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## **Informal Sector and Informal Employment: Elements of a Conceptual Framework**

by

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## 1. Introduction

The informal sector is a dynamic segment of the economy and the labour market. In a context of jobless economic growth, recurrent financial crises, economic downturns and highly-skilled labour demands by formal sector enterprises, in many countries around the world the informal sector not only continues to grow, but has also altered its characteristics in order to be able to adapt to changing conditions. In parallel to the transformation processes of the informal sector, there is a trend towards an increasing *informalisation* of the formal sector. One reason is that formal sector enterprises respond to competitive pressure in resorting to mixed-mode labour arrangements in which observance of labour regulations for a number of workers is combined with the use of non-standard, atypical, irregular, precarious, etc. types of labour or various forms of sub-contracting. This process, which is also known as the *informalisation of employment*, is closely associated with the increasing globalisation of the economy. As a result, the boundary between the informal and the formal sector increasingly blurs. It is therefore sometimes argued that the concept of the *informal sector* is no longer valid and that it needs to be replaced by other concepts, such as that of an *informal economy*.

In January 1993, the Fifteenth International Conference of Labour Statisticians (15<sup>th</sup> ICLS) adopted an international statistical definition of the informal sector, which was to be included subsequently in the revised international System of National Accounts (SNA 1993). Inclusion in the SNA of the informal sector definition was considered essential as it would open the way for identifying the informal sector separately in the accounts and, hence, for quantifying the contribution of the informal sector to the national economies. In order to obtain an internationally agreed definition of the informal sector, that was acceptable to labour statisticians as well as national accountants, the definition had to be enterprise-based. Accordingly, the informal sector was defined in terms of characteristics of the production units (enterprises) in which the activities take place (enterprise approach), rather than in terms of the characteristics of the persons involved or of their jobs (labour approach).

From the beginning, it had been clear to labour statisticians that an enterprise-based definition of the informal sector, and the data collection methods that follow from it, would not be able to capture all dimensions of the phenomenon. The Meeting of Experts on Labour Statistics, which was held in preparation of the 15<sup>th</sup> ICLS, already recognised in 1992 that in some countries there had been a sharp rise in various forms of *non-standard employment*, including small jobs, casual work, precarious employment, unpaid family work, piece-rated work and outwork. It was pointed out that this increase was closely related with that of the informal sector, and that the two should be analysed in conjunction. The Meeting agreed that the appropriate approach would be a cross-classification of workers in the informal sector and other sectors by their status in employment, at a sufficient level of disaggregation so that particular types of non-standard employment could be identified (*ILO, 1992, paragraph 24*).

As work on the revision of the International Classification of Status in Employment (ICSE) was done by the 15<sup>th</sup> ICLS in parallel with the adoption of the Resolution concerning statistics of employment in the informal sector, the Resolution

limited itself to defining the informal sector in terms of characteristics of enterprises. The revision of ICSE was hoped to provide sub-categories of status in employment that were sufficiently detailed to make it possible to identify informal jobs. However, these expectations remained unmet as the 15<sup>th</sup> ICLS was unable to define an internationally agreed set of sub-categories of ICSE.

Since then, proposals to complement the enterprise-based concept of the informal sector with a wider, labour-based concept of informal employment have been made repeatedly. Examples are provided by *Pok, 1992* and *Unni, 2000*. Other proposals were based on less rigorous approaches, not making a distinction between the two concepts and thus risking to >mix apples with oranges=.

The purpose of the paper is to present elements of a conceptual framework that would make it possible to complement statistical measures of the informal sector, or of employment in the informal sector, with statistical measures of informal employment. Both types of measures are useful for analytical purposes, as they refer to different dimensions of informalisation. One of the two concepts cannot replace the other. However, the two concepts need to be defined in such a way that one can be clearly distinguished from the other. Statistics= users often tend to confuse the two concepts because they are unaware of the different observation units involved (enterprises vs. jobs). It may well be that a lack of understanding of the difference between the two concepts is at the origin of some of the reservations expressed against the use of the Ainformal sector@ concept.

