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*A methodology for statistics on activity carried out
via establishment abroad by service enterprises
and its implications for European policy on services*

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ABSTRACT

Faced to a cacophony of definitions, the preface on terminology clarifies that the term "establishment trade" is used as synonymous with "activity via establishment abroad". "Direct investments" is referred to a statistical system related to balance of payments which could be a starting point to build over a system on activity carried out abroad by units which are controlled by resident enterprises.

Introduction to a proposal of work is made by describing the theoretical basis of the analyses of internationalisation of service activities.

From the theoretical basis of the analysis it comes that new statistical information is necessary. Business statistics, balance of payments and direct investments statistics should co-operate closely for collecting this new information by adapting step by step already existing (or constructing) statistical systems.

Proposal of a study to develop a methodology for statistics on activities carried out via establishment abroad, with a view to compiling a chapter on the international activities of services enterprises in the methodology manual for statistics on services enterprises is made.

Eurostat is seeking the advice of the Voorburg Group on the proposals made, on how better conduct the study, being very interested to receive materials which will enable the study to be based on countries experiences in the area.

The paper is complemented by two annexes prepared by M-P. Benassi and J.W.S. Walton.

**A methodology for statistics on activity carried out
via establishment abroad by service enterprises
and its implications for European policy on services**

by Thierry Coulet* and Marco Lancetti**

0. Preface on terminology

Please note that the term "establishment trade" is used by community terminology in the sense of "freedom of establishment" viz., activity carried out via establishment abroad. But care is needed to avoid confusion with the "Anglo-Saxon" use of the word "establishment" to denote a particular statistical unit (similar to EC's "local unit"). Note that the ESA defines "notional resident units", whether set up with the legal form of an enterprise or that of a branch, as resident "institutional units" and hence as equivalent to enterprises.

The duality of international service activity has been endorsed (not without some ambiguity) by the GATS negotiations, where the definition of international trade in services covers "the supply of a service through the commercial presence of service providing entities of one party in the territory of any other party".

In the OECD questionnaire used during the seminar on globalisation indicators (Paris, 12-13 November 1992) reference is made to activities of foreign-controlled enterprises (inward investment) and to activities of domestic firms abroad (outward direct investment). The OECD questionnaire makes also reference to intra-firm trade as "trade between a subsidiary and its parent company or between subsidiaries of the same group located in different countries".

In M-P. Benassi document "Service Transactions in the Balance of Payments" presented at the seventh Voorburg group meeting, a proposal for a typology taken from a complex matrix of transactions between operators that can be linked together by capital or other agreements is made (abstract from M-P. Benassi document is reproduced in annex 1).

Faced to this cacophony, that in itself justify proposal made at section 2 for a methodology study, the authors wish to clarify that to simplify the term "establishment trade" is used as synonymous with "activity via establishment abroad". "Direct investment" and "foreign-control" being different concepts, the reference made to "direct investments" is mainly done in the sense of a statistical system related to the Balance of Payments which could be a starting point to build over a system on activity

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carried out abroad by units which are controlled by resident enterprises. This system being build by adapting and enlarging step by step already existing statistics.

1. Introduction

Following a study of the role of statistics on service enterprises in the analysis of international activity in services, a series of conclusions was put forward, the most of important of which concerned the creation of a system of statistical information on activity carried out via establishment abroad by service enterprises. The study described below should be seen as part of the contribution of statistics on service enterprises to the analysis of international activity in the services sector.

1.1 Internationalization of service activities and establishment trade: the theoretical basis of the analysis

Services have for many years been the poor relation of economic analysis, particularly analysis of international trade. Several reasons have been put forward to explain this Cinderella status: the fact that services are not readily definable, a lack of information on these activities, especially statistical information, the fact that there is no international trade in the sector, and so on.(1)

The opening of the Uruguay Round and the fact that international service activities have been placed in the spotlight have lent new urgency to economic analyses. Research activity has mushroomed, focusing on the determinants of international trade in services, the application of the theory of comparative advantage and the HOS theorem(2) and the application of the principle of economies of scale.(3) However, it is the analysis of the nature of international activity in services which has attracted the most attention.

