

**13th Meeting of the Advisory Expert Group on National Accounts,
1-3 October 2019, Washington D.C., USA**

Agenda item: 3.6

Update on statistical classifications

Introduction

This note provides an update on the ongoing work on the following classifications: ISIC Rev.4, the Classification by Broad Economic Categories (BEC), the Classification of Business Functions, the Harmonized Commodity Description and Coding System (HS), and the Standard International Trade Classification (SITC)

A paper on: Update on statistical classifications

Main issues to be discussed

The AEG is invited:

- to take note of the ongoing work on these classifications

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1. Background

This note provides an update on an update on the ongoing work on classifications regarding ISIC Rev.4, the Classification by Broad Economic Categories (BEC), the Classification of Business Functions, the Harmonized Commodity Description and Coding System (HS), and the Standard International Trade Classification (SITC).

2. ISIC

The Expert Group on International Statistical Classifications mandated the Technical Subgroup on the International Standard Industrial Classification of All Economic Activities (TSG-ISIC) to investigate if issues raised on ISIC Rev.4 can be addressed in the current structure of the ISIC with additional guidance provided, and, in case the TSG-ISIC investigation showed that this was not a practical approach, recommend to the EG that a review of ISCI Rev. 4 take place.

A meeting of the TSG-ISIC took place in New York from 18-20 June 2019 discussed several issues with ISIC that were identified during the review of the classification of economic activities in Eurostat, the Philippines, Brazil, Morocco, Canada, New Zealand and UNSD. Based on the assessment of the issues previously discussed and on the issues identified by members of the TSG-ISIC during its meeting, the TSG-ISIC concluded that these issues cannot be addressed within the current structure of ISIC. However, the extent of the changes to ISIC can be assessed only after a global consultation with countries, international organizations and relevant groups of experts. The TSG-ISIC subsequently prepared a questionnaire for the global assessment to seek the views and inputs on the list of issues identified and inquire whether there are other issues to be considered in the update of ISIC Rev. 4.

The global assessment was launched on 13 September 2019 to countries, international regional organizations and relevant expert groups. Based on the results of the global assessment, the TSG ISIC will prepare a report to the Expert Group on International Statistical Classifications containing recommendations on the extent of the revision of ISIC. This report will also include an expected timeline and process for the update of ISIC Rev 4. Further detail on the ISIC update may be included in the report of the international expert group on international classifications to the Statistical Commission in 2020.

The set of issues identified by the TSG-ISIC include the following:

- **Internet retail sales and e-Commerce sales**
ISIC classes in retail trade are defined on the basis of store retail and non-store retail. This class distinction creates difficulties measuring Internet sales and e-Commerce. As the retail environment changes, omni-channel retail is growing covering a combination of non-store and store retail channels. There are substantial sales using the web in both store and non-store categories of ISIC.
- **Intermediaries in service activities**
The increasing use of Internet enabled technologies is rapidly changing the business practices of several industries. For example, the traditional local travel agencies are declining, and Internet based reservation services are increasingly being used by both businesses and households. New service transaction intermediaries also bring together producers and consumers in new ways. Intermediaries have created the ability for a local traveller to arrange a ride with a local driver in the absence of a traditional local taxi service provider. Intermediaries can also bring together owners of real estate with customers looking for short-term accommodation. In 2017, the Expert Group adopted guidance for classification of these intermediaries (ESA/STAT/AC.340/10 - 15 August 2017 available at <https://unstats.un.org/unsd/classifications/expertgroup/egm2017/ac340-10.PDF>).
- **Audio and video content distribution**
The distribution of both audio and video content has rapidly changed to take advantage of new technologies. ISIC Rev.4 Section J, Information and communication, currently includes distinctions for publishing, program production, broadcasting, and telecommunications activities. Much of the distribution activity is now taking place over a mixture of wired and wireless networks. Internet enabled on-demand services (streaming) are not easily classified to a single location in ISIC.
- **The distinction between wholesale and retail trade**
Several countries have expressed problems with the ability to implement the concepts of wholesale trade and retail trade in ISIC. In many instances, businesses actually perform a mixture of sales to both business and household customers. While surveys may attempt to 6 separate class level data with additional inquiries for class of customer, concern remains with the quality of available class of customer data when attempting to assign a business to wholesale trade or retail trade.
- **Factoryless goods producers (FGPs)**
Outsourcing of manufacturing transformation services has remained an implementation problem for users of ISIC. Many countries have noted that the FGPs who outsource all manufacturing transformation activities to non-affiliated enterprises, either abroad or in the resident economy are hard to identify. Some countries have expressed the opinion that the FGP activity is not significant while other countries have noted that it is both important and growing in their economies. FGP enterprises are characterized in ISIC as units that perform all of the necessary steps that result in the production of goods but

outsource the actual transformation or manufacturing activities to unaffiliated entities domestically or unaffiliated entities outside of the domestic economy. After significant discussion, the technical subgroup recommends no changes in the current guidance in ISIC based on ownership of input materials as discussed in paragraphs 136-145 of ISIC Rev.4 because no firm recommendations for improvement are available. However, the text in the ISIC manual could be further clarified that the FGP activity refers only to a production arrangement between non-affiliated entities, either abroad or in the resident economy.

