

**I. DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)**  
**II. OUTCOME PAPER (DITEG) # 3**

April 8, 2005

1. **Topic: Indirect investment: Fully Consolidated System, U.S. Method or 50 per cent ownership**
2. **Issues: See DITEG Issue Papers # 3 Indirect Investment – FCS, USM and 50 percent Ownership: Determining Direct Investment Relationships by Australia (ABS- November 2004); Background document #3 Determining Direct Investment Relationships: Cross Holdings of Investments and Direct Investment Relationships by Australia (ABS - February 2005); Background document #3 Determining Direct Investment Relationships: Reconciliation of the differences in the definitions of Foreign Direct Investment used in the Balance of Payments Textbook and the OECD Benchmark Definition of Foreign Direct Investment by Australia (ABS - January 2005); Background document #3 Indirect Investment: FCS, USM or 50% Ownership, prepared by the US Bureau of Economic Analysis (March 2005)**
  - (i) As the Committee and the WIIS had endorsed the Fully Consolidated System (FCS) as representing the best basis for capturing indirect direct investment relationships, the issues and background papers from the Australian Bureau of Statistics were prepared to clarify fundamental issues relating to the concept underlying the identification of direct investment relationship, the interpretation of the various sets of rules used to determine these relationships, and to highlight differences between the *Balance of Payments Textbook* and the *Benchmark Definition of Foreign Direct Investment* in the definitions of direct investment. The papers confirmed that the various systems are based on same concept that the differences in definitions are small, but they may result in different interpretations. The papers provided no information on the materiality of these differences. Some members felt that the differences may be swamped by variability in reporting, and therefore may have little impact.
  - (ii) The issues paper introduced a hybrid system which attempted to illustrate an application of related *BPM5* principles for purposes of discussion. The paper highlighted some ambiguity in the implied residence of units in the FCS. Discussion at DITEG confirmed this ambiguity and emphasized the need for clear guidance in the revised standards.
  - (iii) The group discussed the very useful background paper from the US Bureau of Economic Analysis that provided data comparing the FCS, the USM, and the 50 percent ownership approach. Though the results were biased, in that the US could only use the data in its own database to make the comparisons, and therefore, some offsetting differences from using different databases based on the EUM were omitted, the results indicated that, at the aggregate level, the differences between the different approaches were small. For some bilateral and some industry data, the differences were quite large. The differences between the USM and the FCS were smaller than those between the USM and the 50 percent ownership approach.

- (iv) Subsequent discussion of the Ultimate Beneficial Owner (UBO)<sup>1</sup> identified close links between the direct investment relationships determined under the FCS and related systems and those which need to be taken into account in determining the UBO.

**3. Recommendations:**

- (i) The concept underlying the determination of direct investment relationships be confirmed as being the existence of significant influence of one unit over another through an equity holding.
- (ii) The aim of the recommended system FCS and alternate systems US and EU systems be confirmed as being to determine the extent of the existence of significant influence through a chain of equity holdings.
- (iii) Work on determining direct investment relationships is to be coordinated with work on determining UBO.

**4. Rejected Alternatives:**

DITEG did not take a view on the acceptability of the hybrid approach.

**5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)**

- (i) Do the Committee and the WIIS agree that the concept underlying the determination of direct investment relationships is the existence of significant influence of one unit over another through an equity holding?*
- (ii) Do the Committee and the WIIS agree that the US and EU systems, which both aim to determine the extent of the existence of significant influence through a chain of equity holdings, represent reasonable proxies to the FCS?*
- (iii) Do the Committee and the WIIS agree that work on determining direct investment relationships should be coordinated with work on determining UBO?*

Disclaimer:

The views expressed in this paper are those of the author and should not be attributed to the International Monetary Fund, its Executive Board, or its management.

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<sup>1</sup> See also DITEG outcome paper #12(I) on Ultimate Beneficial Owner.