



## ► Frequently asked questions (FAQ)

# ► Social Protection for Workers in the Informal Economy

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## ▶ What is the informal economy?

The ILO adopted in 2015 the [Transition from the Informal to the Formal Economy Recommendation \(No. 204\)](#), where the term informal economy “refers to all economic activities by workers and economic units that are – in law or in practice – not covered or insufficiently covered by formal arrangements (section 2.(a)).

## ▶ What is the difference between the informal economy and the informal sector?

In its [Resolution concerning decent work and the informal economy](#), adopted by the ILO in 2002, the “term ‘informal economy’ is preferred over the concept ‘informal sector’. This is because the workers and enterprises in question do not fall within any given sector of economic activity. On the contrary, informal work appears and cuts across many different sectors. In that sense, it is better to see informal employment as a job-based concept, “defined in terms of the employment relationship and protections associated with the job of the worker.” (ILO 2018, p.7).

According to the ILO, informal employment includes informal jobs in informal sector enterprises, but also in formal sector enterprises, or households. Informal employment is found in many structured and strongly regulated branches of economic activity. For the ILO and OECD “the substantial share of informal employment in large formal enterprises can be significant and may result from lack of recognition of the employment relationship or from contracts that provide no social protection and other benefits.” (ILO and OECD 2019, p.38)

## ▶ Does the informal economy refer to the absence of regulations or also to their weak implementation?

For the ILO, informal employment refers to working arrangements that are *in practice* or *by law* not subject to national labour legislation, income taxation or entitlement to social protection or certain other employment benefits (advance notice of dismissal, severance pay, paid annual or sick leave, etc.).

## ▶ How does the concept of informal work compare to the concept of flexible employment?

The concept of flexible employment is adopted in the official English translation of the 2011 Social Insurance Law in China<sup>1</sup>. It refers to workers that are not employed under a full time labour relation. It is therefore close to the concept of non-standard forms of work, with some differences.<sup>2</sup>

According to ILO and OECD, non-standard forms of employment are not exclusively affected, but are more affected, by informality than standard forms of employment (ILO and OECD 2019). Labour laws have often not been applied to new forms of work due to the lack of 'fit' between new types of employment and the traditional rules of labour law that were designed for standard forms of employment. Non-standard work involves for example, working time that goes beyond normal standard practices or normal workplaces (outwork) that are insufficiently regulated (Hendrickk 2019). The concept of informality adds to the notion of flexibility the fact that there is not an adapted regulatory environment or the existing regulations are not fully implemented.

## ▶ What is the impact of unregulated forms of non-standard employment on the labour market?

A high proportion of nonstandard employment produces a number of negative effects on the labour market development, from a human capital development perspective and a social justice perspective. From a human capital perspective, non-standard employment is not conducive to skill development (Cooke and Jiang 2019:170). It holds down career advancement, and threatens workplace harmony. It can generate income disparities as a result of lower wages. It tends to decrease social security provision that is legally entitled and/or actually enjoyed.

Two examples illustrate these points. Cooke and Jiang (2019) report that in South Korea, large Korean firms (chaebol) expanded the use of subcontract firms to be based on the company premises. Workers are hired by the subcontracting firm who also decides their employment

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<sup>1</sup> "A proprietor of privately or individually-owned business with no hired labour, a part-time worker who is not covered by the basic old-age insurance system through his or her employer, and any other person in employment of flexible forms, may elect to enroll in the basic old-age insurance system, and the person in question shall make basic old-age insurance contributions."

In [http://www.mohrss.gov.cn/qjhzs/GJHZzhengcewenjian/201506/t20150625\\_212401.html](http://www.mohrss.gov.cn/qjhzs/GJHZzhengcewenjian/201506/t20150625_212401.html)

<sup>2</sup> With the exclusion of temporary or short term contracts, that are full time employment that is covered by labour relations and social security, but is also conventionally considered non standard form of employment.

terms and conditions (Cooke and Jiang 2019:167). In Japan, interns work in small-scale family-run businesses, which operate on a low margin and quick turnaround time. Officially as trainees, they are paid lower hourly wages than standard employees are, and are paid by piece (Cooke and Jiang 2019:165). In both situations, workers work alongside permanent employees of the firms doing similar work but they earn less and are not covered by pension and/or unemployment insurance.

## ▶ Why is the concept of work in the informal economy important?

Workers and economic units are increasingly engaged in flexible work arrangements, including outsourcing and subcontracting; some are found at the periphery of the core enterprise or at the lowest end of the production chain, and have decent work deficits. The concept of flexible work does not inform policy makers whether there is appropriate regulation or enforcement of regulations on social protection and working conditions work applicable to such forms of work. Informal economy can distinguish regulated and non-regulated forms of flexible work in law and in practice.

