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CLASSIFICATIONS OF KIND OF ECONOMIC ACTIVITY
THE INDUSTRIAL CLASSIFICATION OF ENTERPRISES AND COMMODITIES
Report of the Secretary-General

INTRODUCTION

1. This paper deals primarily with the character, structure and application of a scheme for classifying enterprises, or equivalent units, according to kind of economic activity. The thirteenth and fourteenth sessions of the Statistical Commission requested that an international scheme for purposes of classifying enterprises be developed. This scheme is required for purposes of classifying data on income and outlay and capital transactions and on balance sheets according to kind of economic activity, in the context of national accounting and other programmes of compiling financial and related statistics.
2. The proposals concerning a scheme for classifying enterprises according to kind of economic activity are based on studies of national practices and consultations with national statistical offices. National schemes for the industrial classification of enterprises and establishments have been examined in relation to one another; and the patterns in which establishments of similar and differing kinds of activity are combined into enterprises, have been studied. Information has been gathered on national practices and views in respect of the relationship between schemes for the industrial classification of enterprises and establishments as part of the comments on the revised ISIC set out in document E/CN.3/359.^{1/} And, the first and second session of the

^{1/} The Draft Revision of the International Standard Classification of All Economic Activity, Statistical Commission, Fifteenth session, E/CN.3/359.

Working Group on Activity and Commodity Classification of the Conference of European Statisticians discussed the nature, principles and use of an industrial classification scheme for enterprises.^{2/}

3. After the discussion of the industrial classification scheme for enterprises, this report outlines the character and principles of a commodity classification scheme which is based on the revised ISIC. Such a scheme for classifying commodities is wanted for use in national accounting (e.g., in the revised SNA) and in other studies concerning the links between commodity and establishment data.

II. PURPOSE AND CHARACTER OF THE CLASSIFICATION SCHEME FOR ENTERPRISES

4. The scheme for classifying enterprises according to kind of economic activity is intended for use internationally in the reporting and compilation of profit-and-loss and balance-sheet data primarily. It is the enterprise which controls and manages the income and other sources of finance investment and similar outlays, and financial resources in respect of all the establishments of a legal entity. Not infrequently, the property and financial affairs of two or more legal entities which are owned and controlled by the same interests are managed in common. A scheme for the industrial classification of enterprises, or similar units, is also needed for such purposes as compiling data on the distribution and concentration of the ownership of various industries.

5. A number of the uses of data concerning enterprises involve linking these statistics with data in respect of the constituent establishments. An increasing number of countries are also building registers of economic units which delineate

^{2/} Report of the meeting held in Geneva, 16-20 May 1967, Conf.Eur.Stats/WG.28/5 and Report of the meeting held in Geneva, 8-19 January 1968, Working Group on Activity and Commodity Classification, Conference of European Statisticians.

the structure of these units in terms of enterprises (e.g., legal entities and in addition, sometimes groups of legal entities which are owned and controlled by the same interests) and their constituent establishments. In order to best serve these purposes, the international scheme for the industrial classification of enterprises should be as closely linked with the revised ISIC as is possible. As enterprises may consist of two or more establishments engaged in differing kinds of activities, the industrial classification scheme for enterprises must necessarily be less detailed than the industrial classification scheme for establishments.

6. It is proposed that the two most summary levels of the revised ISIC - the major divisions and divisions - be utilized as the international scheme for the industrial classification of enterprises, or similar units. This proposal emerges from the practices and views of national statistical offices and was recommended by the second session of the European Working Group on Activity and Commodity Classification. A number of countries utilize the less detailed levels of classification of their national schemes for purposes of classifying enterprises according to kind of economic activity; and consider that the same practice should be followed in the case of the international classification. The second session of the European Working Group considered that the division of the draft revised ISIC reflected the patterns in which differing kinds of activities were combined in the same enterprises well enough to be used as international guidance for the industrial classification of enterprises. It was considered that in any case, categories of at least the level of the divisions of the draft revised ISIC are required in order that the industrial classification of enterprise statistics may provide useful data for most analytical purposes.

