year stock positions and changes by net transactions and other changes during the year. Changes in positions are called flows. Flows should not be confused with financial transactions. Flows are composed of net financial transactions and other changes. Financial transactions take place between residents and nonresidents on account of both assets and liabilities. Transactions on assets should be kept separate from that of liabilities. Transactions in assets or liabilities can be in either direction. It could be from residents to nonresidents or vice versa in assets and separately in liabilities. Whether in assets or liabilities, they should be netted out. Gross transaction in either assets or liabilities are not required to be reported. In short term financial instruments such as trade payables/receivables, there could be hundreds of gross transactions (increases/decreases) between residents and non-residents and it would be very time consuming for respondents to compile them for purpose of reporting them on the questionnaire.

48. **Other changes are those caused to stock positions by factors other than financial transactions such as changes in exchange rates, prices, write offs, revaluations etc. These changes are reflected in the comprehensive income of enterprises. Notes to the financial statements refer in some details about the items in the comprehensive income that are different from net profits and loss**. If these changes are limited to a few recognizable financial instruments that could be attributed to the appropriate investees/investors, then compilers may be able to determine the correct cells where they should be reported. This is not always the case. **Therefore, compilers depend pretty much on what the respondents report.** However, most respondents do not even differentiate between net transactions and other changes. Data is reported undifferentiated either in the net transactions or other changes column to minimize response burden.

49. There is another significant challenge for both respondents and compilers. For assets abroad, the respondents may have to report for several entities in Section 2 and not for one entity as in the case of liabilities in Section 3. Then the changes to the combined assets need to be differentiated between financial flows and other changes. **Reporting changes for liabilities is much easier since these are reported for one entity only – the reporting entity.**

50. In practice, very few companies report components of the changes of stocks (that is financial transactions and other changes) correctly. Most companies attribute the total changes to either net transactions or other changes. **For BOP data, it is necessary to obtain data on financial transactions. Flows data (that is financial transactions and other changes) will not do. Due to response burden, appeals to the companies to report these data correctly will not elicit positive responses. This is where financial statements could be of some help to determine whether companies are reporting these data correctly and if not explore possibilities of effecting changes to reported data through data in the financial statements**. It is not always that companies will have changes to stocks caused by other factors. So, if companies do not report other changes to stock positions and if there is no difference in the reported data on net profits and comprehensive income, then it is established that the company's reporting is correct. However, if the company has reported comprehensive income that is different from the net profits and does not report other changes, it is possible that the company's reporting is not correct. **Other changes may have occurred in investments between residents and residents and therefore have no implications for investments between residents and non- residents**.

51. **To what extent is it then possible for the compilers to derive the other changes from data reported in the financial statements and accompanying notes?** In some cases, it may be possible if the other changes are few and related to financial instruments such as those denominated in currencies other than the reporting currencies or certain assets or liabilities that have been written off or revalued. Since data are requested by financial instruments by different types of investees/investors, and other changes could be spread over many financial instruments, it would be very time consuming for compilers to apportion other changes to appropriate financial instruments by different investees/investors and related to asets/liabilities between residents and non-residents (excluding those between residents and residents). Further, the compilers will not have enough financial information (as much as the

company accountants have) to make such estimates. Therefore, it would be easier for the compilers to determine broadly what the net financial transactions are between residents and non-residents for various financial instruments and then derive other changes residually. Since reporting data is very time consuming and only limited time is available for respondents to assemble and report data and for compilers to validate and compile quarterly and annual FI data to meet deadlines, practical measures need to be adopted to compile quality data on a timely basis. Therefore, the compilers need to concentrate their attention on the few enterprises that account for a substantial amount of FI. **Any errors committed because of lack of close scrutiny given to the editing of small and medium sized enterprises is not likely to affect the overall quality of the data.**

Section 4 – Shareholders' Equity

52. Equity investments are usually more predominant than debt instruments in FDI. In addition to initial equity investments, established enterprises reinvest substantial part of their earnings, thereby increasing equity. However, there are exceptions. In manufacturing industries such as petro-chemicals that use oil and gas as raw materials, huge amounts of capital are required. Parent companies may borrow these funds from banks in their home countries and on-lend them to the DIE or arrange for the DIE to borrow directly from foreign banks. In the latter case, foreign other investments may be higher than FDI during certain phases of investment. Over time, when these investments are paid off, equity investments tend to become more predominant.