## ▶ How can informal economy be measured according to the ILO?

The definition of informal employment differentiates three groups of workers: (i) employees, (ii) employers and own account workers, and (iii) contributing family members.

- An employee is considered informally employed if his/her employer does not contribute to social security on his/her behalf or, in the case of a missing answer, if he/she does not benefit from paid annual leave or sick leave.
- An employer (with hired workers) and an own-account worker (without hired workers) is considered informally employed if he or she runs an economic unit in the informal sector (a non-incorporated private enterprise without a formal bookkeeping system or not registered with relevant national authorities). In the case of the question not asked or a missing answer, the enterprise is considered part of the informal sector if there is no fixed place of work or it employs five employees or fewer. This threshold can vary, depending on the reporting structure of country questionnaires.
- Contributing family workers are informally employed by definition, regardless of whether they work in formal or informal sector enterprises.

Informal economy is usually measured by the inclusion of specific questions in labour force surveys or dedicated surveys on the informal economy, or a combination of the two.

Recommendation 204 Recommendation concerning the transition from the informal economy  
12 June 2015 guides member states to monitor and evaluate the progress towards formalization. It says that " (art 37). *In developing or revising the concepts, definitions and methodology used in the production of data, statistics and indicators on the informal economy, Members should take into consideration relevant guidance provided by the International Labour Organization, in particular and as appropriate, the guidelines concerning a statistical definition of informal employment adopted by the 17th International Conference of Labour Statisticians in 2003 and their subsequent updates.*"

## ► **Is informal economy linked to criminal or illicit activities?**

The concept of informal economy excludes criminal and illicit work. It does not for example the provision of services or the production, sale, possession or use of goods forbidden by law, including the illicit production and trafficking of drugs, the illicit manufacturing of and trafficking in firearms, trafficking in persons, and money laundering, as defined in the relevant international treaties.

## ► **Does the provision of a social protection floor guarantee that employment is no longer informal?**

For many households dependent on the informal economy, lack of effective financial protection against health risks, occupational hazards, unemployment or old age often results in significant financial burdens that can lead to poverty. A social protection floor contributes to reducing poverty in informal work related to the financial consequences of these risks. However, care needs to be taken that existing contributory schemes may not be sufficiently adapted to the situation of informal workers and may render regulations inapplicable in practice. Where non-contributory schemes are established to guarantee basic income security, benefit levels may be too low which may lead to persistent inequalities.

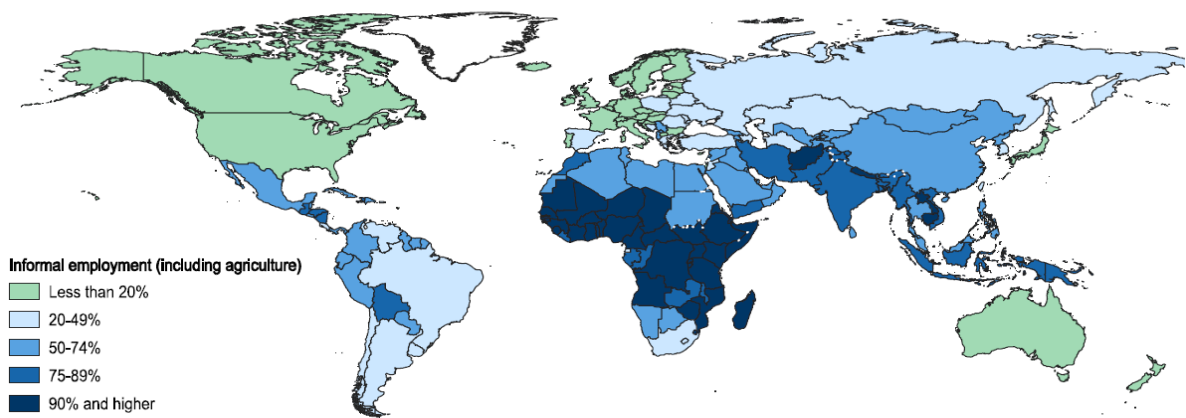
In addition, the informal economy is characterized by several deficits tied to the nature of the activities. For example, labour law affords other workers job security, working time regulations, holidays, minimum wage and health and safety protections which are not provided to workers in the informal economy due to the lack of their sufficient recognition, regulation or the enforcement of these. Work in the informal economy is often characterized by small or undefined workplaces, unsafe and unhealthy working conditions, low levels of skills and productivity, low or irregular incomes, long working hours and lack of access to information, markets, finance, training and technology. ILO Recommendation 204 recommends a diversity with tailored

approaches to the informal economy and the establishment of an appropriate legislative and regulatory framework.

