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COMMUNICATION FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT

**on progress in harmonization of GNP
and the evaluation of financial support**

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1. Summary and conclusions

The decisions of the Edinburgh European Council concerning the financing of the Community for the period 1993 to 1999 envisaged a gradual replacement over the period 1995 to 1999 of the third resource, based on VAT, by the fourth resource, based on GNP, as the main source of Community finance. Work will therefore need to be speeded up if there is to be the most solid and equitable basis possible for the Member States' contributions to the Community budget.

The work carried out by the Commission with the assistance of the GNP Committee has revealed shortcomings in the comparability of the GNP of the Member States.

1. The Commission has already adopted Decisions aimed at clarifying certain rules of the European System of Integrated Economic Accounts (ESA) and ensuring that they are applied in a uniform fashion in all the Member States. Other Decisions will also be proposed.

Two areas could be improved as regards the reliability of the accounts: the production of national business registers and the extension of statistics to cover market services would be in line with the concerns of the Community statistical programme and action has already been undertaken in both these areas.

2. Work should in future concentrate mainly on evaluating the underground economy and integrating it into the national accounts.

Some Member States have made more effort than others to cover this part of the economy, even in the case of countries with similar levels of statistical development.

The Commission has adopted a programme of work on the underground economy and a timetable with a view to obtaining reliable results by 1 October 1995, the date by which the Commission must be informed of the GNPs (pursuant to Article 3 of the Directive).

3. In order to examine the possibility of including corrections for tax evasion and avoidance in the present estimates, the programme includes a section concerning the use of the results of tax audits. Most of the Member States' delegations present at the meeting of the GNP Committee stressed the difficulties of obtaining access to these results and the Commission therefore calls on the competent national authorities to facilitate cooperation between the tax authorities and the statistical institutes.

4. It will not be possible to implement this programme of work unless the Member States and the Community are able to finance the necessary actions in the various countries with a view to improving estimates of the underground economy.

The Commission urges the Member States to take measures to allocate the necessary resources to the statistical institutes.

The Commission will have to support this effort. Community financing has been estimated at ECU 3 million, of which 1 million has been taken from the Eurostat^(*) credits in the Commission budget for 1993.

(*) Statistical Office of the European Communities (Eurostat).

2. Introduction

- 2.1 Since 1988, the gross national products of the Member States have formed the basis of a new form of Community own resource. The Council Directive on the harmonization of the compilation of gross national product at market prices (GNP)^(*) therefore establishes a procedure for verifying and assessing the comparability and representativeness of the GNP of the Community Member States calculated in accordance with the European System of Integrated Economic Accounts (ESA).

In addition, the Edinburgh European Council (11-12 December 1992) made a statement concerning the financing of the Community for the period from 1993 to 1999 and, in particular, adopted a modification to the structure of own resources which would result in an increase in the relative weight of GNP, thus increasing the need for comparable and representative GNP data, as provided for in the GNP Directive.

- 2.2 On 31 March 1992, the Commission submitted to the Council a report on the application of the Directive, in accordance with Article 10 thereof.

In this report it made a general assessment of the degree of harmonization achieved in the GNP of the Member States so far. This assessment was based on an initial analysis of the inventories of the basic statistics and procedures used to calculate GNP provided by the Member States in accordance with Article 4 of the Directive. It can be summarized as follows:

- GNP is reasonably comparable in the majority of the Member States as far as the regular economy is concerned, i.e. that part of the economy which takes due account of the relevant economic and social regulations.
- However, there are shortcomings in a number of Member States and appropriate action has been taken to rectify this situation.
- There would appear to be a need to improve coverage of economic activity by the national accounts in order to take more accurate account of activities which, for various reasons, escape current statistical enquiry and in order to obtain more systematic information on activities carried out without due respect for the relevant economic and social regulations, which it has been agreed to call the "underground economy".

- 2.3 The aim of the action undertaken is to increase the degree of harmonization of GNP. The approaches adopted have been discussed in the Committee set up by the Directive:

- Certain specific subjects have been identified as requiring ad hoc decisions so that that field covered by GNP can be dealt with progressively. Measures aimed at clarifying certain ESA definitions and ensuring their uniform application in all the Member States have been proposed and in some cases already adopted.
- The Commission^(**) has drawn up a report on each of the Member States on the basis of the inventories and additional contacts. These reports particularly stress that the reliability of GNP depends on factors which are largely beyond the direct responsibility of the national accounts departments, as evinced by the need to produce central business registers and to extend statistics on market services.
- All the Member States have made efforts to cover the underground economy, but some more than others. The Member States are aware of the work they have to do to make up for the shortcomings in this area.