53. **Although, according to accounting concepts, preferred shares are part of equity securities, according to BOP/IIP concepts they should be treated as debt securities. In the questionnaire, they are left in the Shareholders' equity, so as not to confuse the respondents who are mostly accountants. If any data are reported for preferred shares, they should be transferred to the section on debt securities. This would have the effect of reducing the amount shown in Section 7 (Grand Total). This would also reduce the total equity investment and correspondingly increase the amount of debt investments through increase in debt securities.**

54. Very few enterprises float preferred shares. Therefore, not more than a handful of enterprises will show preferred shares. Therefore, for purpose of compilation of FI, BOP and IIP data, preferred shares will not be part of paid-up capital in 4.1.

55. Data reported in 4.1.2 Contributed Common Shares of non-residents is a component of inward FDI and FPI equity. BOP/IIP concepts are used to define FDI and FPI. Three types of direct investors are identified – (a) non-resident direct investors (1.2.2.1) (b) foreign direct investment enterprises (1.2.2.2) and (c) fellow enterprises abroad (1.2.2.3). Data reported enables compilation of FDI by either the directional principle or on assets/liabilities basis. For instance, 1.2.2.2 is reverse investment in the case of inward investment (outflow of inward FDI or negative inward FDI). When the concept of assets/liabilities is used, it will constitute part of FDI liabilities. It is not likely that fellow enterprises and FDIE abroad will make equity FDI in a FDIE of a host country. Their FDI is more likely to be in the form of debt instruments.

56. Lines 1.2.2.4 represents portfolio equity liabilities to non-residents. Portfolio investors are those who hold less than 10% of the voting shares of a company. A respondent may not always be able to identify all the related entities of a direct investor. Hence some of the FDI may be misclassified to FPI. Similarly, some respondents may total up all the portfolio investments from a country and if they total 10% or more, they may report them as FDI. Editors need to watch out for such errors and make necessary adjustments.

57. Notes to the financial statements may identify transactions with related parties by name but not always by geographical identity. Related parties may include residents whose transactions are not relevant for BOP/IIP data.

58. 4.2 Treasury stock are those shares already issued but bought back by the company from existing shareholders in a share buy- back program. Treasury stock does not mean authorized but unissued shares. Share buy backs are initiated for various reasons. It may be done to make future incentive payments to employees in the form of shares of companies; to increase per share earnings by reducing the number of shares in the hands of investors or the company might decide that of all the alternatives available at a given time, the best form of investment is in itself. Treasury stock has the effect of reducing the total shareholders' equity.

59. 4.3 Retained earnings indicate accumulated profits /losses from normal operations of the company that have not been distributed to the shareholders. The term retained earnings and reinvested earnings are used interchangeably by accountants and others except the BOP/IIP compilers. The latter make a distinction between the two terms. For them, retained earnings mean, accumulated undistributed earnings but reinvested earnings mean undistributed profits for a particular period such as a quarter or a year. In BOP data, earnings of direct investors are shown in two separate lines (a) dividends (b) reinvested earnings (also known as undistributed earnings for the indicated period). Since, it is not a cash payment, the contra entry in the BOP account is FDI inflows. No such calculation is made for payments made or accruing to portfolio investors. Respondents may not report or report incorrectly these data on the questionnaire. Therefore, compilers should make appropriate calculations for both direct investment income payments and financial transactions using the data in the Shareholders' Equity, and the Income Account of the company which identifies normal earnings of the company and other comprehensive earnings.

60. 4.4 All types of Reserves apply to the various reserves set up, both on account of statutory requirements and others for prudent management of funds by the company. The reserves are funded out of the earnings of the company. Other comprehensive earnings are not included in retained earnings but in one of the reserves.

61. 4.5 Companies will identify the various types of reserves separately. If a company identifies the reserve set up for other accumulated other comprehensive income separately, it would help to calculate reinvested earnings correctly.