## ► Is informal economy characteristic only of developing countries?

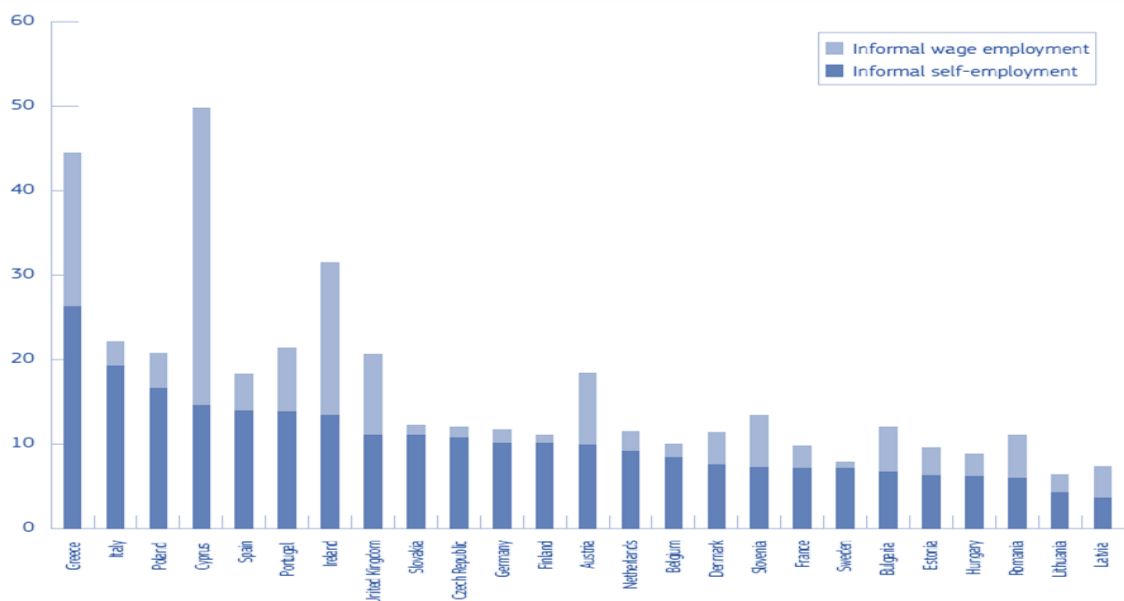
The informal economy is more prevalent in the global south but is not exclusive of developing countries. In many countries, both developing and industrialized, there are linkages between changes in the organization of work and the growth of the informal economy. Informal employment ranges from 10%-50% in Europe (Fig. 2) and 31% to 99.6% in Asia

**FIGURE 1. SHARE OF INFORMAL EMPLOYMENT IN TOTAL EMPLOYMENT INCLUDING AGRICULTURE (2016)**



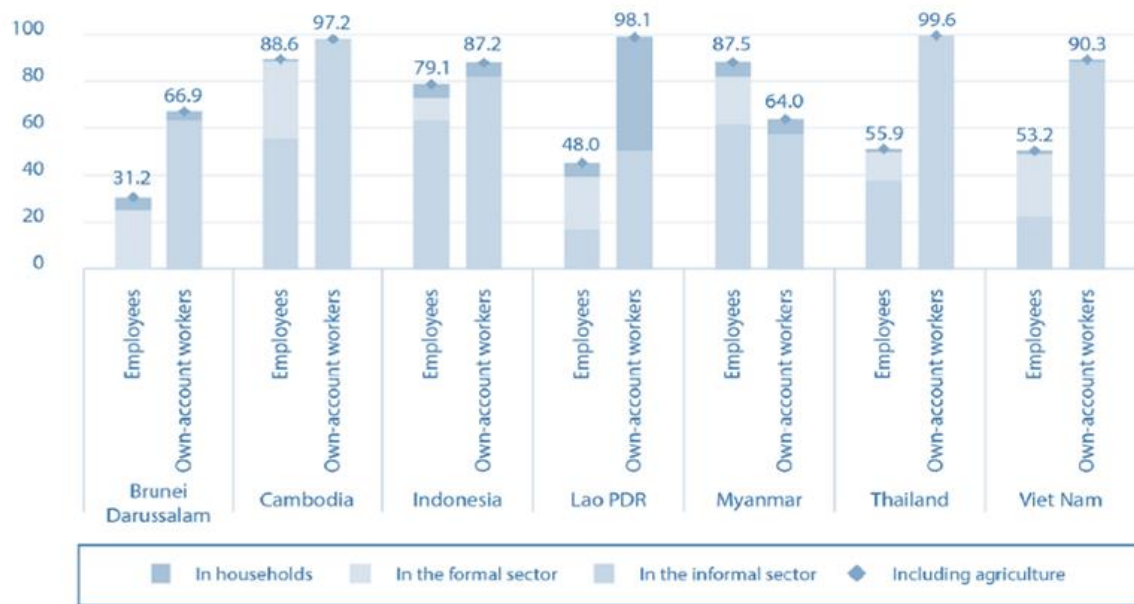
Source: ILO, 2018

**FIGURE 2. INFORMAL EMPLOYMENT IN EUROPE**



Source: Hazans (2011), "Informal Workers across Europe: Evidence from 30 Countries", IZA Discussion Paper No. 5871, Institute for the Study of Labor, Bonn.