(*) Council Directive of 13 February 1989 (89/130/EEC, Euratom), OJ No L49, 21.2.89, p. 26.

(**) Statistical Office of the European Communities (Eurostat).

It will not be possible to complete the work programme concerning the exhaustiveness of GNP measurements drawn up by the Commission by the end of 1995 unless the necessary financial resource both national and Community, are granted to the Member States.

It should be borne in mind that when the Directive was adopted the minutes of the Council meeting contained the following declaration in connection with Article 7 of the Directive: "The Council and Commission declare that the Committee shall concentrate its work on increasing the degree of coverage of the so-called underground economy in the context of national accounts."

2.4 In accordance with Article 10(8) of Council Regulation No 1552/89 on own resources^(*), the 1988 GNP data have been made definitive except as regards the points notified by the Commission by 30 September 1992. The Commission has therefore expressed a number of reservations for each Member State regarding the points which need to be improved. These reservations will make it possible to correct the financial contributions of the Member States retroactively.

2.5 The improvement of the quality of the accounts has benefited from the financial contribution provided for in Article 8 of Directive: the ECU 6 million deemed necessary have thus been made available to the Member States following the 1989, 1990, 1991 and 1992 budget years. The use of these credits is outlined in the annex to this communication.

Further work on harmonizing GNP, particularly to take account of the underground economy, with a view to having harmonized data by the end of 1995, will require additional financial support of ECU 2 million. This aid will be used for actions carried out in each Member State under the responsibility of the national statistical institute.

3. Harmonization of GNP

3.1 The work undertaken

The work on harmonizing GNP first required the Member States to produce an inventory of the procedures and basic statistics used for calculating their GNP.

On the basis of these inventories as well as additional contacts, a report was drawn up by the Commission on the various countries, which was submitted to the GNP Committee at its meetings in July and September 1992. These reports are largely devoted to assessing non-financial and non-agricultural market activities in the regular economy, excluding housing services. In addition to a critical assessment, they contain precise recommendations for improving the quality of current estimates for this part of the economy.

The recommendations fall into three categories:

- Some involve corrections which the Member States can introduce in a very short time - often concerning compliance with the ESA rules.
- Others stress the need to compare results from different sources. The validation of estimates of household consumption carried out in connection with the national accounts by comparing them with the most recent results of the family budget surveys or the retail trade production statistics is of relevance to all the Member States.

(*) Council Regulation of 29 May 1989, OJ No L155, 7.6.89, p. 1.

- Finally, a third type advocates the development in the majority of Member States of central business registers and the extension of the statistics to cover market services.

The recommendations set out in the country reports enabled the Commission to formulate "specific reservations" for each Member State, as opposed to reservations which were common to all the countries and concerned either the horizontal analysis themes (cf. end of part 4) or the exhaustiveness of GNP measurement, particularly as regards the underground economy (cf. end of part 6).

In addition, pursuant to Article 19 of Regulation No 1552/89 on own resources, the Commission is undertaking missions in each Member State to define a work programme and a timetable for the lifting of the specific reservations. These missions will be completed by the end of 1994.

3.2 The main harmonization problems

The definition of GNP, as of all the concepts used in national accounts, obeys certain rules. Measurement of GNP is the result of statistical work and the comparability of the GNP of the Member States presupposes the application of common accounting rules and depends on the quality of the statistical sources and valuation methods used.

1. The common accounting rules are those proposed in the European System of Integrated Economic Accounts (ESA). The Member States respect all the ESA rules affecting the measurement of GNP.

It is also necessary to take account of specific statistical matters in following the ESA. It makes the accurate quantification of the basic concepts dependent on the sources of information. In particular, the data coming from the accounts kept by the various economic operators themselves may obey specific rules and consequently need adjusting to bring them into line with the national accounts.

2. The degree of coverage of economic activity depends on the statistical sources and methods used for producing the national accounts. Ideally, coverage should be both exhaustive, in the sense that all productive operations are measured, and reliable, in the sense that the figure obtained for GNP is as accurate as possible.

Most economic activities in the Community Member States are carried out openly, particularly with due respect for tax and social security regulations. However, possibly to varying degrees from one country to another, certain economic operators conceal part of their activities and income from the authorities and certain production units even operate totally underground.