62. 4.6 In a fully consolidated financial statement, minority interest would represent ownership of equity by the non-controlling entities.

63. 4.7 represents the total Shareholders' Equity. From this total, FDI and FPI data are derived using the respective shares owned by the direct and portfolio shareholders. For inward FDI, data can be derived by the different types of direct investors and also by directional and assets/liabilities basis. Respondents report these data in detail in Section 3 of the Questionnaire – Financial Liabilities to Non-Residents. They may not always report these data diligently because of the time requires. Therefore, compilers need to cross check data reported in Sections 3 and 5 carefully to ensure accuracy of reporting.

64. 4.8 A branch is not a company. It is part of a company. It has no shareholders. This item is added as a memorandum item to the Shareholders' Equity in order to obtain the investments made by branches in a host country by foreign based companies. The net Head /Home office Account represents the net FDI in the host country. If a questionnaire is sent to a branch without this memorandum item, it will likely not give any data indicating that since it is a branch, there are no shareholders in it.

Sections 5, 6 and 7– Outward Foreign Direct Investment

65. Data obtained on Sections 5, 6 and 7 are further details on inward and outward FDI obtained in Sections 2, 3, 4. These details are on geographical origins and destinations of FDI by countries and by industry by direct investors, direct investment enterprises and fellow enterprises which include flows (differentiated by transactions and other factors). Flows and positions include those related to assets and liabilities, including those related to reverse investments. It should be noted that the concept of reverse investments is applied to FDI only and not to the other functional classifications such as portfolio and other investments. These details enable construction of FDI data on the basis of both directional principle and assets/liabilities for each country of origin and destination of FDI.

66. Sections 5 and 7 seek data on inward FDI by country of residence and industry of DIE and fellow enterprises on the directional and assets/liabilities bases. Therefore, data are sought separately on liabilities owed to direct investors and fellow enterprises abroad and reverse investments by the DIE on the direct investors in their home countries. Data sought are on stocks (positions) at the beginning and end of year; flows (financial transactions and other changes separately identified); and by equity and financial instruments during the period. Data on financial instruments sought include those on debt securities and all other financial debt instruments as one category instead of distinguishing between debt securities and other debt instruments by the different types such as loans, trade receivables/payables etc. The data on maturity profiles (long/short) is also not requested.

67. The data requested would be reported for each of the direct investor's country of residence. If there are more than one country of residence for the direct investors, data for them need to be reported separately. **Investments made through holding companies in the host country should be carefully analyzed to ensure that they are reported on a consolidated LEG basis and not on a cost basis. Otherwise, investments made through holding companies could be understated.**

68. Sections 6 and 7 seek data on FDI abroad by country of residence and industry of DIE and fellow enterprises on the directional and assets/liabilities bases. Therefore, data are

sought separately on assets held on DIE enterprises and fellow enterprises abroad and reverse investments by the non-resident entities on the direct investors in the home country. Data sought are on stocks (positions) at the beginning and end of year; flows (financial transactions and other changes separately identified); and by equity and financial instruments during the period. Data on financial instruments sought include those on debt securities and all other financial debt instruments as one category instead of distinguishing between debt securities and other debt instruments by the different types such as loans, trade receivables/payables etc. The data on maturity profiles (long/short) is also not requested.

69. The data requested would be reported for each of the non-resident entity abroad (DIE/fellow enterprise). If there are more than one entity in a foreign country, data for them need to be reported separately. **Investment made through holding companies abroad in other entities abroad should not lead to duplication of investments abroad since investments between holding companies abroad and their subsidiaries and associates would be non-residents to non-residents transactions.** In fact, the existence of holding companies abroad through which other investments are held abroad could result in understating the values of FDI abroad since the direct investors may show their investments in the holding companies at cost. The holding companies too may not show their investments in their subsidiaries on an equity basis (that is they may not show their share of retained earnings in their subsidiaries in their own books).