The starting point of this attention is a simple observation which is far from new: that a service can, in some cases, be provided at a distance. However, it is often necessary for both producer and consumer to be present in the same place at the same time. This applies mainly to personal services, but also to many others requiring some interaction

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- (1) See, in particular, Kierzkowski, "Services in the development process and theory of international trade", Discussion Papers in International Economics, No 8405, Geneva, 1984; Gershuny J. and Miles L., "Economic theory - History of a neglect", in "The New Service Economy", Frances Pinter, London, 1983, Chapter 2.
 - (2) HSO (Hecksher, Ohlin, Samuelson) see, in particular, Deardorff, A.V., "Comparative advantage and international trade and investment in services", working paper, University of Pennsylvania, Philadelphia, 1985. Deardorff develops an original theory of the "missing factor". See also Sapir A. and Lutz E., "Trade in services: economic determinants and development related issues", World Bank Staff Working Papers, No 480, Washington, 1981. Sapir and Lutz develop the concept of "structural advantages".
 - (3) See, in particular, Nusbaumer J., "Les services: nouvelle donne de l'économie", Economica, Paris, 1984.

between producer and consumer. International trade in services can thus entail a temporary change of location on the part of either the producer (e.g. an accountant may visit the premises of a foreign company to audit its accounts) or the consumer (e.g. a student at a foreign university). In cases where producers go abroad, it is usually in order to provide an occasional service.

If a provider of services wishes to develop regular activity abroad, however, he will often find it necessary to become established in the country concerned.

Many service activities quite simply do not involve international trade in the strict sense of trade between residents of different countries, while in other cases international trade in services in the strict sense accounts for only a small fraction of international activity.

One of the fundamental features of the internationalization of service activities is thus the special importance attaching to foreign establishment trade.(4)

Thuillier states that "the advantages of proximity are such that service enterprises prefer establishment trade to exporting".(5) This conclusion is confirmed by the few statistics which are available on international trade in services and establishment trade, which "converge to underline the preponderance of establishment trade in the development of international service activities".(6) Thuillier also says that this phenomenon is linked not so much to the non-transferability of services (i.e. the fact that they are intangible and cannot be stocked) as to the nature of the relationship between producer and consumer.(7)

Similarly, Mayère and Bonamy conclude that "internationalization in services is in general directly conditional on the multilocalization of production".(8) Indeed, they ask whether it is relevant to apply the logic of trade to "activities for which it appears more appropriate to talk in terms of international production and consumption of services".(9) The logic of internationalization in services is therefore the logic of "all or nothing".

Numerous authors have developed analyses in which establishment trade appears as a form of international services activity in its own right. Dunning, for example, states: "International involvement in services ... usually takes three forms: exports, licensing and foreign direct investment; this embraces the sale of services produced by the

(4) Thuillier J.P., "Les sociétés françaises de services sur les marchés internationaux", Seminar "Internationalisation des services - Les enjeux", C.F.C.E., Paris, 27 January 1993, p. 3.

(5) Ibid.

(6) Thuillier J.P., "Les déterminants de la multinationalisation des entreprises de services", working document, Institut de Recherches et de Documentation en Sciences Sociales, Université de Rouen.

(7) Ibid.

(8) Mayère A. and Bonamy J., "Internationalisation des services, partenariat et mise en réseaux", symposium "Métropoles en déséquilibre?", Lyon, 22-23 november 1990, p. 4.

(9) Ibid.

foreign affiliates of multinational enterprises".(10)

Schwamm and Merciai, taking as their basis work by the Office of the US Trade Representative, distinguish five forms of trade in services: transactions from country to country, licensing contracts, journeys undertaken by consumers, journeys undertaken by producers, and the sale of services via branch offices or subsidiaries. They consider that "the export of services is generally impossible without prior direct investment (establishment)".(11)

Gadrey begins his analysis of the "economic geography of services" as follows: "As regards the internationalization of services, we shall examine in turn two forms: international trade and direct foreign investment (multinational production)".(12) He goes on to distinguish four types of international trade, depending on the mobility of the producer and of the consumer, and four types of direct investment, depending on the legal and organizational form. Gadrey, too, notes the inherent difficulties associated with international trade in services and the "strong growth" of establishment trade as a form of internationalization.(13)

