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Paper

A new statistical definition of the enterprise - conceptual and practical implications

A. Introduction

Coming from actions of Eurostat launched methodological expert groups (organised as European Statistical System networks – ESSnets) a discussion about new definitions for prominent statistical units – the “enterprise” and the “kind-of-activity unit” – is going on in the fora and the brains of European statisticians.

The subject has been started (or rather re-started after some years of more or less attempts to implement the current definitions as laid down in European legislation) and driven by spoken and unspoken intentions. Conception, percipience and – in the author’s view – a great deal of interpretation are heating the discussion among experts as well as among decision makers. As Eurostat has included the statistical units definitions in the proposed FRIBS (Framework Regulation for Integrated Business Statistics) legislative act, discussions are also corseted in the time frame of the FRIBS legislative procedure.

This paper tries to approach the proposals to re-define the named statistical units – most prominently the “enterprise” – from a conceptual viewpoint. Starting from the analysis of the differences between the current and the proposed definitions the author will try to delineate the generally possible and the factually expectable consequences for practical statistical work.

In the authors percipience the ESSnet on Multinational Profiling gave the starting shot for a discussion about “Global Enterprises” in the year 2010. The ESSnet has the task to develop a methodology to profile large and complex multinational enterprise groups. In the conception phase the ESSnet decided that its methodological work should base on a definition of the enterprise that is different from the present one. The terms “Global Enterprise” and “Truncated Enterprise” have been created and further on been used by the ESSnet consortium. Meanwhile another ESSnet had come into action – the ESSnet on Consistency – which deals among others with definitions. The task to elaborate the details of the proposed new definition of the “enterprise” was handed to this ESSnet, while the ESSnet on Profiling concentrated on their core task to develop a profiling methodology.

Meanwhile both ESSnets are close to their planned termination at the end of year 2013. The ESSnet on Consistency has already provided two proposals for new definitions of statistical units: one for the “enterprise” and one for the “kind of activity unit” (KAU). These proposals

have been passed on to a Task Force on Statistical Units which has been launched by Eurostat. The Task Force gathers experts of statistical domains at Eurostat and experts of statistical units and business registers from some member states – among which also participants of the two ESSnets mentioned. This Task Force shall provide the wording of the definitions which shall be included in the coming European Framework regulation for Integrated Business Statistics (FRIBS) and the operational rules for the application of the renewed definitions.

This paper concentrates on the new definition of the **enterprise**. The second unit that is proposed to be defined newly, the KAU, delineates from the enterprise so all changes that concern the enterprise can also affect the KAU, therefore the enterprise must be understood first. Neither the intended volume of this paper nor that of the presentation allows dealing in depth with both definitions. Moreover from the work done by the Task Force so far it seems that the proposals for new definitions of the two units mentioned may affect the current definitions of some more units – namely the “enterprise group”, the “legal unit” and the “institutional unit”.

B. A glimpse into the wording of the current and the proposed definition of the enterprise

The enterprise is currently defined by the EU Regulation 696/93 on Statistical Units as

the smallest combination of legal units that is an organizational unit producing goods or services, which benefits from a certain degree of autonomy in decision-making, especially for the allocation of its current resources. An enterprise carries out one or more activities at one or more locations. An enterprise may be a sole legal unit.

The proposed definition – which is still under discussion and no final wording is available at the moment – will define the enterprise as

an organisational market oriented unit which benefits from a sufficient degree of autonomy in decision-making. An enterprise carries out one or more activities at one or more locations.

The enterprise can correspond to either

- *a single legal unit not controlled by any other legal unit*
- *an enterprise group as a set of legal units under common control, or*
- *an autonomous part of an enterprise group*

C. What is **new** about the proposed definition?

The differences between the current and the proposed definition of the enterprise may be obvious to different degrees at first reading:

Market orientation is explicitly mentioned in the proposal and states that enterprises refer to the economic sector. In the current definition the same was the case but it was in the explanatory note but not in the core definition itself. So this aspect is *not new but more explicit*.

Autonomy is a second aspect that – compared to the current – definition becomes *more prominent and explicit* in the proposed one. Autonomy is the criterion which defines the

shape of the unit enterprise, its demarcation against the “rest of the world”. Autonomy is the constituent feature for the identification and delineation of the enterprise.

Legal units are dealt with *differently* in the current and the proposed definition. What is skipped from the definition is to build enterprises from one or more legal units. Instead the proposed definition of the enterprise makes reference to either the legal unit (as the current definition does) or to the enterprise group.