FIGURE 3. SHARE OF INFORMAL EMPLOYMENT IN TOTAL EMPLOYMENT IN ASIA



Source: ILO calculations based on household survey micro datasets, based on ILO, 2018a.

Industrialisation and economic growth are a very important driver of formalization. Indeed, sustained economic growth results in more predictable labour markets, thus favouring an increase in long-term contracts. In this context, formalization becomes more feasible (Maurizio and Vázquez, 2019). Nevertheless, economic growth alone will not solve the challenge of mass informal employment. Comparative data shows that countries with similar level economic development (measured by GDP per capita) are presenting very different levels of informality. In effect, the problem of mass informality is rooted in the inability of growth patterns to create sufficient formal jobs to absorb all those who want to work (either new entrants or those trapped in the informal economy). Structural transformation leading to reducing informal non-wage earners and increasing formal wage earners, and to up-scaling economic units and increasing their productivity, are crucial conditions for transition from the informal to the formal economy (ILO 2018:5-6)

## ► What is a dependent contractor?

The term “Dependent Contractor” is an international term adopted at the 20th International Conference of Labour Statisticians (ICLS) in October 2018. A Resolution was passed at this conference to include a new meta-category of Dependent Contractors in the revised International Classification of Status in Employment (designated ICSE 18).

Dependent contractors are “Workers who have contractual arrangements of a commercial nature (but not a contract of employment) to provide goods or services for or through another economic unit. They are not employees of that economic unit, but are dependent on that unit for organization and execution of the work, income, or for access to the market”.

*"They are workers employed for profit, who are dependent on another entity that exercises control over their productive activities and directly benefits from the work performed by them."*

It is added that:

- Their dependency may be of an operational nature or an economic nature such as through control over access to the market, the price for the goods produced or services provided...
- The economic units on which they depend may be market or non-market units which benefit from a share in the proceeds of sales of goods or services produced by the dependent contractor...
- The activity of the dependent contractor would potentially be at risk in the event of termination of the contractual relationship with that economic unit.

## ▶ What is the ILO's position regarding the enactment in law of the legal status of dependent self-employment?

Dependent self-employment is recognized as a separate legal category in certain countries (including Germany, Spain and the United Kingdom). One of the risks is that it may hide disguised employment, and that it may therefore also lower the level of protection (transforming employees into dependent self-employed workers).

This is currently not prohibited by international labour standards. However, Recommendation No. 198 (2) stresses that the determination of the existence of an employment relationship (ER) should be based on the primacy of facts instead of the contractual characterization of the relationship. Accordingly, states should consider the possibility of a broad range of means for determining the existence of an ER, and institute the legal presumption that an ER exists where some indicators are present, determining that certain workers must be deemed to be either employed or self-employed.

Possible indicators include instructions / control, integration in the organization of the enterprise, specified working hours, periodic payment of remuneration, absence of financial risk. Finally, according to the ILO, the settlement of disputes concerning the employment relationship should be a matter for industrial or other tribunals or arbitration authorities.