It is worth repeating that this special feature of the internationalization of services arises not so much from "technical" constraints (simultaneity and proximity) as from the need for effective interaction between the producer and consumer of the service. Moreover, although technical innovations in the fields of telecoms and information technology have overcome some of the technical constraints of proximity, they have not, generally speaking, eliminated the usefulness of a local presence. Thus, Bhagwati(14) writes: "If tradeability of services has increased through "long-distancing" trends in the provision of services, it has also increased for the very different reason that, where physical proximity continues to be necessary but has been traditionally difficult or impossible to achieve across countries, organizational innovations have appeared which have made such proximity feasible and even economical."

This duality in international service activity - with the two basic forms of export and establishment (the other forms identified above generally being special forms of export) - clearly has an impact on the concept of international activity itself. Nusbaumer, for example, states: "Exchange of services involves transactions which do not fall within the traditional definition of international trade; in common usage and in all economic literature to date, this term is understood to cover the movement of goods across national borders. Extended to services, it may be considered to cover only cross-border

(10) Dunning J.H., "Multinational enterprises and the growth of services: some conceptual and theoretical issues", *The Service Industries Journal*, Vol. 9, No 1, January 1989, p. 17.

(11) Schwamm H. and Merciai P., "Les entreprises multinationales et les services", Presses Universitaires de France, Paris, 1985.

(12) Gadrey J., "L'économie des services", La Decouverte, Paris, 1992, p. 104.

(13) Ibid, p. 111.

(14) Bhagwati J., "International trade in services and its relevance for economic development", in "The emerging service economy", Giarini O. (ed.), Pergamon Press, Oxford, 1986.

sales. Technically speaking, a great many services can be traded across borders but, even if this is so, a presence in foreign markets may still be necessary for a variety of reasons."⁽¹⁵⁾ This comes down to the relational aspect of services: "First-hand knowledge of the working of the foreign markets is an essential operation tool for certain services. Building up and maintaining consumer confidence may not be possible without personal contacts [...]. Such considerations lead to the conclusion that a definition of international transactions in services which excludes the direct sale abroad of services through a presence in foreign markets may unduly restrict the scope of any consideration of issues in this sector."⁽¹⁶⁾

Several authors draw conclusions from these analyses as regards statistics: "Sales in the local market by established firms owned or controlled by foreign interests are transactions between residents of the same country. According to IMF definitions, they are not international transactions [...]. Therefore, in order to include such transactions in the definition of trade, one would need to adopt an IMF-plus definition of trade."⁽¹⁷⁾

A proposal for just such an "IMF-plus" definition has been put forward by Lederer et al., who suggest that a second balance-of-payments account be compiled, based on the criterion of ownership, to complement the traditional system, which is based on the criterion of residence.⁽¹⁸⁾ Ascher and Whichard think that such a system would be difficult to set up at present, and concentrate instead on more conventional proposals for improving existing statistics.⁽¹⁹⁾

Without going as far as Lederer et al., a number of official bodies have noted the special nature of international service activity and the gap in current statistics. Some of these bodies, most notably US agencies such as the Bureau of Economic Analysis and the Office of the US Trade Representative, have developed very extensive statistical systems covering establishment trade. Nederland and Denmark are collecting some information on services activities via establishment abroad. France is currently measuring activities of domestic foreign-controlled enterprises and a register of branches of domestic firms abroad has now been established.

1.2 Statistics on the international activity of service enterprises in the form of establishment trade and the political implications

The duality of international service activity has been endorsed (not without some ambiguity) by the GATS negotiations, where the definition of international trade in

(15) Nusbaumer, J., "Services in the global market", Kluwer Academic Publishers, Boston, 1987, pp. 185-186.

(16) Ibid. p. 186.

(17) Ibid. p. 187.

(18) Lederer, E.P., Lederer W. and Sammons R.L., "International services transactions of the United States: proposals for improvement in data collection". Report for the Departments of State and Commerce and the Office of the US Trade Representative, Washington, 1982.