7. It is recognized that international guidance in respect of an industrial classification scheme must be more tentative in character in the case of enterprises than in the case of establishments. The manner in which economic activities are combined and distributed among statistical units is far less uniform in the case of enterprises than in the case of establishments. The

enterprises are not only much larger units than establishments but also are not constrained in their range of activities by technological factors. Further, experience with an international standard industrial classification scheme for enterprises is lacking.

8. If the major divisions and the divisions of the revised ISIC are to be used as international guidance in respect of the industrial classification of enterprises, the publication on the revised ISIC should be extended to deal with this topic. This will involve elaboration of the purposes, nature and use of the revised ISIC, the principles of constructing the international classification, and the criteria of classification according to the revised ISIC in the case of enterprise and similar types of statistical units. It will also be necessary to add definitions of the enterprise-type units to be classified to the discussion of the underlying principles of the revised ISIC.

III. DEFINITION OF THE ENTERPRISE

9. In the case of countries with market economies, the narrowest definition of the enterprise is the single legal entity (e.g., the corporation, joint stock company, co-operative association, incorporated non-profit association, partnership, individual proprietorship) which engages in economic activity. The legal entity owns and manages the property of the business, enters into contracts and receives and disposes of all of its income, and maintains independent profit-and-loss and balance-sheet accounts and other records. It may consist of more than one establishment (i.e., mine, factory, shop) though a large number of legal entities will own one establishment only. The establishments of multi-unit business entities may engage in differing kinds of economic activity but these kinds of activities may be related, one to the other.

10. In the case of countries with centrally planned economies, the enterprise is the management and bookkeeping unit of limited scope. It enters into contracts, has an independent plan of production, receives and disposes of income, maintains a separate bank account and an independent, complete set of accounting records, for example, profit-and-loss and balance-sheet accounts.

Though the enterprise may consist of a number of shops or factories, it usually engages in a single class of activities. In other words, the kind of activities of the enterprise is often as homogeneous in character as the kind of activities of establishments in the countries with market economies.

11. Some of the countries with market economies (e.g., the Netherlands, United Kingdom, United States) employ an enterprise-type unit which is broader in scope than the individual legal entity. It consists of the group of legal entities which are owned or controlled by the same interests. This unit may be defined as a group of legal entities where a consolidated balance sheet, as well as profit-and-loss statement, is maintained or where the majority of the equity (shares or other forms of capital participation) of each member of the group is owned by the same interests. In these cases it is likely that the property and financial affairs of the group of legal entities will be controlled and managed together.

12. Some countries with centrally planned economies appear to utilize the combine or trust or other groups of enterprises for certain purposes. In the case of the USSR, for example, enterprises are grouped together into broader management units in the case of such industries as metal mining and manufacturing, leather and footwear production, and small-scale manufacturing in rural areas. Limited statistical use appears to be made of these groups of enterprises.

13. Both legal entities and families of legal entities constitute useful statistical units.

14. Where the analysis of financial experience and behaviour is the focus of attention, it is valuable to employ families of legal entities as statistical units. As was noted above, the finances and investment of the legal entities of a given family are likely to be planned, controlled and managed together. There may also be a number of formal financial links between the members of a family of legal entities which are of little, if any, real significance. The family of legal entities is of course the most suitable statistical unit for

purposes of studies of the distribution and concentration of ownership.

15. On the other hand, the use of the family of legal entities is likely to increase the degree of heterogeneity in respect of kind of economic activity of the enterprise-type statistical units. Further, some countries may find it impracticable to identify families of legal entities and gather consolidated data in respect of their profit-and-loss and balance-sheet accounts. For these reasons, a number of countries use the legal entity as the enterprise-type statistical unit. The legal entity is also the appropriate enterprise-type unit for purposes of studies of the marketing and pricing of goods and services, value added and the links between production, income and the disposition of income.