## ▶ Is there a specific position of the ILO concerning employment relations in the platform economy?

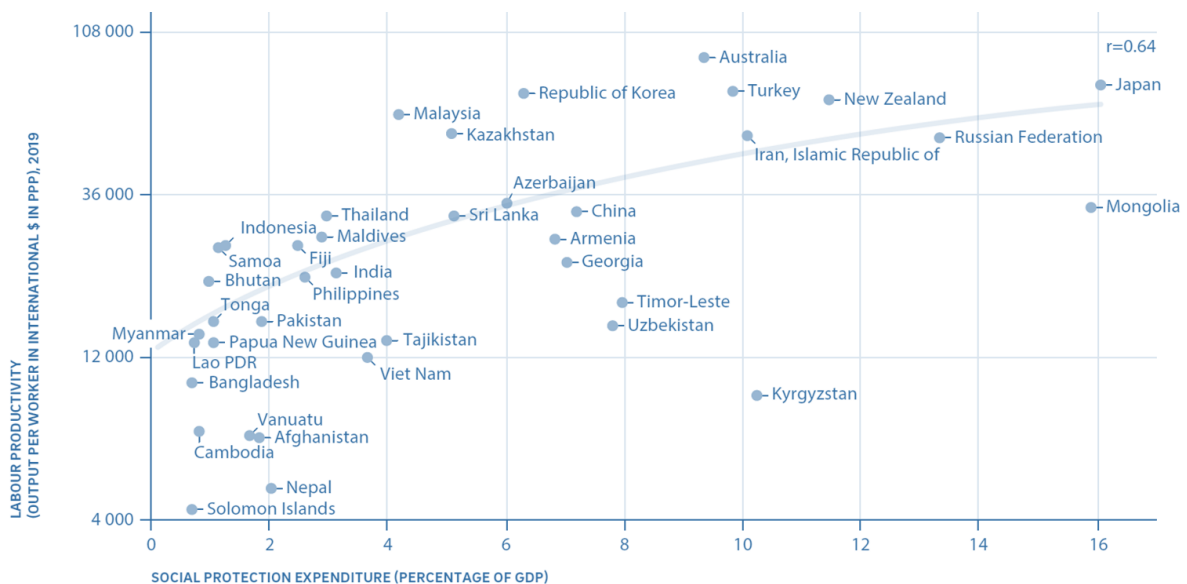


There are no specific ILO positions regarding platform work contractual relations. Conclusions reached across national jurisdictions are at early stages, they have varied - between and within countries. There is a large diversity of the modalities of operation of digital platforms, including among crowdwork (web-based work) and location- based platform work.

## ▶ How des social protection contribute to formalisation?

One driver is the contribution of social protection to furthering labour productivity which helps set informal jobs in sustainable growth paths.

FIGURE 5. SOCIAL PROTECTION AND PRODUCTIVITY



SOURCE: ILO AND UNESCAP. 2020 SOCIAL OUTLOOK FOR ASIA AND THE PACIFIC: THE PROTECTION WE WANT.

A growing body of evidence shows that the extension of social security coverage, by promoting access to health care and education, contributes to enhancing nutrition and health status and plays an important role in promoting productive employment. Indeed, informality is associated with low education levels and health status.

At the same time, the formalities required for social security coverage, such as the registration of households or individuals with the public authorities, can constitute a first step towards their formalization and the realization of their civil, economic and social rights (including the right to vote, to property and to education). The experience of [Brasil](#) and [Argentina](#) showed how social protection, combined with other economic and labour instruments provided pathways to formalisation.

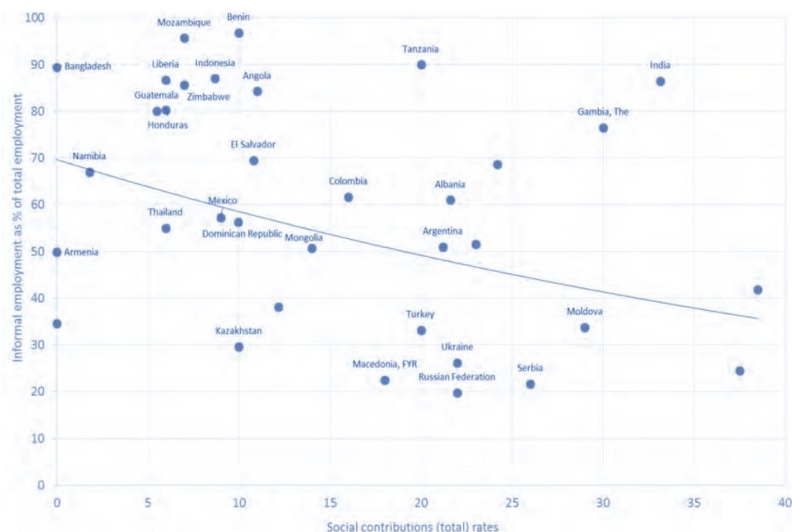
## ▶ **What drives the expansion of the informal economy today?**

There is a variety of forms of informal work with distinct manifestations. Therefore, the drivers depend on specific contexts. In many developing countries, the pressure exerted by low-skilled labour continues to be a major driver of informal employment. When good jobs (usually high skilled jobs in the formal economy) are scarce, a large number of people – often the least educated, who cannot compete – engage in low-productive and informal jobs as part of a survival strategy (OECD 2019:51). In middle income and industrialised countries, the segmentation in the labour market, which prevents low-skilled workers from taking formal jobs with state-mandated benefits is another driver of informalisation. To increase global competitiveness, investors are restructuring production and distribution to generate more flexible, productive systems and higher efficiency gains, including through outsourcing or subcontracting productive and labour processes within global value chains. This can trigger formal firms to shift formal wage workers to informal employment arrangements and creates a demand for goods and services from small production units that may operate in the informal economy and tend to outsource some of their work to isolated informal workers.