The problems of measuring the underground economy are by no means the same as those of measuring the regular economy:

- In the case of the regular economy, reliability plays a central role. The national accounts departments have information systems based on declarations by the economic operators concerning production, income received or distributed and expenditure from this income. The question therefore is to extend the observations received to the known population of economic units and, if possible, to compare assessments made according to different methods.
- The purpose of assessing the underground economy, on the other hand, is to correct the GNP figures for the effects of under-reporting by production units and to try to cover the activity of non-declared units. By their very nature, the methods used in this field can only be indirect and cannot hope to be as reliable as is possible in measuring the regular economy.

3.3 General approach to the problems of harmonization

The ideal approach would involve breaking down all the problems arising in the valuation of GNP into a number of subject groups. These would be analysed simultaneously, and proposals made, for all the 12 Member States. Given the diversity of the statistical sources and valuation methods, however, it is not possible to adopt this approach systematically.

It has therefore been decided to combine the two approaches, i.e. the subject approach and the country approach, depending on the type of problems involved. The subject approach is also referred to as the "horizontal" approach to indicate that the question is dealt with simultaneously for all 12 Member States.

Part 4 of this communication describes progress to date on the subjects of horizontal analysis.

Part 5 describes progress to date on improving the reliability of GNP measurement and particularly stresses the need to improve the statistical instruments in most Member States.

Part 6 deals with the exhaustiveness of GNP measurement and describes work in this field - particularly the work programme and timetable drawn up by the Commission.

Part 7 gives a brief outline of work undertaken in three countries (Greece, Portugal and Luxembourg), at the request and with the assistance of the Commission and the statistical institutes of certain Member States, with a view to bringing about a fundamental improvement in the methods for producing the national accounts.

4. Subjects of horizontal analysis: progress to date

4.1 A number of subjects have already been examined in connection with the Member States as a whole:

- a. The delimitation of the economic territory of the Member States is the subject of a Commission Decision^(*) which concluded the discussions in the GNP Committee. According to the Decision, the Overseas Departments must in future be included in the economic territory of France and Madeira and the Azores in the economic territory of Portugal.
- b. Classification of taxes and subsidies: at its meeting on 16 June 1993, the Commission submitted to the GNP Committee, pursuant to Article 6 of the GNP Directive, two draft Commission Decisions - one setting out a number of definitions of taxes and the other of subsidies. Since they were favourably received by the GNP Committee, these two draft Decisions were adopted.
These Decisions will particularly result in the GNP data transmitted to the Commission each year, pursuant to Article 3 of the GNP Directive, being revised in certain Member States.
- c. The question of how to evaluate housing services has been discussed in the GNP Committee; it should be finalized by mid-1994 on the basis of the guidelines proposed by the Commission.
- d. The transition from GDP to GNP: the discussion following the presentation to the GNP Committee of an initial document primarily concerned problems in connection with the integration of balance of payments data into the national accounts. It was decided to consult the Committee on Monetary, Financial and Balance of Payments Statistics. This question should also be settled by mid-1994.

(*) Commission Decision of 26 July 1991 (91/450/EEC, Euratom), OJ No L240, 29.8.91. p.36.

4.2 It is intended to discuss the following subjects for horizontal analysis during 1994:

- general government;
- financial institutions;
- agricultural activities;
- distinction between final uses and intermediate consumption;
- private non-profit institutions.

Pursuant to Article 10(8) of Council Regulation No 1552/89 on own resources, the Commission has formulated reservations for each Member State corresponding to each of the subjects for horizontal analysis mentioned above, apart from agricultural activities. These adjustments enable account to be taken retroactively of changes to GNP for 1988, which became definitive on 30 September 1992, with the particular exception of the points notified by the Commission.

5. **The reliability of the measurement of GNP: progress to date**

Of the recommendations formulated for each of the Member States, those likely to have the greatest impact on the measurement of GNP are very probably the ones connected with the production of central business registers and the extension of statistics to cover market services.

a. Business registers

An exhaustive knowledge of the statistical units is a matter of priority if the reliability of estimates is to be improved, since, for various reasons, the sources used for the national accounts do not cover all production units and it therefore needs to be possible to extrapolate from the observations made concerning those units included in current sources of information to the total population of units, or at least to those which are not deliberately trying to escape observation. For this reason, the total population of production units must be known.

Generally speaking, the Member States, apart from Denmark, France and the Netherlands, do not have a single centralized register of statistical units.

Denmark has produced a register on the basis of turnover returns in connection with VAT and employers' statutory annual wages declarations. In the Netherlands, the register of statistical units and the survey system, in which production statistics are a common element, are closely linked. In France, an interadministrative business register has been produced.