(19) Ascher B. and Whichard O.G., "Improving services trade data", in "The Emerging Service Economy", op. cit.

services covers "the supply of a service through the commercial presence of service providing entities of one Party in the territory of any other Party". It is also sanctioned by the Treaty of Rome, in which the liberalization of service activities is based on the two principles of "freedom to provide services" (the "trade" aspect, Article 59) and "freedom of establishment" (the "establishment" aspect, Article 52).

However, the GATS negotiations and the completion of the Single Market in services are proceeding on the basis of information which is far from complete. There is at present no coherent statistical information at European level on service activities carried out in the form of establishment trade.

The only statistics currently available are balance-of-payments statistics, which cover all international trade in cross-border services, but there is no information directly concerned with international activity carried out via an establishment abroad. What is available is, at best, "correlated" information on direct investment, revenue from direct investment, direct investment stocks etc.

The only certainty is that activity conducted through establishments abroad, although its actual extent is not known with any accuracy, is an essential element, if not the essential element, in international service activity. (According to GATT estimates, worldwide establishment trade is now worth between \$2 000 and \$3 000 billion, compared with \$900 billion for international trade in cross-border services.)

This is no basis for analysing the effects which completion of the Single Market in services or the GATS negotiations will have on these activities.

Implementation of the Single Market may lead service enterprises - indeed this is among its *raison d'être* - to develop their activities in Europe and consequently change the form of their international activities within the European Community. As has already been seen, the development of an enterprise's activity in Europe could lead it to favour the extension of its Community network at the expense of its cross-border activities. If this happens, what will be the result? Intra-Community trade in services as recorded in balance-of-payments data will decrease, whereas the enterprise's intra-Community activity will have grown.

It is therefore impossible to understand the effects of a Single Market policy, and consequently to take informed decisions about such a policy, without being able to see both parts of the picture clearly.

The same reasoning can be applied to the GATS. The current negotiations are based on a definition which covers establishment trade although, as we have seen, there is only the vaguest idea of the actual extent of this trade. Again, the only certainty is that establishment trade is much more important than cross-border trade.

What is needed, therefore, is a genuine system of statistical information on activity

carried out via establishment abroad by service enterprises.

1.3 Domestic establishment trade, foreign establishment trade, statistics on service enterprises and the balance of payments

This information exists, at least in part, in hidden form in business statistics, which gather information on enterprises' turnover and from where they are controlled. All that is needed to make the information usable is to give priority to collecting the necessary primary information and to establish a methodology, definitions and tools which are compatible with those in other statistical fields.

Nevertheless, when collecting statistical information on establishment trade, it is necessary to distinguish between information on activities performed abroad by units controlled by resident enterprises on the one hand, and domestic activities performed by foreign-controlled units on the other.

Although these two types of information are symmetrical, they are obviously obtained from different statistical sources and raise specific problems of methodology.

By nature, information on domestic activities carried out by foreign-controlled units (domestic establishment trade) comes under "business statistics". It requires the matching of data on turnover by product and information on the control of resident units collected in connection with those statistics.

On the other hand, information on activity carried out abroad by units which are controlled by resident enterprises can only be derived starting from data on direct foreign investment and, as such, comes under a statistical system related to the balance of payments.

Each of the relevant statistical systems: "business statistics and balance of payments", should therefore cooperate closely in developing statistics on establishment trade.

1.4 The need for coordination between services statistics and balance of payments towards a new information

If, depending on the direction of the flow, the development of statistics on establishment trade comes under two statistical systems and therefore in a majority of cases under the responsibility of different administrative bodies or units (Central Statistical Offices, Central Banks, Ministry of Foreign Affairs, etc.), it is quite obvious that coordination is necessary to avoid double work and cacophony.

It will not be possible to develop two symmetrical statistical systems for the same economic analyses and economic policies unless they share the same methodological base.

From the theoretical basis of the analysis of internationalization of service activities and

establishment trade above-mentioned, it comes that coordination is a necessary prerequisite but in itself will not completely satisfy the need for information.