- **Technology and the application of new technology**
Technology and the application of new technology raises a number of questions for ISIC. Is the application of new technology a new activity or an incrementally new way of performing an existing activity? For example, the use of technology in financial transactions, sometimes referred to as Fintech, has expanded the availability of services to much broader segments of the population than previously had access to physical banks or other service providers. The transfer of money between parties, even in different countries, has been possible for many years using wire transfer services. Now, the same transfer of money can be performed by money transfer apps on a smart phone, greatly expanding the market. Similarly, in the past, loans were provided by banks. The application of technology has seen the rise of alternative lending facilities such as non-bank lending and even arranging peer to peer lending.
- **Statistical units**
ISIC is primarily intended as a classification of establishments. However, the increased fragmentation of production (both domestic and foreign) and the increasing availability and access to administrative and non-traditional data sources put in question the validity of the establishment as the preferred unit. The Expert Group on international classification recognized in 2017 that the review of “the statistical unit model could be a driver for a major review of ISIC, noting that a change from establishments to enterprises as the main unit would require a complete conceptual review of ISIC and would most likely result in major changes, including at structural level” (ESA/STAT/AC.340/4). It is important therefore to make an assessment across countries of the unit level ISIC is applied to.

The full summary report of the meeting of the TSG-ISIC is available online at https://unstats.un.org/unsd/classifications/ExpertGroup/TSG-ISIC2019/Summary_Report_TSG-ISIC_2019.pdf

3. Classification of Business Functions

The classification of business function is being develop to better capture and reflect the organization of business functions within a multinational enterprise. Companies are increasingly outsourcing business functions abroad. This typically results in jobs being moved abroad, thus affecting domestic employment and economic activity.

Building on the experience of the Eurostat International Sourcing Survey, a classification of business functions is being developed. It is expected that an UN expert group will be organized

in the first half of 2020 followed by a global consultation on the business function classification. The classification of business functions will subsequently be submitted to the Expert Group on International Classification for their endorsement. The Classification is expected to be finalized by the end of 2020.

4. Harmonized Commodity Description and Coding System (HS)

The WCO Conference on the Future of the Harmonized System was held 2-3 May 2018 at the WCO Headquarters in Brussels. The Conference recognised that the Harmonized System (HS) is an essential tool for our global trade system and plays a central role in trade and statistics. In accepting this, the Conference also recognised that improvements to the HS were possible and desirable. Factors such as globalisation and the rise of Global Value Chains and intermediate goods, the rapid pace of technological change, digitalisation, the emergence of new integrated, connected and multifunctional goods and the increasing demands on the HS were among the factors indicated as part of the impetus for the HS to evolve. It also noted that failure to adapt to change would endanger the future utility of the HS.

Taking into account the outcomes of the WCO Conference on the Future of the Harmonized System, it was recommended to the WCO Policy Commission that the Policy Commission support the implementation of a project to further examine potential areas of change for the Harmonized System which, in the first instance would: a) continue the consultation process; b) gather further information on the current issues in relation to the use of the HS; c) conduct a feasibility study examining the desirability and impacts, including initial cost and benefit analysis, of the proposals resulting from the Conference and the subsequent consultations; and d) make subsequent recommendations to the Policy Commission on the progressing of viable changes, including on the most appropriate bodies and mechanism to advance these changes.

A follow-up WCO Committee meeting is scheduled 23-26 September 2019 at WCO Headquarters Brussels to take the review forward.

5. Classification by Broad Economic Categories (BEC)

The fifth revision of the Classification by Broad Economic Categories was endorsed by the United Nations Statistical Commission in 2016, at its fourth-seventh session, for use as an international statistical classification.

This fifth revision of BEC (BEC Rev.5) is the outcome of a review process that spanned several years and involved contributions from many classification experts and data users around the world. This process resulted in a structure that is both more detailed and more logical than the previous version. It responds to the need for more relevant economic categories, includes services in addition to goods, and more clearly distinguishes the end use of products. New broad categories include “mining and energy”, “construction and housing”, “textile and footwear”, “information and communication” and “health and education”.

The BEC Rev. 5 was published in 2018 and is available at <https://unstats.un.org/unsd/trade/classifications/bec.asp>

6. Standard International Trade Classification

The United Nations Statistics Division is in the process of circulating a proposal to undertake a fifth revision of the Standard International Trade Classification in collaboration with the World Customs Organization in preparation of the forthcoming 2022 edition of the Harmonized Commodity Description and Coding System (HS 2022).