## ▶ **Are social security contributions major barriers for formalization?**

Informality depends on a number of social, economic and institutional factors. A recent study on entrepreneurship in 142 countries rejects the classic economics hypothesis that informality is associated with high taxes and points to the importance of institutional factors (Williams and Kedir 2017). The ILO (2019) indicates that the share of social protection expenditures paid by social contributions varies from country to country. In addition, empirical evidence shows that there is no negative correlation between the level of contributions (ILO 2019:59) and informality.

**FIGURE 6. SOCIAL CONTRIBUTIONS (TOTAL) RATES VERSUS INFORMAL EMPLOYMENT SHARE IN TOTAL EMPLOYMENT**



**IN: ILO 2019 FISCAL SPACE FOR SOCIAL PROTECTION. A HANDBOOK FOR ASSESSING FINANCING OPTIONS, P.59**

While many factors influence the costs and benefits of informality, often it is their comparison that matters. The impact of social security contributions on the labour market cannot be analysed without reference to the benefits and injection of cash in the economy that it produces. Social security contributions are linked to legal entitlements and should be considered a deferred wage and a social and economic investment, rather than a simple item of labour cost as indicated by the term “tax”. Social security contributions can be clearly linked to a variety of positive social and economic implications.

There is a strong correlation between the extent to which regulations are fairly and effectively implemented and enforced and the level of informality across countries at various stages of development. Where compliance is not strictly enforced across economic sectors or occupations, a rising tax burden on compliant industries or jobs can incentivise informality in those industries, expanding the informal economy and creating a vicious cycle by further inclining governments to push up taxes to keep up revenues. This evidence suggests that a narrow focus on reducing taxes may miss more important institutional factors that can facilitate the transition to the formal economy.

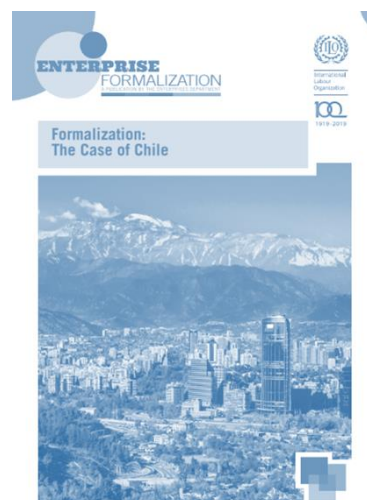
**► Why is it important to consider administrative constraints in the coverage of social security in the informal economy?**

Large informal economies can be triggered by regulatory inadequacies and administrative barriers. In turn, social protection coverage is associated with good governance and trust in the institutions. In some countries, bringing informal actors in line with regulations can entail extensive and cumbersome administrative procedures, paperwork and bureaucracy that cost time and resources.

Therefore, according to the ILO, countries should progressively extend the coverage of social insurance to those in the informal economy and, if necessary, adapt regulatory and administrative procedures. In effect, countries that were successful in formalising the informal economy have introduced specific measures to incentivise formalisation of enterprises and regulations to simplify business registration.

## ► Are there country success stories in formalizing the informal economy in the recent decades?

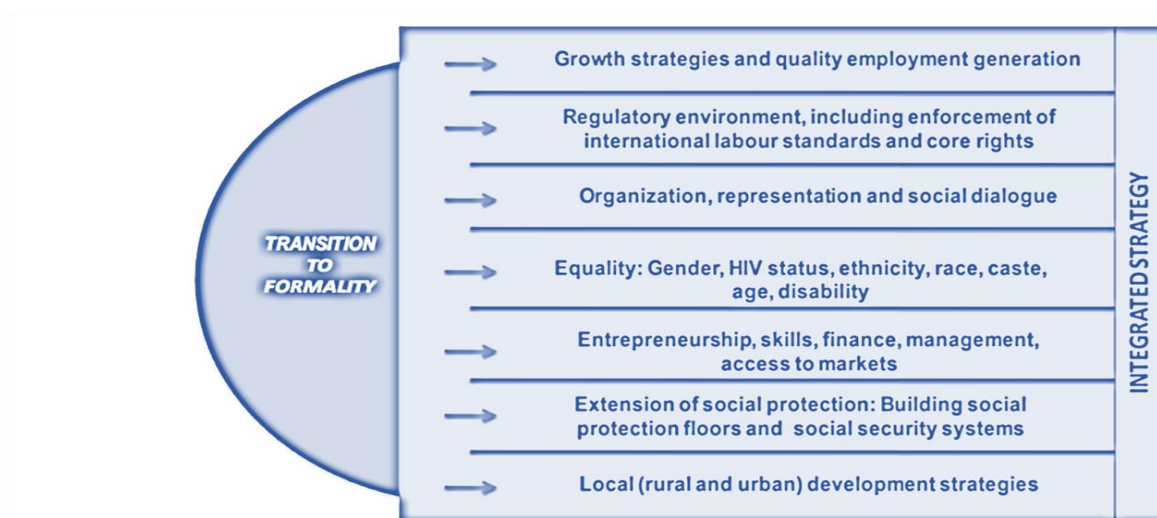
Since the turn of the century, in early 2000s, a trend towards increase in formality has been observed in several developing countries around the world. This has happened in Latin American countries and also in Africa and Asia. The number of formal jobs rose by almost 60% in Argentina between 2003 and 2017, while total employment increased by 20%. In Brazil, these numbers are 40% and 20%, respectively. The process of formalization was even more pronounced in Ecuador, Paraguay and Peru, where the number of registered jobs more than doubled during the period under review (Mauricio and Vasquez 2019). Chile also experienced a substantial reduction in its labour informality rate since 2010, with a fall from around 40 % to 29 % of all active persons by June 2018.