70. According to *BPM 6* and also BPM5 and earlier IMF manuals, FDI abroad should be compiled according to the financial statements of the entities abroad. For this reason and for a better validation of reported data, compilers should request the respondents to submit the financial statements of all their entities abroad. The values reflected in the books of the foreign entities may not necessarily coincide with the values carried in the books of the direct investors in the home countries.

71. Data requested on DIEs and Fellow Enterprises including reverse investments are reported separately as follows:

Sections 8 and 9 – Portfolio Investments – Assets and Liabilities

72. Section 8 requests information on the stock (positions) of portfolio investments at the beginning and end of the year, differentiated between equity and debt instruments by country of non-resident issuer/holder. For assets abroad, the industry of the home country entity is used, the same for the liabilities. Flows are derived as changes in positions between two consecutive periods.

73. Section 9 – Income Receivables from and Payables to Non-Residents

74. Section 9 requests Income receipts from and payments to non-residents by interest, dividends and undistributed profits (re-invested earnings) by direct investors, DIEs, fellow enterprises abroad other unrelated non-residents. The questions have been structured to obtain payments and receipts on direct, portfolio and other investments. The only issue is whether these are reported gross or net of withholding taxes. The financial statements could be helpful in the case of inward investments to determine whether the data supplied is on a gross or net basis.

Section 10 – Activities of your Enterprises

75. There is much interest by policy makers on the activities of MNCs. Data requested on the questionnaire include total assets, net worth, characteristics of employment and wages, value added, exports and imports, differentiated by goods and services and selected expenditures on services such as research and development, training expenditure and payments for royalties and license fees.

76. Some of the requested data such as on total assets, net worth, value added, gross comprehensive earnings, taxes on earnings, net comprehensive earnings, differentiated between earnings from normal operations and other earnings (exchange and price effects) could be obtained from the financial statements. Some MNCs may give data on exports and imports and services payments made to related parties abroad in notes to the financial statements. However detailed data on employment and wages are not be disclosed in the financial statements.

Section 11 – Local Enterprise Group (LEG)

77. Section 11 requests whether financial data on companies (subsidiaries) controlled (usually owned 50+%) by the reporting company are included. It does not ask for data on associates (those owned 20 - 50%) or other ownerships of less than 10%. It is also necessary to request whether such companies are fully consolidated or whether the investments are carried on an equity or cost basis.

78. The Enterprise structure of the LEG will also include the associates in which the share ownership will vary between 20% - 50%. The accounts of these will not be fully consolidated. The ownership interest will be reflected in the accounts of the local parent on an equity basis.

79. To make the picture complete, it is necessary to obtain data on investments less than 20% with a subset of data for investments between 10% - 20% since FDI is defined as investments over 10%. All investments under 20% will be carried in the local parent's accounts on a cost basis.

D. Distinction between the local enterprise group and global enterprise group.

80. The distinction between the local enterprise group and the global enterprise group is very vital for the compilers of FIS. What the compilers of FIS in each country need is a financial consolidation based on the local enterprise group since the global enterprise group will comprise the consolidated accounts of the worldwide units of the global enterprise.

81. It is the practice of MNCs especially the conglomerates that may have investments in several different industries in a country, to manage their investments in different ways. Operational supervision or line management of these entities may be effected through a regionally based external entity which may or may not have the ownership interest in those companies. The holding company may have ownership, represented by a nominal equity

contribution but will not get involved in the management of the entity. The holding company in the host country will act essentially as a conduit for financial, trade (especially services) and income transactions between its investees in the host country and its immediate parent company, regional holding company, ultimate parent or fellow enterprises abroad. The holding company may provide certain administrative services for these entities. In most cases, these holding companies do not consolidate the accounts of these entities. The entities prepare their own financial statements as stand-alone entities. When the mapping of the ownership links of such companies is done, the tendency for the compilers is to send the questionnaire to the holding company to report on behalf of the entities under its ownership. However, if the holding company does not consolidate the accounts of its entities, the full extent of the operations of the Group will not be reflected.