Once the economic concepts, their related statistical definitions and relationship to other statistical area have been clarified, it will be necessary to work out the actual methodology for collecting this new information by adapting step by step already existing (or constructing) statistical systems.

2. Aim of the study: to develop a methodology for statistics on domestic establishment trade, with a view to compiling a chapter on the international activities of service enterprises in the Methodology Manual for Statistics on Service Enterprises

The aim of this study is to develop the methodology of statistics on establishment trade as regards the part which comes under statistics on service enterprises ("domestic establishment trade"), while maintaining coordination and consistency between these methodological developments and those undertaken in connection with the balance of payments for "foreign establishment trade".

In order to measure domestic establishment trade, it will be necessary to combine two types of information which are already covered by the methodology of service enterprise statistics:

- information on turnover by product;
- information on the control of the enterprises in question, distinctions being made between resident/foreign and Community/non-Community control.

It will therefore not be sufficient to define the nature of the information to be provided: it will be necessary to devise a genuine methodology on activity carried out via establishment abroad by service enterprises.

In the first instance, this methodology will have to define the concepts of direct investment (or commercial presence) and of international activity carried out by such establishments. It is obvious, for example, that this type of activity cannot be equated with imports and exports as defined for balance-of-payments purposes. It is therefore necessary to define the status of this type of operation.

Once the concepts and their relationship to other statistical areas have been clarified, it will be necessary to work out the actual methodology for collecting this new information, i.e. to define the type of "primary" information required, the sources, the methods of evaluation etc.

The following are some examples of the methodological problems which will have to be solved:

- The definition of direct investment: to complement and to specify the IMF criteria of

"effective voice in management" which is wider version of the criterion of "control", several criteria could be applied, and several thresholds of capital ownership may be relevant for deciding whether a unit is under foreign control (10%, 20%, 50%). It will be necessary to decide on one (or two?) criteria. "Control" is the criterion used in the EC directives on concentration.(20)

- How to treat chains of ownership: in other words, how to record the activity carried out in one country by a unit which is controlled by a foreign enterprise which itself is controlled by an enterprise in a third country. How far up the ownership chain should we go? How should we record the activity of a resident unit controlled by a foreign enterprise which is itself controlled by a resident enterprise?
- How to record affiliations in sectors other than that in which the parent company operates. Where domestic establishment trade is concerned, it would seem natural to take as a basis the activity of the foreign-controlled resident unit. The question of how to access information on the activity of a unit in another country arises mainly with regard to foreign establishment trade.
- How to treat exports by foreign-controlled units, in particular exports to the country of the parent company.

This study is part of work on preparing a chapter on the international activity of service enterprises for the Methodology Manual for Statistics on Service Enterprises. This chapter will also have to deal with the methodology of exports by service enterprises from their country of origin, using a "sectoral" approach to international trade in services which complements the "transactions" approach adopted for balance-of-payments purposes.

Furthermore, this chapter will need to deal with how to analyse other forms of international alliance between service companies (cooperation networks, franchising, licensing etc.) and how to record their activities.

These supplementary studies, which are likely to be of more modest scope than the study of establishment trade, are necessary preconditions for a full chapter on the international activity of service enterprises.

3. Work programme

The study will comprise the following four phases:

1) Definition of the information required

An in-depth study will be carried out into the concepts underpinning the analysis of

(20) See Eurostat's Manual on Services Statistics - chapter on Insurance, at the foot of page 28.

establishment trade and into the user needs which emerge from the working documents of various organizations responsible for the conduct of policy in this field. The aim is to obtain a clear picture of the importance of this information and to define the desired information content.

2) Problem statement

The second phase, which will build on the definition of the information required, will comprise an examination of the main methodological problems (definitions, classifications, methods of collection, etc.) which will have to be solved if an information system on establishment trade in services is to be built up.

3) Inventory of available information

Some countries already collect certain items of information on foreign and domestic establishment trade. Precise knowledge of these countries' experiences, the available information and the methodologies they have adopted seems indispensable for formulating a Community methodology in this field.

4) Formulation of a Community methodology on activity carried out via establishment abroad by service enterprises

This, the key phase of the study, will consist of working out, on the basis of a synthesis of the previous elements, the actual methodology for the information system.