Conceptually the *current definition* provides a clear hierarchy of legal unit – enterprise – enterprise group: One or more legal units act as an enterprise and a multitude (more than one) of enterprises can form an enterprise group. The *proposed definition* does differently: Only for the simple case where one legal unit forms an enterprise this relation is still in the definition. For the more complex case in which more than one legal unit are involved in an enterprise (“complex enterprise”) the proposed definition does no longer refer to the legal unit at all but to the enterprise group instead. According to the proposed definition the whole enterprise group may be seen as one enterprise or more than one enterprise can be detected inside the enterprise group.

The third suggestion of the proposed definition (an enterprise as an autonomous part of an enterprise group) deals with the situation that more than one enterprise can be found inside one enterprise group. In this case it is left open what the relation of the enterprise to legal units may be. An enterprise may consist of some *legal units but legal units may also be split* and the parts of them may be apportioned to different enterprises. This novelty can be seen as a very important motivation for the proposal to change the definition. This is for two reasons: Firstly the phenomenon can be observed in reality (so it exists and should therefore be covered by the definition to make the definition cover the reality). Secondly it may be very helpful for the practical delineation of enterprises by the method of top-down profiling of enterprise groups to identify the enterprises within the enterprise group without having to find out relations between enterprises and legal units (so the change of the definition would be helpful for practical work). At the same time this is the element of the proposal with the most far-reaching implications both conceptually and practically.

To summarize the proposed definition of the enterprise allows two constellations which the current definition does not include:

1. An enterprise may be identical with an enterprise group.
2. An enterprise may consist of parts of legal units; in other words legal units may be split and the parts may be apportioned to different enterprises.

Another implication that has so far not been tackled in the discussions is that the proposed definition ties the enterprise to be demarcated inside an enterprise group only. The current definition is more open since it allows enterprises to form an enterprise group but does not prohibit that enterprises can be formed (as combination of legal units) without reference to an enterprise group and therefore without reference to links of control.

There are also some misperceptions about the novelties of the proposed definition. These shall be dealt with in the next sections.

D. National versus multinational enterprises

The regional aspect of enterprises is not dealt differently with by the current and the proposed definitions. The present and the proposed definition do not refer to any regional territories. Both are *indifferent* about the regional coverage of an enterprise. The perception is however, that the discussion about the new definition is driven by the aim to catch the

multinational reality of big enterprises. The multinational aspect has been highlighted of course by the circumstance that the proposed definition – as described in section A – has been promoted by an ESSnet that deals with multinational units: enterprise groups as well as enterprises. The well known argumentation is:

- Economic (autonomous) actors act more and more globally. Therefore statistics have to focus on global enterprises.
- Legal units are not suitable to identify these actors and to provide meaningful data. Therefore we should delineate the enterprises top down by asking the decision makers of the enterprise groups: How are the groups' enterprises shaped?

Although complex enterprises are relevant and appropriate statistical units, they are not easily detectable. Therefore research is done for good methods to profile them. The enterprise groups, which contain the complex enterprises, are taken to be a good starting point for the detection/identification of complex enterprises. In the case of multinational enterprise groups this will lead to multinational – “global” – enterprises (GENs). If it is accepted that the “real” actors are acting globally then it is logically stringent to take sub-consolidated figures on lower level within the multinational actors as not economically meaningful. Therefore multinational profiling aims to get the economically meaningful figures in direct contact with the group managers.

By the intensive promotion of the GEN concept the belief was highlighted, that for the big international economic actors the relevance of the data was no longer given if data refers to national borders, since the parts of a multinational enterprise that are situated within the territory of a country are more or less random and this “national part” of the multinational enterprise is not acting *autonomously* but in context with the other parts of the multinational enterprise in other countries.

Since the current and the proposed definition allow generating “global enterprises” the decisive question is whether and how the users can deal with this situation. The statements by the users at Eurostat level shows the dilemma: The production of statistical figures is so far organized according to national borders and the figures themselves refer to a national territory and to statistical units that are shaped to be within this national territory. The European statistical system and its legislative framework – structural business statistics (SBS), Foreign affiliates Statistics (FATS), short term statistics (STS), national accounts (NA), you name them – is aligned according national borders. This of course is for good reason since the data users traditionally demand data at that level.