82. Refer to this in Section 3. Hence, much of the investment reflected in the operating companies will be missed out, if their investments in the operating companies are carried at cost of investments (that is not including their share of retained earnings and reserves in the equity of the operating companies) in the holding companies. In such cases, questionnaires should be sent to the investee companies. However, the investee companies may not report non-resident equity investment since the holding companies are residents of the reporting country. Hence the compilers need to look through the holding company to determine foreign ownership of equity investment. A simple way to do that would be to add the retained earnings and reserves accounts of the holding company to the total value of the shareholders' equity of the operating companies if the latter attributes the holding company's investment in them as a resident investment.

83. The global enterprise group represents the worldwide corporate structure of an enterprise of which the LEG of any country is a part. It will help the compilers to know the worldwide structure of an MNC to fully understand the activities of an MNC and perhaps to identify the ultimate control of some of the fellow enterprises. But it is not necessary to know all the links. It is enough to know only the essential links that relate to the operations of the entities in the host countries.

84. Financial statements for an entity of a global MNC in a host country will be available at different levels of the global enterprise – at a single company level in the host country, at the LEG level, at the immediate non-resident parent company level, at the regional level of the MNC and finally at the global level. The financial statements that are appropriate for a host country are the consolidated financial statements at the LEG level.

E. Residents on Both Sides and Non-Residents on Both Sides

85. References to identification and exclusion from Financial Statements of data on FI position and financial flows between (1) residents on both sides, and/or (b) non-residents on both sides; that is, excluding resident to resident and non-resident to non-resident positions and flows are made to the above issues in other Sections of this report especially in Section H.

F. Arriving from global enterprise group data and to local enterprise group data

86. It is not possible to arrive at local group data from global enterprise group data except for the relevant associates and joint ventures which are not consolidated with the data of the global enterprises. These could be done to some extent with the help of notes to the financial statements as explained in Section H. Some MNC refer to assets held in various geographical regions or major countries of investment. While some data such as total assets could be had, it is not possible to categorize them by functional and financial instruments by maturity. See also Section H.

G. FIS data validation and verification using financial statements

87. Editors need essentially (a) the Balance Sheet and (b) the Income or Profit and Loss Account for data validation and verification of data reported using financial statements. The major uses are as follows:

1. Verification of data reported on Shareholders' Equity – Section 4 and Sections 2 and 3 of GCCSTAT's CFIS. Non-resident equity is one of the biggest components of foreign investments especially FDI. However, FDI is not always reported correctly in Section 4. Respondents sometimes report all investments from the country of residency of foreign direct investor as FDI. Some of them calculate FDI on the value of common shares rather than on total equity. Other errors include failure to identify direct investments in the range of 10% - 20% of equity. Failure to identify fellow enterprises as direct investors is another short coming.

2. In the case of FI abroad, it is more difficult to identify FDI exactly as financial statements of investees abroad are not requested or provided. In the Balance Sheet shown on pages 10 - 11 of this report, the following data is given for assets

3. Since this is a consolidated statement, all the accounts of the controlled entities (usually ownership of shares of 50% + but not necessarily always) will be consolidated. The current and non-current assets will show the consolidated amounts plus the amounts not consolidated. These assets will include both domestic and assets held abroad. Usually, the notes will be helpful to distinguish domestic assets from those held abroad but not always.

4. Notes 8, 9, and 10 will cover FDI abroad if some of them are foreign entities. If some of them cannot be identified as FDI abroad, queries should be made to the respondents. By definition, joint ventures are 50% owned and their accounts will not be fully consolidated. Dues from non-resident associates covered in Note 10 will be long-term loans and should be classified to FDI abroad. Other assets covered by Note 11 may include long term loans made to entities in which the share ownership may vary between 10%-20% which are not associates according to accountants but FDI entities according to BOP/IIP concepts. Therefore, follow up queries should be made to the respondents for further information to determine the nature of those assets if enough information is not given in Note 11.