In the light of the information currently available, Phase 4 is likely to centre on the following five themes:

- definitions: direct investment, establishment trade, control etc.;
- identification of the primary information to be collected: please note that to simplify there is an implication in several places in the paper that only turnover would be needed in addition to profits (as already recorded, in principle, in the balance of payments). This may well suffice in most cases, but the common standards and surveys being developed go much further and cover the whole production account - input as well as output. In insurance, for instance, turnover is not an adequate proxy for output (see annex 2 attached). This speaks for concentrating on the activities of foreign-controlled enterprises rather than on the much more difficult - and perhaps unnecessary activities of domestic firms abroad side.
- choice of appropriate classifications;
- methods of collection;
- methods of aggregation and compilation.

Some of the problems and issues mentioned in the paper have been addressed in the Chapter on Insurance of Eurostat's Manual on Statistics of Services, though adaptations may be needed as a common methodology is developed (an abstract,

mainly descriptive of direct trade as well as of "establishment trade", is given by J.W.S. Walton in annex 2).

4. Conclusions

The development of a statistical information system on establishment trade is of major importance for statistics on service enterprises, the understanding of international service activities, the GATS negotiations and the monitoring of the Single Market in services. The system will fill a gap in statistics on a key aspect of policies in these fields.

A number of official bodies have already noted the special nature of international service activity and the gap in current statistics. Some of the bodies have developed very extensive statistical systems covering establishment trade.

Eurostat is seeking the advice of the Voorburg Group on the proposals made, on how better conduct the study, being very interested to receive materials which will enable the study to be based on countries experiences in the area.

SERVICE TRANSACTIONS IN THE BALANCE OF PAYMENTS

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ABSTRACT: The balance of payments (BOP) is the main source on international activities of enterprises of service sectors. It constitutes a territorial approach coherent with the National Accounts to measure transactions between residents and non residents and particularly cross border trade in services. But This approach is not sufficient to analyse all the international activities of enterprises and particularly the turnover of establishments abroad. A patrimonial approach, characterising enterprises with ownership would enable one to get rid of geographical frontiers and to assess the global activity of enterprises.

In the field of services, internationalisation entails a complex matrix of transactions between operators that can be linked together by capital or by other agreements. The above typology can help to better understand what is recorded in the BOP or not.

1) Direct cross border trade : transactions are exports and imports of services recorded as such in the BOP service account.

The product moves: A finished product is done in one country and directly sold to a final client abroad. This may concern studies (marketing, legal, accounting, research), software, databases, press agency services. The provider of the service has contacts with his clients mainly by post or telecommunications.

The provider moves: Providers of services are going temporarily to another country to render their services: technical support, construction, consulting, training, entertainment... The staff is supposed to come back when the work is achieved and the company continues to manage this staff.

The client moves: People travelling are buying services during their trips: transport, lodging and catering, entertainment, hairdressing, health, training ...

The transport moves or a space equipment is used: In transport activities, space launching or satellite services international trade occurs when the client is resident of a different country than the transport operator or the owner of the space equipment.

2) Indirect cross border trade (through a "commercial presence"): In the BOP, this is recorded like direct cross-border trade as exports and imports of services. When it is difficult to establish direct contacts between service providers of one country and final clients of another country a "commercial presence" is necessary. It can be any related company or agent which has contacts with the clients and the providers but produces nothing but an intermediation service.

3) Services requiring an international logistic (transportation, courier, telecommunication, postal services): Ideally, the service should be divided in as many parts as there are providers. Usually the client has no direct relationship with foreign companies, but parts of the service have been provided by non-resident agents so they constitute cross border trade in the BOP framework. However, in such cases data collection is difficult. When the companies involved are independant (e.g. national postal offices), they can provide information. When it is a complete network (e.g. courier companies) the relevant information may be simply not available depending on the accounting system adopted by the company.

4) Services produced within international agreements: In the BOP all kind of services transactions done under contract agreements are considered as imports and exports.