16. In the case of government bodies, departments or ministries might be taken as the equivalent of the enterprise-type units for purposes of industrial classification. While each organ of government (e.g., the central government, each state, municipality) will plan, control and manage the finances of all of its constituent bodies collectively, the organs of government are of course unsuitable units for purposes of industrial classification.

IV. CRITERIA FOR CLASSIFYING ENTERPRISES

17. The classification of each enterprise should be determined according to the category of the industrial classification in which the principal class of activities of the enterprise is covered. In concept, the kinds of activity of the enterprise to be considered for purposes of the classification should be determined from the products sold or the services rendered to others. Activities carried on in one establishment of an enterprise to produce goods or render services for other establishments of the same enterprise should in general not be considered distinct kinds of activity for purposes of classification. Instead, these activities are to be considered part of the chain of activities linked with the output for sale to other economic agents of a given class of goods and services. Ideally, the relative value added by the enterprises to the goods and services sold should furnish

the basis for ascertaining the principal class of activities.

18. In practice, the lack of data on the distribution of the products of establishments between other establishments of the same enterprise and other economic agents, may result in identifying the kinds of activity carried on by the enterprise from the full range of goods and services produced by its constituent establishments. In a number of instances, it will be necessary to base the principal class of activity of enterprises on data in respect of the kind of activity assigned to each of their constituent establishments. Under these circumstances it is important that the data used furnish net measures of the activity of the establishments. Gross measures of activity can be seriously misleading in respect of the relative importance of the constituent units. If figures of value added are not available, data in respect of numbers of persons engaged or wages and salaries paid might be used.

19. Enterprises will engage in kinds of activity in addition to their principal activity. In order to indicate the degree of specialization of enterprises in their principal activity it will be useful to compile data on homogeneity ratios. These ratios may be compiled in respect of aggregated data for enterprises grouped according to principal kind of activity or in respect of individual enterprises. In either case it will probably be necessary to utilize data on the value added, employment, etc. of the whole of the individual constituent establishments of enterprises in compiling these homogeneity ratios.

V. CLASSIFICATION SCHEME FOR COMMODITIES

20. It is proposed to develop a scheme for the classification of commodities in terms of kind of economic activity in which the various types of goods and services are characteristically produced. The first four digits of the code for each class of goods or services would represent the group of the revised ISIC where the goods or services are characteristically produced. The next levels of the classification would consist of successively more detailed sub-divisions of the ISIC groups in terms of types of goods or services. Use would be made of at least one, and perhaps two, levels of classification for

this purpose; and each level of classification would involve the addition of two more digits to the code for categories of goods and services. Thus, at least a six-place code, and perhaps an eight-place code, would be used.

21. It is proposed that the five-digit categories of the Standard International Trade Classification (SITC), Revised, be used as the point of departure in defining the sub-division of the ISIC groups into commodity classes. This approach will facilitate the forging of links between external trade and other commodity statistics and between commodity and establishment statistics. The preparation of the index to the revised ISIC, which will also be a key between the industrial classification and the SITC, that is described in document E/CN.3/360, will furnish the basis for this work. In a number of instances, it will no doubt be essential to adapt the five-digit categories of the SITC for use in subdividing ISIC groups into commodity classes. This will be necessary not only because single five-digit SITC categories may encompass commodities which are the characteristic products of more than one ISIC group, but also because some of the five-digit SITC categories may not be suitable for the general-purpose commodity classification.

22. The European Working Group on Activity and Commodity Classification approved on the whole of the proposal to develop a commodity classification scheme based on the revised ISIC. Questions were however raised concerning the considerable number of categories such a classification might involve and the appropriateness in some instances of five-digit SITC categories for purposes of constructing the classification. It was suggested that national statistical offices be consulted concerning the commodity classification scheme as the planning of the work reaches an advanced stage.

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