Table 2 - Consolidated Statement of Financial Position at 31 December 2018, Assets

Year Ended 2018 and 2017

XYZ Corporation

Any Currency '000

Financial Items	**Notes**	**2018**	**2017**
Assets			
Current assets			
Cash and bank balances	4	208,752	359,799
Trade and other receivables	5	450,386	406,581
Inventories	6	16,418	27,593
Investment securities at fair value through profit/loss	7	964	1,164
Total		**676,520**	**795,137**
Non-current assets			
Investment securities available for sale	7	22,134	26,598
Investment in associates and joint ventures	8,9	190,396	219,902
Dues from associates	10	381,661	350,673
Other assets	11	15,598	15,880
Property and equipment	12	798,156	901,679
Intangible assets and goodwill	13	1,007,237	
Total		**2.415,182**	**2,700,044**
Total assets		**3,091,702**	**3,495,181**

5. Note 7 covers investment securities, both short and long-term. They could be either equity or debt securities and either domestic or foreign securities. If Note 7 does not clarify these, the amounts reported in 2.A. 4 and 2.B.4 should be cross checked. If there is still doubt about proper classification, queries should be made to the respondents.

6. If cash and bank balances held abroad are identified (Note 4, Balance Sheet), the amounts reported should be cross checked with the item reported in 2.C.4 in the CFIS. If the amounts differ, a query should be made to the respondent. The verified amount will be classified as FOI abroad.

7. Note 5 is on trade and other receivables. Transactions with related parties will be identified separately. The note may mention the names of the related parties but may not identify them as domestic or non-resident. Sometimes, the names may give a clue to whether they are residents or non-residents. Otherwise queries should be made to the respondents. The identified trade and other receivables should be checked with items reported on 2.F.1-4. Those identified as with related parties abroad could fall into any of the categories 2.F. 1-3. And would be classified to various FDI abroad categories. Assets with non-related parties abroad would be classified to FOI.

8. The following is the Liabilities section of the same Balance sheet noted above.

Table 3 - Consolidated Statement of Financial Position at 31 December 2018, Liabilities

Year Ended 2018 and 2017
XYZ Corporation

Any currency '000

Financial Items	**Notes**	**2018**	**2017**
Liabilities			
Current liabilities			
Trade and other payables	14	570,920	761,758
Due to banks	15	219,154	213,330
Total		**790,074**	**975,068**
Non-current liabilities			
Due to banks	15	830,193	751,569
Other non-current liabilities	16	48,953	40,454
Total		**879,146**	**792,023**

9. The same procedure should be followed for these liabilities identified as owned by non-residents as followed for the assets items. In this case, the validation will be done in reference to the counterpart items reported in Section 3 of the CFIS. The biggest liabilities are to the banks followed by trade and other payables. The relevant liabilities are those of the home country based entity to no-residents. The liabilities of the relevant non-resident entities to other non-residents are not relevant. If the notes do not disclose enough information, queries should be made to the respondents.

10. Note that dues to banks are both short and long term. These may all have been originally long term loans. According to accounting convention, loans due in less than 12 months are classified as short term whereas according to BOP/IIP conventions, the original long term loans are treated as such until they are all repaid. If the loans owed in less than 12 months are classified as short term in the financial statements, then the editors should re-classify them back to long-term.

11. Some of the other non-current liabilities covered in Note 16 may be due to non-residents. Cross check that with data reported in Section 3.D.

12. The following statement of equity is from the Balance Sheet data shown above for a typical global consolidated financial statement. Therefore, it will not compare with an equity statement based on LEG consolidation. What is needed by compilers is a consolidation based on LEG. Therefore, if the data reported on CFIS and the accompanying global financial statement data are the same, then the data reported is incorrect.

Table 4 - Consolidated Statement of Financial Position at 31 December 2018, Equity

Year Ended 2018 and 2017
XYZ Corporation

Any Currency '000

Financial Items	Notes	2018	2017
Equity		**1,422,482**	**1,728,090**
Attributable to Company shareholders		**1,265,129**	**1,542,692**
Share capital	17	432,706	432,706
Share premium		1,707,164	1,707,164
Treasury shares		(567,834)	(567,834)
Various reserves		(878,413)	(538,539)
Retained earnings		571,503	510,641
Non- controlling interest		**157,353**	**185,398**
Total equity		**2,212,566**	**2,703,158**

13. The following statement helps to differentiate the profits from normal operations from other income of the company (also known as other comprehensive income). This is the subset of the Profit and Loss or Income account. What is important for the BOP/IIP and FI accounts is the data on profit/loss from normal operation of the company. It is this amount that will be taken into the retained earnings. Other comprehensive income will be allocated to various reserves. In the case of this entity, most of the loss recorded on other comprehensive income has come about as a result of adverse exchange rate movements in respect of assets denominated in foreign currency (probably on assets held abroad). However, when some of the for sale assets are sold, the realized funds may differ from what was booked historically in the reserves. Hence adjustments are made to the historically recorded data for retained earnings and the appropriate reserve accounts.