5) Services totally produced by direct investment establishments: Neither in the BOP nor in the SNA is the turnover locally produced and sold considered as international trade because domestically owned establishments abroad are non-residents and foreign owned establishments in the domestic territory are residents. Nothing will be recorded in the BOP. In that case a patrimonial approach is necessary.

6) Intra-group miscellaneous service transactions: They are considered as imports and exports in the BOP. The only problem is that they are sometimes not separately identified in the companies account because they are calculated on an apportioned basis.

7) Technological and other knowledge related activities: Sales of trade marks, patents, other rights, franchising fees are recorded in a special BOP service item.

ANNEX ON INSURANCE

John W.S. Walton

There is an Annex 4 to the Insurance Chapter, on international insurance transactions. This is mainly descriptive, of direct trade as well as of "establishment trade".

Domestic establishment trade. (Section 1.3 of the paper.)

Pages 28 and 29 of the Insurance Chapter propose 'designators' which would identify whether a domestic reporting unit (either enterprise or branch) is controlled from abroad, with a split between parent enterprises located in the EC and those located elsewhere. A full production account for such units could be obtained if the data base is set up correctly.

Foreign establishment trade. (Section 1.3 of the paper.)

Page 30 of the Insurance Chapter proposes to identify domestic (parent) enterprises which have affiliates abroad. Direct exports are identified as a sub-division of turnover in the production account, with a subdivision between EC and non-EC countries. It is proposed to obtain information on profits arising on outward direct investment, also with a split between EC and non-EC countries (Code 87a, page 71). It is not proposed to ask for information on the sales by the units situated abroad giving rise to these profits.

Methodological problems. (Page 7 of the paper.)

Definition of direct investment. See pages 28 and 71 of the Insurance Chapter.

Chains of ownership. See foot of page 29 of the Insurance Chapter.

Affiliations in other sectors (domestic establishment trade). See Code 3 (d) (ii), page 29 of the Insurance Chapter, in combination with Code 3 (d) (i), on the same page.

Special problems with insurance.

Turnover as a proxy for gross output. Turnover is an inadequate proxy for the value of production in the case of insurance, because of claims. The value of production may be only, say, 10-20% of turnover (including investment income), whilst in many service trades turnover is the same as gross output and intermediate inputs are relatively small. This does not matter in the case of domestic establishment trade, since it should be possible to record the full production account; in the case of establishment trade in foreign countries, however, it would be necessary to collect information on claims as well as on premiums, if the information were to be obtained through the country in which the parent enterprise is located, rather than

through the foreign country in which the unit is situated.

Reinsurance. The newly proposed "gross" treatment of reinsurance should greatly improve information on international reinsurance transactions. The value of reinsurance services purchased by direct insurers (to be treated as part of their intermediate inputs) would need to be split between services purchased from resident reinsurers and those purchased from non-resident reinsurers.

Information systems based on regulation. For both insurance and banking, the approach is to derive as much statistical information as possible as a by-product of the systems of regulation (including the requirements for the publication of annual accounts). But the EC Third Directives, establishing a common market, have limited the amount of information which national regulators can require for control. They can no longer require information for the branches of other EC insurers set up on their territory. As part of implementing the "freedom of establishment", these branches will be subject only to the control of the EC country in which the parent insurer is located, not that of the country in which the branch operates. The limitation of information on branches will not apply to the branches of non-EC insurers which operate in EC countries.

When an EC insurer operates through a subsidiary in another EC country, the subsidiary will have to submit accounts in accordance with the Directive on Annual Accounts. Possibly this will encourage the use of branches rather than subsidiaries, within the EC.

Therefore the regulatory system will be sufficient to provide aggregate figures, for the whole EC, on the amount of "establishment trade" within the EC through the legal form of branches, but not, of itself, sufficient for a sub-division into individual countries. That would appear to be needed, however, to compile balance of payments figures on an individual country basis, and to enable branches, as "notional resident units" (ESA, 214), to be included within the ambit of economic activity in a particular country.

Another aspect of the Third Directive for insurance is to ensure that there is "freedom to provide services" in another EC country, e.g., by mail order or with the assistance of local agents. That may encourage some shift from establishment trade to direct exports.