In using the terms Ainformal sector@ and Ainformal employment@, the paper tries to call things by their names. It does not resort to the use of an aggregate term such as Ainformal economy@. The term Ainformal economy@ does not seem to be particularly useful for statistical purposes, as it is vague and likely to be confused with terms such as Anon-observed economy@, Aunderground economy@, or Aillegal production@.

The paper is based on work which the author carried out as a member of the Informal Sector Task Force (ISTF) of the ILO. The ISTF comprises senior staff of various parts of the ILO headquarters dealing with the informal sector; it was established for the preparation of a comprehensive report on the informal economy, which the Director-General of the ILO will submit to the 90<sup>th</sup> Session of the International Labour Conference (*ILO, 2002*). The Session will be held in June 2002, i.e. 30 years after the ILO employment mission to Kenya which marked the first appearance of the term Ainformal sector@ in an official document. The author wishes to thank other members of the ISTF for their valuable contributions and comments.

## **2. Conceptual framework**

The proposed conceptual framework for measurement of employment in the informal sector and of informal employment is shown in the matrix attached as Annex 1 to this paper. The matrix shows the relations between the concept of employment in the informal sector (defined in terms of characteristics of enterprises) and the concept of informal employment (defined in terms of characteristics of jobs). Enterprises and

jobs are the observation units that are relevant in this context. They stand for two different dimensions of analysis of the phenomenon, which complement each other rather than being alternatives. This is because employed persons hold jobs that can be described by various job-related characteristics, and these jobs are undertaken in enterprises (production units) that can be described by various enterprise-related characteristics. Due to the existence of multiple job-holding, jobs rather than employed persons (workers) were chosen as the observation units for employment. (Note that a person can simultaneously have a formal job plus one or more informal jobs). Employment is defined according to the Resolution concerning statistics of the economically active population, employment, unemployment and underemployment adopted by the 13<sup>th</sup> ICLS in 1982 (*ILO, 2000c*). The matrix provides a comprehensive framework which makes it possible to disaggregate total employment according to two different dimensions: sector of employment (matrix rows), and type of job (matrix columns). Sector of employment is defined in terms of legal organisation and other enterprise-related characteristics, while type of job is defined in terms of status in employment and other job-related characteristics.

Matrix cells shaded in black refer to jobs which, according to the proposed conceptual framework, by definition do not exist in the sector in question. For example, it follows from the definitions specified in the SNA 1993 that own-account workers, employers and contributing family workers cannot be employed in enterprises other than private unincorporated enterprises. Similarly, since formally established producers=co-operatives are incorporated enterprises, there cannot be members of such co-operatives in private unincorporated enterprises. By contrast, employees can be employed in any type of enterprise.

Matrix cells shaded in grey refer to jobs which are found in the sector in question, but which are not relevant in the present context. Examples are own-account workers and employers owning formal sector enterprises, employees with formal jobs in formal sector enterprises, and members of formally established producers=co-operatives.

The remaining, unshaded matrix cells refer to groups of jobs which represent different segments of employment in the informal sector and/or informal employment and, hence, require different research orientations and policy actions. Indeed, each of these cells can be further disaggregated to identify specific types of jobs as targets for analysis and policy-making.

According to the SNA 1993, an enterprise is defined as an institutional unit engaged in the production of goods or services. In the rows of the matrix, a distinction is made between private unincorporated enterprises and other enterprises (corporations including quasi-corporate enterprises, unincorporated enterprises owned by government units, and non-profit institutions). Private unincorporated enterprises are unincorporated enterprises owned by households, as defined by the SNA 1993 (*Inter-Secretariat Working Group on National Accounts, 1993*). They include unincorporated enterprises owned and operated by individual household members or by several members of the same household, as well as unincorporated partnerships and co-operatives formed by members of different households, if they lack complete sets of accounts. Regarding the production units in question, the term *Aenterprise@* is

used in a broad sense. It covers not only production units which employ hired labour, but also production units that are owned and operated by single individuals working on own account as self-employed persons, either alone or with the help of unpaid family members. The activities may be undertaken inside or outside the enterprise owner=s home, and they may be carried out in identifiable premises or without fixed location. Accordingly, independent street vendors, taxi drivers, home-based workers, etc. are all to be considered enterprises. The SNA 1993 includes among private unincorporated enterprises not only unincorporated enterprises created by households for the purpose of producing goods or services for sale or barter to others, but also households producing goods for their own final use and households employing paid domestic employees.