Table 5 - Consolidated Statement – Profit or Loss and other Comprehensive income

Year Ended 2018 and 2017

XYZ Corporation

Any Currency '000

Financial Items	2018	2017
Profit for the year	158,735	166,118
Other comprehensive income (Items that may be re-classified subsequently to profit and loss account)		
Exchange differences on translating foreign operations	(342,525)	(73,395)
Net unrealized loss/gain on available for sale investments	847	(5,269)
Net loss transferred to consolidated statement of profit or loss on sale of available for sale investment (net of impairment loss)	4,083	2,618
Cash flow hedges	96	1,715
Total comprehensive income for the year	**(178,764)**	**(91,787)**
Comprehensive income attributable to:		
Shareholders of the company	(181,723)	73,742
Non-controlling interests	2,959	18,045
Total	**(178,764)**	**91,787**

14. The Profit and Loss Account is also a source to extract other BOP/IIP related data. Some data needed to gauge the activities of the MNCs are also available from the P&L account.

15. The BOP related items are identified in the following subset of the P&L account. Interest income may arise from domestic or foreign sources. However, there is no footnote for this item. Hence, it could be assumed that it is from domestic sources and that there are no BOP implications. Investment income shows negative amounts. Therefore, they cannot be dividend receipts. In this case, note 20 should be looked at for an explanation. Share of results of Associates and Joint Ventures are negative for both years. That means, on balance, the various Associates and Joint Ventures made net losses. Notes 8 and 9 should provide explanations. Depending on the locations of these entities (home/host countries), they could impact inward/outward FDI. Finance costs are borrowing costs or interest payments. These will have BOP implications only if one of the parties is a non-resident. If they are non-residents to non-resident transactions, or residents to resident transactions, there are no BOP implications. Since there are no notes, the assumption may be made that they are residents to residents' transactions. Loss from currency revaluation noted in the P&L account is a currency revaluation that impacts the current year's normal operations and is not part of other comprehensive income. So is the net monetary gain. Note 32 should be read for an explanation of this item. The sum of the items shown in **Table 12** will not equal the profit for the year as there are other financial items in the P&L Account.

Table 6 - Consolidated Statement – Profit or Loss – Year Ended 2018 and 2017 – Selected Items.

XYZ Corporation

Any Currency '000

Financial Items	**Note**	**2018**	**2017**
Interest income		5,992	7,243
Investment Income	20	(3,925)	(5,863)
Share of results of Associates and Joint Ventures	8,9	(30,781)	(29,297)
Finance costs		(32,598)	(29,029)
Loss from currency revaluation		(42,044)	(22,119)
Net monetary gain	32	(30,781)	-
Profit for the Year		158,735	166,118

16. Some data items needed for the activities of the MNCs can also be derived from the Consolidated Statement of Profit and Loss. These include revenue, cost of sales and profit for the year from normal operations, excluding other comprehensive income. MNC data include that on exports and imports. Enterprises that derive a large part of their revenues from exports of goods and services may show these data as subsets of revenue or refer to them in notes to the financial statements. Similarly, if imports form a large part of the cost of sales, they will be shown as a subset of cost of sales or references will be made in notes to the financial statements.

Table 13. Consolidated Statement – Profit or Loss – Selected Items - Year Ended 2018 and 2017

XYZ Corporation

Any Currency '000

Financial Items	**Note**	**2018**	**2017**
Revenue	18	1,087,774	1,137,547
Cost of Sales		(266,764)	(259,945)
Profit for the Year		158,735	166,118