## ► What strategies did these countries implement to reduce the incidence of the informal economy?

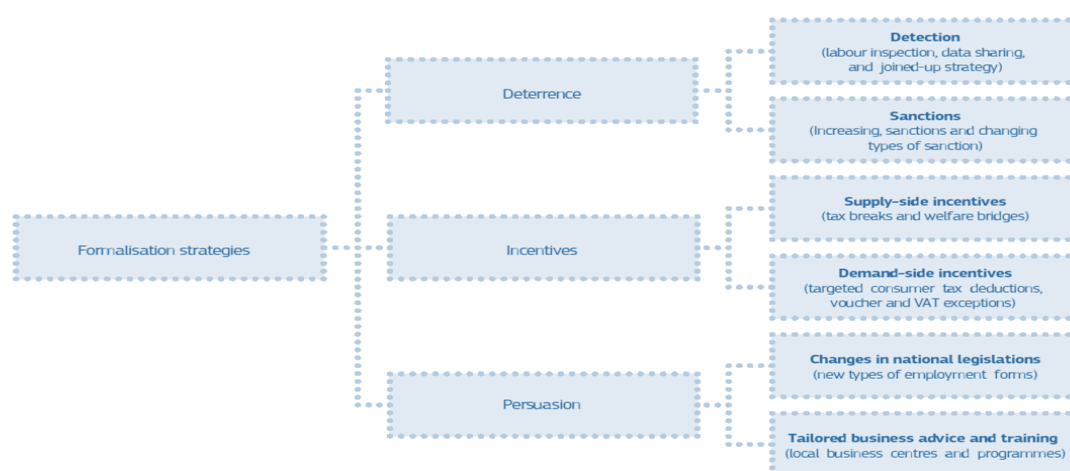
For the ILO, it is necessary to have a combination of integration strategies for formalisation. Indeed, even the impact of control measures such as labour inspections depends on workers' valuation of the benefits being enforced. For example, in Brazil, there is evidence that stricter enforcement leads to increased formal sector employment and reduced informal sector employment is more likely as labour inspectors enforce compliance with regulations highly valued by workers. The ILO advises therefore a combination of integrated strategies for formalising informal work (Figure 7).

FIGURE 7 DECENT WORK STRATEGIES FOR THE INFORMAL ECONOMY



OECD in turn proposes a typology of measures combining deterrence (inspection, sanctions, data exchange), incentives and persuasion measures (Figure 8).

FIGURE 8. TYPOLOGY OF STRATEGIES FOR FORMALISATION



Source: OECD based on Williams (2014)