To cope with this situation one step back was done in the conceptional discussion from the puristic approach that would prefer to take the autonomous economic actors as they are (multinational, global). The distinction between “global” and “truncated” enterprises was defined. “*Truncated*” was established to be the “*national aspect*” of a multinational enterprise, the truncated enterprises thereby the national parts of the multinational enterprises. Autonomy was attributed to the multinational enterprises (“global enterprises” – GEN), or to say it more precisely, autonomy was the criterion to delineate and demarcate the GEN. As a logical consequence, the national parts of these enterprises – the TENs – were necessarily *not* autonomous (since if they were they would be the enterprise and not only an artificial part of the enterprise).

E. Implications for practitioners: How users and producers of statistics are affected

In the authors perception the analysis of the consequences of the proposed definitions – both methodological and practical – so far only scratches the surface. Many users of the

statistical units' definitions are just becoming aware that something is going on these days. Many are unsettled since they feel not able to think through the implications in short time. Many see heavy implication for practical work, such as running a register for the new units, conducting data collection about the new units and producing results based on the new units. This paper is not the place to list and discuss in detail the bulk of practical difficulties that is suspected to be connected with the proposed definitions. There exists a "frequently asked questions"-paper by Eurostat which is work in progress still but which tries to give answers to the concerns that have been raised so far. The amount of aspects dealt with in that FAQ-paper encourages assessing at this stage that the consequences of the proposals are immense.

Doubtless the EU-ESSnet work "disturbed" or "upset" the practical handling of the current enterprise definition by putting emphasis on the issue that building (by profiling) actors (enterprises) *according to national borders is no longer appropriate* in case of multinational groups. The methodological discussions have so successfully put emphasis on this statement that it now is perceived in the European countries as the *heart of the new approach* which Eurostat has been advised for practical application. This again is the reason why many statisticians in the Member States are now very worried. They are *worried because they take this approach seriously* and try to imagine how it can be applied and what differences it will cause compared to the statistics done till now.

The users of the units are the **statisticians** of course **who produce statistical data**. An early proposal was to explain to these users what the reality about enterprises nowadays is and *what should the users need* ("pedagogy"). This seems to have been relieved and the decisive question to be: *What do the users want?* To name just three prominent ones:

- How shall Structural Business Statistics (SBS) in the future describe a world of multinational actors?
- How can Foreign Affiliates Statistics (FATS) describe cross-border activities if the subject and objects of cross border financial links are multinational units?
- Shall National Accounts be replaced by European Accounts (or EU Accounts?) – or even World Accounts?

Asking the users in Eurostat gives the preliminary impression that for the time being the national aspect of statistical figures shall remain first priority. Moreover explicitly asking the users highlighted an aspect that was maybe lost sight of a bit in the early phase of the GEN/TEN-discussion: *Who actually needs or wants global statistical figures?* Truly global figures are not national ones nor European ones. Global economic actors care no more about European (or EU-) borders than they care about national borders. So the dilemma about the diminished meaningfulness of "national" data is the same at the European level.

The proposed definition bares heavy consequences for the **statistical business registers**, not only for their practicalities of the maintenance (including profiling activity) but also for the basics of their data model. A business register should provide (up to thresholds of course) the full population of economically relevant units and it should provide the relations between these units. The proposed definition of the enterprise does not facilitate this work, to say the least. Business registers nowadays can make use of the clear relationships that are provided by the current definitions of the enterprise, the enterprise group and – as basic elements – the legal units. By the latter they can build the link to the administrative world as well which is important since the use of administrative data has become equal if not predominant to direct surveys. For surveys the legal units provide the respondent to whom questionnaires can be sent. This well elaborated system of units gets now disturbed if we break conceptionally the link between the legal unit and the enterprise.

Implications on **data collection and relation to respondents** will have to be dealt with as well. Do statisticians want to collect from respondents, perhaps in direct cooperation with the managers of the enterprise groups, maybe in international workshare and data exchange? Shall statisticians ask for figures that are fully consolidated at GEN level and additionally for figures sub-consolidated at TEN level? How will statisticians explain to respondents that the statistical concepts require that the sum of the different sub-consolidated turnovers in each European country will not be usually equal to turnover fully consolidated at the European level? How can statisticians manage to do so in times where they have to explain convincingly to respondents that the new ways to delineate enterprises aim to reflect the global organisation in order to make it simpler for the global enterprise groups to provide data and to improve the quality, also to improve consistency with the business statistics of the other Member States? And how about using administrative sources?