Nevertheless, in the other Member States lists have been produced for launching surveys in specific areas of activity.

In Germany, a census of local production units is carried out at the same time as the population census and in Italy periodic censuses of establishments are also organized.

In Luxembourg, the registration authorities provide Statec (Luxembourg statistical office) with a list of persons subject to VAT. In Belgium, there is also a register based on VAT returns in certain fields, which is used for production surveys.

In Greece, the periodic industrial censuses are the only reference universe with which the current surveys can be compared. The situation used to be similar in Spain and Portugal, but recently efforts have been made to produce a register of statistical units. This has resulted in the creation of the "Directorio Central de Empresas" in Spain from tax and social security records, and of the "Ficheiro Central de Empresas e Estabelecimentos" in Portugal. Both are already used for certain business surveys.

The UK Central Statistical Office, in cooperation with the Department of Employment, is also producing an interadministrative business register, initially on the basis of data contained in the VAT files and income returns. This will in due course be supplemented by other business registers used by the Government for statistical purposes.

b. Statistics on market services

In France, the use of the accounting data included with the tax returns of enterprises means that all non-financial non-agricultural businesses can be covered. In the Netherlands, the revision of the 1987 accounts benefited from the extension of standardized production statistics to cover the services sector.

However, in the other Member States, market services other than those produced by public enterprises and financial services are not completely covered by specific regular surveys. Partial surveys are conducted in certain Member States but these do not permit exhaustive coverage of market services.

These gaps are sometimes filled by using VAT statistics, at least in Denmark and Germany.

It must be stressed that the implementation of these two priority actions is not the direct responsibility of the national accounts departments alone. It also depends on the extent to which the national statistical systems are developed; the improvement of these systems is a long-term task which must take account of the concerns of the Community statistical programme, the main aim of which is to implement measures to improve the quality of the Member States' statistics and to make them more comparable.

Some work has already been done in the fields of business registers and market services.

On 18 June 1992, following a proposal by the Commission, the Council approved a two-year programme (1992-1993) for the development of European statistics in the field of services^(*), and on 22 July 1993 decided to implement a harmonized system of business registers^(**).

6. **Exhaustiveness of GNP measurement: work programme**

Questions in connection with the exhaustiveness of national accounts, and particularly the coverage of the underground economy, have been discussed at GNP Committee meetings, at which the following documents have been presented:

- . a summary of how the underground economy is covered in the national accounts of the various countries;
- . a draft programme of work in this field.

The summary was presented in the report on the application of Directive.

The contents of the work programme and the timetable are presented below.

6.1 **The contents of the work programme**

The Commission's proposals for a programme of work on exhaustiveness fall into four categories:

- a. An assessment of adjustments to the accounts in order to cover the underground economy.

It is possible that adjustments not mentioned in the inventories of statistical sources and methods used for calculating GNP provided by the Member States were not included in the summary report. It is also possible that use of certain methods at local level enables part of the underground economy to be included.

The Member States should therefore revise the summary report so that the appreciation of the present situation can be made as precise as possible.

(*) Council Decision of 18 June 1992 (92/326/EEC), OJ No L179, 1.7.92, p. 131.

(**) Council Regulation (EEC) No 2186/93, OJ No L196, 5.8.93, p. 1.

- b. Comparing the employment data from demographic sources with the employment figures underlying the measurement of GNP.

The aim is to try to assess the proportion of clandestine work. Whatever approach is used for calculating GNP, there is a volume of employment underlying the measurement obtained, provided by the units declared. This volume needs to be compared with the volume of employment resulting from the declarations made in connection with the surveys - i.e. population censuses and employment surveys - of households. Obviously the problem of people holding more than one job must be investigated.

- c. Describing the tax provisions and statistical adjustments applicable to benefits in kind and tips.

- d. Correcting the declarations made by producers or receivers of income in the statistical surveys for the effects of tax evasion.

For this purpose, it is recommended to examine the scope for using the results of verification operations carried out by the tax authorities. The Commission considers that it is desirable that the competent national authorities facilitate access by the statistical institutes to the results of tax audits.

If the work described above makes it apparent that certain productive activities are not covered exhaustively, the Member States will need to estimate what activity is missing from the GNP.

This presupposes the definition of methods to integrate the results of the work described in points a, b, c and d, particularly regarding the attribution of value added to the clandestine units. The Commission has started work on this important question and the results were submitted to the GNP Committee in September 1993.