► **Do employment agencies contribute to formalisation?**

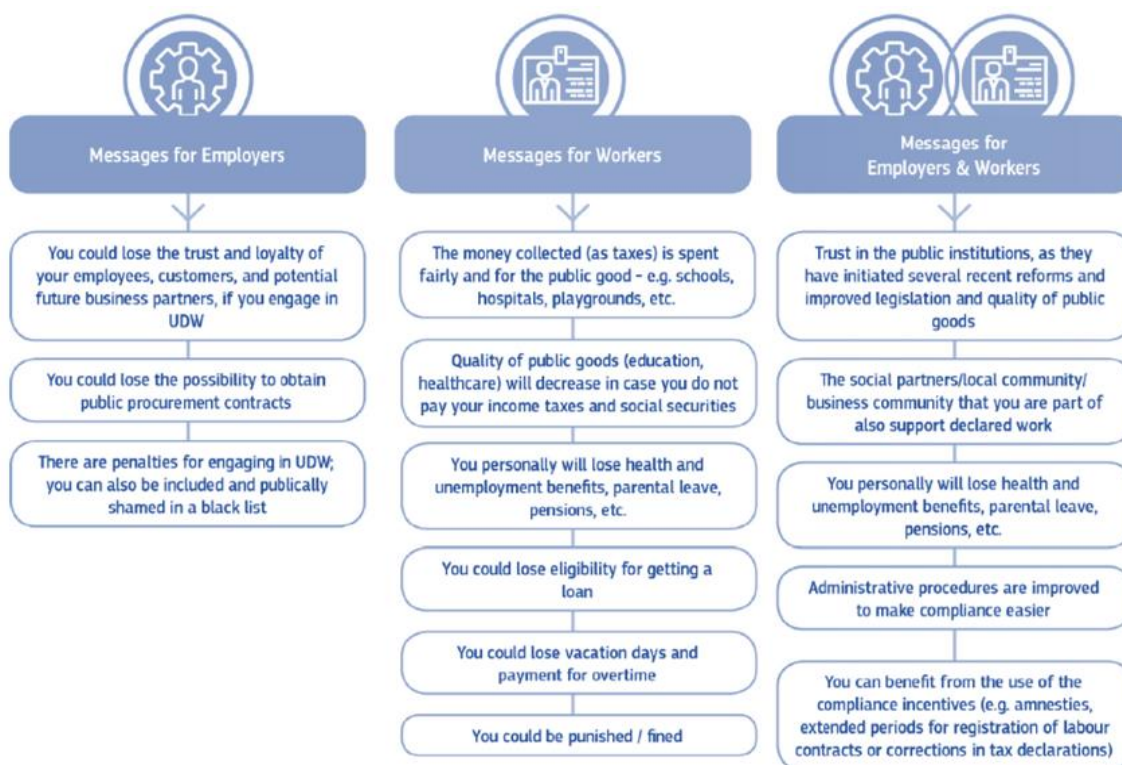
ILO standards on private employment agencies ensure that employment under multiple party employment relationships does not lead to informalisation. When workers are not directly employed by the company to which they provide their services, their employment falls under [contractual arrangements involving multiple parties](#). For example when a worker is deployed and paid by a private employment agency, but the work is performed for the user firm. [Temporary agency work \(TAW\)](#) is a key type of contractual arrangement involving multiple parties. It is characterised by a “triangular” relationship between the worker, the employment agency and a user firm. In some areas, TAW is referred as “labour dispatch” (particularly in Asian countries such as China, Republic of Korea or Japan) or “labour brokerage” (e.g. South Africa) and “labour hire” (e.g. Namibia). Besides TAW, another type of contractual arrangement involving multiple parties is subcontracting.

Subcontracting differs from TAW in that subcontractors in general do not merely hire out workers, but execute work that provides goods or a service. In addition, the subcontractor generally manages their workforce, even if their personnel work at the principal employer’s premises. In practice, however, the difference between subcontracting services and subcontracting workers may be blurred.

Art. 11 of [C181 - Private Employment Agencies Convention, 1997 \(No. 181\)](#) requires members, “*in accordance with national law and practice, to take the necessary measures to ensure adequate protection for the workers employed by private employment agencies as described in Article 1, paragraph 1(b) above, in relation to (a) freedom of association; (b) collective bargaining; (c) minimum wages; (d) working time and other working conditions; (e) statutory social security benefits; (f) access to training; (g) occupational safety and health; (h) compensation in case of occupational accidents or diseases; (i) compensation in case of insolvency and protection of workers claims; (j) maternity protection and benefits, and parental protection and benefits.*”. In practice, the extensive use of unregulated private employment agencies as a way to promote employment is subject of intense debate in Europe and East Asia. In some countries, firms increasingly use agency temporary workers instead of full-time employees to reduce labour costs and to increase staffing flexibility. However, studies have shown that dispatched workers from the temporary service firms suffer from atypical employment patterns that can be characterised by decent work deficits, including lack of social protection (Cooke and Jiang 2017-162).

## **How can communication strategies help reduce work in the informal economy?**

There are different possible communication strategies depending on the characteristics of informal work and occupations or economic sector targeted. Generic persuasion and sensitisation strategies contribute to form a culture of compliance. For example, the European Union implemented a campaign to fight undeclared work from March to October 2020. It included several communication resources, communication channels and a Week of action and outreach in parallel in 27 European countries from 21 to 25 September 2020. The [campaign’s communication toolkit](#) illustrates some of the actions in country and across the EU. It recommends the following campaign messages to different audiences:



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