F. How profiling is affected by the current and the proposed definitions

There can hardly be doubts left that profiling methods are needed and have to be applied to deal with the enterprise concept as far as big economic actors are concerned. The question should be settled whether a pure one-to-one relationship between legal units and enterprises has to be overcome in practice: Yes it has to be overcome, and it has to be overcome in practice.

A misperception seems to exist that the current definition would allow only for the bottom-up **approach of profiling** (which is supposed to be burdensome if not impossible to apply for really big and complex enterprises) whereas the proposed definition would be needed to apply the top-down profiling approach. The true situation is that the current definition is neutral to both ways profiling.

The proposed definition instead enforces the top down approach. This becomes obvious easily from the explicit reference of complex enterprises to the enterprise group instead of the legal units. It is furthermore stringent when dealing with the splitting of legal units. To find out in the bottom up way the parts of legal units that form an enterprise is even more unlikely to be applicable compared to a situation where complete legal units are the building elements of enterprises.

The proposed definition allows delineating enterprises without referring to legal units as their elements. This in practice can only be managed top-down from the enterprise group and preferably in direct contact with the management of the enterprise group. As the delineation of the newly defined enterprise would be connected indispensably with the top down approach, it is important to look at the findings of the case study works of the ESSnet on profiling. What is – regarding the splitting of legal units – the state of the art of how to apply the top-down approach of profiling big enterprise groups in order to identify the enterprises inside them?

The case studies executed in the ESSnet on profiling are still in progress when this paper is written and they accordingly have not been systematically analysed. The provisional state of the art nevertheless allows for two findings:

- The splitting of legal units between different enterprises occurs in reality.
- Data for split legal units – that means the apportioning of the data of one legal unit to different enterprises – is hard to obtain. Only in lucky circumstances the enterprise groups' information systems provide this detailed and apportioned data.

This means that the real new aspect of the proposed definition will *not be applicable* in practice.

Three other preliminary findings can be drawn from the case studies on profiling:

- The crucial aspect that defines an enterprise (autonomy) tends to be not easily detectable and no easily applicable. Especially where profiling is done without direct contact to the management of the enterprise group (so called “light” or desktop profiling) the enterprises tend to be demarcated according to information about the activity (NACE-code) instead of information about autonomy. Doing so would mean that there is a tendency to delineate KAUs instead of enterprises by the profiling activity.
- The descriptions of the profiled enterprises depend on legal units in practice. This is not a surprising result since the legal units are identifiable and are stored as well in the statistical registers as in the annual report of the enterprise groups.
- The profiling tends to identify some legal units that either can not be attributed to one enterprise since they work for more than one enterprise or because they do the management of the enterprise group. In many cases this is dealt with by putting these legal units into a quasi-enterprise “management” or “others”. Thereby a residual is created within the enterprise group whose content can hardly be analysed when taken as a statistical unit “enterprise”.

G. Definitions and operationalisation

a. National versus multinational

In the past and in the present the issue of global versus truncated enterprises has so far been “solved” – or better to say “dealt with” – by an **operational rule** used by those who apply the current definition of the enterprise: As every statistical office has to produce data on national level (as explained, also the European regulations demand to produce data for Member States, that is at national level) everybody who applies the current definition of the enterprise does so in national context. As explained this is not demanded by the current definition itself, which makes no reference to geographic borders. It is just an operational rule – maybe not even realized properly as being such – coming from the purpose of the application of the definition: producing national figures based on appropriate statistical units (nationally demarcated enterprises). This means that the operational rule should be changed if its purpose is no longer valid. If the purpose changes to produce data at multinational level then the application of the definition of the enterprise should be in a multinational way.

Nevertheless – countries need national data and Europe (EU) needs European (EU) data of course. So we have to deal with the question which definition serves better the production of national and European statistical figures.

As explained, the crucial feature and starting point to identify enterprises according to the proposed definition is autonomy. The first best “real” enterprises are therefore the GENs. All interactions of sub-units within the GEN are consolidated and the result is the truly meaningful GEN figure. The need for national data then leads to a breakdown of the GEN into TENs. A TEN is defined as the fragment of a GEN that is situated within a national border. The rule is set: One TEN per GEN and per country. All subunits within the TEN are consolidated again, but only inside the TEN. Therefore the sum of the TEN will not necessarily result in the GEN, since some consolidation for the real GEN figures is missing.

The approach to delineate the TEN (as an approximation of enterprises at national level) by using the GEN and the national borders produces units that are defined by these two aspects. Whatever belongs to a GEN and is situated within a country is to be taken as a TEN. Compared to an approach where from a country view the elements of which an enterprise is formed can be chosen by the statisticians of this country in their own responsibility, the GEN/TEN approach makes them dependent on the actor who defines the composition of the GEN.