6.2 Timetable

In order to obtain harmonized GNP data by the end of 1995, particularly as regards coverage of the underground economy, for each module of the work programme:

- review of adjustments;
- comparison of employment;
- description of benefits in kind and tips;
- use of tax audits,

the following timetable has been proposed:

- Transmission by Member States of the results of each module: 30 June 1994 at the latest;
- Study of results by the GNP Committee: second half of 1994.

After consulting the Member States at the meeting of the GNP Committee in September 1993, the Commission adopted measures concerning the contents of the programme and the timetable for its implementation.

Finally, pursuant to Article 10(8) of Regulation No 1552/89 on own resources, the Commission has formulated a reservation for each Member State on the exhaustiveness of the measurement of GNP, particularly as regards the coverage of the underground economy, which in this case permits retroactive correction of the financial contributions.

7. **Specific actions**

Even before the situation had been examined in detail, the Commission offered Greece and Portugal assistance in the work on revising their estimates. This work has been concluded in the autumn of 1993.

Greece's national accounts system had some obvious shortcomings and to rectify them the Commission has called on the assistance of experts from the French national statistical institute in order to generally reform the system, with the following main aims: adoption of the ESA as a context for producing accounts, developing more reliable valuation methods and improving the coverage of economic activity. The data which have been submitted in October 1993 led to a substantial increase in the estimate of Greece's GNP.

When the Directive was adopted, the INE - the Portuguese national statistical institute - was planning to revise the Portuguese national accounts in order to bring them up to date. In order to take better account of the objectives of the Directive, the INE has staggered the timetable for its revision. The Commission is keeping a close eye on the revision work. The change in the estimate of Portugal's GNP is not insignificant.

At the request of the Luxembourg authorities, the Commission has called on the technical assistance of an expert from the German statistical office and German university staff to revise the national accounts. Work has also been concluded at the end of 1993. It results in a significant upward revision of the GNP.

ANNEX

Review of use of credits pursuant to Article 8 of the Directive

USE OF "GNP CREDITS"

(Article 8 of the Council Directive of 13 February 1989)

Currency : Ecu

Use of credits	1989	1990	1991	1992	TOTAL
Belgium					
Drawing up of inventory	71 750	8 250	-	-	80 000
Work on improvement	-	-	88 000	119 996	207 996
Total	71 750	8 250	88 000	119 996	287 996
Denmark					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	-	200 000	300 000	120 000	620 000
Total	80 000	200 000	300 000	120 000	700 000
Germany					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	-	320 000	250 000	115 000	685 000
Total	80 000	320 000	250 000	115 000	765 000
Spain					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	100 000	225 000	150 000	115 000	590 000
Total	180 000	225 000	150 000	115 000	670 000
France					
Drawing up of inventory	80 000	-	20 100	-	100 100
Work on improvement	-	100 000	330 000	115 000	545 000
Total	80 000	100 000	350 100	115 000	645 100
Greece					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	-	230 000	180 000	165 000	575 000
Technical assistance	-	28 000	57 699	72 175	157 874
Total	80 000	258 000	237 699	237 175	812 874
Ireland					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	70 000	-	100 000	200 000	370 000
Total	150 000	-	100 000	200 000	450 000
Italy					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	-	-	300 000	120 000	420 000
Total	80 000	-	300 000	120 000	500 000

Use of credits	1989	1990	1991	1992	TOTAL
Luxembourg					
Drawing up of inventory	45 000	-	-	-	45 000
Technical assistance	-	-	62 900	50 300	113 200
Total	45 000	-	62 900	50 300	158 200
Netherlands					
Drawing up of inventory	80 000	-	-	5 400	85 400
Total	80 000	-	-	5 400	85 400
Portugal					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	-	250 000	-	200 000	450 000
Total	80 000	250 000	-	200 000	530 000
United-Kingdom					
Drawing up of inventory	80 000	-	-	-	80 000
Work on improvement	-	-	-	177 100	177 100
Total	80 000	-	-	177 100	257 100
Support services	-	-	100 000	38 330	138 330
SUB-TOTALS					
Drawing up of inventories	916 750	8 250	20 100	5 400	950 500
Work on improvement	170 000	1 325 000	1 698 000	1 447 096	4 640 096
Technical assistance	-	28 000	120 599	122 475	271 074
Support services	-	-	100 000	38 330	138 330
GRAND TOTAL	1 086 750	1 361 250	1 938 699	1 613 301	6 000 000

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