One consequence of the composition of enterprises is the attribution of a NACE code. Taking over the NACE code appropriate to the GEN might not give a good picture about the TEN. Therefore a double coding of NACE for the TENs has been proposed. So statisticians could attribute a NACE code at national level to the TEN that differs from the NACE code of the GEN. Problem solved? Not really. The TEN may consist of sub-elements that are bound together “only” because they belong to a GEN. They would not necessarily be put together from a country perspective. They may not have any flows between them that have to be consolidated at country level and they may therefore at country level be treated for good reasons as separate units – with different NACE codes. The way to delineate TENs may have considerable consequences for the statistical picture of the structure of the economy.

b. The story about the legal units

Legal units do not by their nature refer to the world of statistics, they are *no statistical units*. Reasons why statisticians make use of legal units are:

- The possibility to *identify* them, since – like other units from the administrative world – they are defined and addressed by public administrations.
- Data of statistical use can be *attributed* to them, e.g. financial accounting data or data on people, like social security data about employment.
- Availability of sources to *collect* the data from administrative bodies (which is easier for statisticians than collecting all data themselves).

These three aspects all refer to the use of legal units as **observation units**. Moreover their use as **reporting units** to address respondents to surveys should be mentioned.

There are also reasons not to make use of legal units:

- If you want to observe figures about complex enterprises the unconsolidated flows between the legal units inside these enterprises disturb the picture of the observation unit (the complex enterprise).
- Legal units may not be autonomous and data on legal units may then not be meaningful but give a wrong picture.

The latter set of reasons refer to the use of legal units as **statistical units** and seems to imply for the promoters of the proposed definition of the enterprise to free the delineation of the enterprise from the reference to the legal unit. The counter question that has not been dealt with so far is: Why should these phenomena only occur within enterprise groups. Or, in other words, what is conceptually the difference between legal units working for more than one enterprise *within* one enterprise group and a legal unit working for different enterprises of *several* enterprise groups or without the existence of enterprise groups at all?

From this the proposal can be derived to use the legal units as best proxy for enterprises in cases where no units can be detected that are more or truly appropriate. To treat legal units as enterprises where otherwise they would have to be split is just another **operational rule** that helps with the practical difficulties of identifying the statistical units and collect data about them.

Unfortunately this operational rule is part of the current definition of the enterprise. This could be solved by extending the current definition by a few words (“or parts of legal units”). It would then define an enterprise as “*the smallest combination of legal units or parts of legal units that is an organizational unit producing...*” and so forth. This would allow for all what is intended with the proposed definition but would avoid the disturbances and side effects that must be expected to be implied by the proposed definition.

H. Conclusions

The work of the ESSnet Profiling and of some actions that Eurostat has initiated to examine the practical possibilities of applying the proposed definitions are still under way and shall deliver their results end of year 2013. Therefore it is of course too early to have final conclusions about the implications which the proposed definitions will have. But some tendencies are visible that should be taken into consideration seriously:

1. The discussion started from a situation where a majority of the EU member states do not apply the current definition of the enterprise as far as complex enterprises are concerned. The reason why the situation is such remains to be analysed not sufficiently.
2. Neglecting the legal unit for the description of enterprises causes heavy disruptions for the statistical business registers and for data collection from administrative sources.
3. The really new aspect of the proposed definition (splitting legal units) seems not easy to apply. In practice enterprises are continued to be described as sets of legal units, not as sets of parts of legal units.
4. The preferred regional aspect of enterprises remains an open issue and first priority is given to further on demarcate enterprises according to national borders (resulting in TENS, “truncated enterprises” in the proposed approach). European or world level demarcations (truly “global enterprises”) lack prominent users who feel able to stress their demand for such data in the short and medium run.
5. Full profiling activities in contact with the management of the enterprise groups imply to rely heavily on international cooperation and proofs to be time- and skill-consuming. Many practical aspects will still have to be solved.

From these aspects it seems to be a very open question whether the proposed definition of the enterprise will have the chance to be implemented to a greater deal than the present one. Moreover it remains an open question whether the new definition will tend to be implemented differently from the present one – meaning that it would lead in practice to other, different enterprises. It might also lead to a situation where it is – compared to the situation today – less observable what kind of enterprises will be stored in the statistical business registers and applied by the domain statisticians.