The informal sector is defined as a sub-set of private unincorporated enterprises, in using the criteria specified in the resolution adopted by the 15<sup>th</sup> ICLS (*ILO, 2000b*). These are: (a) legal organisation: unincorporated enterprises; (b) enterprise ownership: households; (c) type of accounts: no complete sets of accounts; (d) product destination: at least some market output; (e) number of persons engaged/employees/employees employed on a continuous basis, and/or non-registration of the enterprises, and/or non-registration of the employees of the enterprises; and (f) kind of economic activity (optional): possible exclusion of agricultural and related activities and of paid domestic services.

The dividing line between the informal sector and other sectors is a dotted one in the matrix, indicating that any such distinction is a convention used to group enterprises (which in reality represent a continuum) into categories for the purpose of describing domains that make it possible to focus research and policy. This is similar to the way in which conventions are used to distinguish, for example, urban and rural localities, young and old persons, etc. In terms of national accounting, a sector groups together similar kinds of enterprises, i.e. enterprises which, in terms of their economic objectives, functions and behaviour, have certain characteristics in common. In a statistical sense, it is thus correct to call the informal sector, as defined by the 15<sup>th</sup> ICLS, a Sector@. As indicated in the matrix, use of the term Sector@ does however not imply that there is a dichotomy of the informal vs. formal sector. Nor does it imply that the informal sector is a homogeneous set of enterprises. Indeed, for purposes of analysis and policy-making it may be useful to divide the informal sector into more homogeneous sub-sectors.

In the columns of the matrix, jobs are distinguished according to status-in-employment categories and, within each category, according to their informal vs. formal nature. The status-in-employment categories correspond to the five substantive ICSE-93 groups: own-account workers, employers, contributing family workers, employees, and members of producers= co-operatives (*ILO, 2000a*). Own-account workers have been sub-divided into producers for own final use only (non-market producers), and producers for sale or barter (market producers).

Being a matter of convention, the distinction between informal jobs and formal jobs is represented by dotted lines. For the time being, there are no internationally agreed guidelines regarding the definition of informal jobs. As a basis for discussion, the following treatment is proposed.

(i) *Own-account workers producing goods for own final use by their household*: Households exclusively engaged in the production of goods for own final use by their household (e.g., subsistence farmers, households engaged in the do-it-yourself construction of their own dwellings) were excluded from the definition of the informal sector adopted by the 15<sup>th</sup> ICLS (*ILO, 2000b*). It is proposed, however, to consider the persons involved in such activities as having informal jobs (matrix cell 6).

Remarks: The production boundary specified by the SNA 1993 includes the production of goods for own final use.

The Resolution concerning statistics of the economically active population, employment, unemployment and underemployment adopted by the 13<sup>th</sup> ICLS in October 1982 extends the concept of employment to all activities included in the SNA production boundary.

Production of goods for own final use can hardly be considered a formal job.

(ii) *Own-account workers producing goods or services for sale or barter; employers*: The situation of an own-account worker producing for the market or of an employer cannot be separated from the characteristics of the enterprise that he or she owns. For this reason, own-account workers producing for the market and employers are considered to have an informal job if their enterprise is an informal sector enterprise (matrix cells 1 and 2).

(iii) *Contributing family workers*: Since contributing family workers usually do not have an explicit, written employment contract and their employment is not subject to labour legislation, social security regulations, collective agreements, etc., all contributing family workers are considered to have informal jobs, irrespective of the characteristics of the enterprise for which they work (matrix cells 3 and 7). (Note that family workers holding an employment contract and/or receiving a wage for the work done are to be considered employees.)

(iv) *Employees*: Employees are considered to have informal jobs if their employment relationship is not subject to standard labour legislation, taxation, social protection or entitlement to certain employment benefits (e.g., advance notice of dismissal, severance pay, paid annual or sick leave, etc.) for reasons such as: the employee or his/her job are undeclared; the job is casual or of a limited short duration; the hours of work or wage are below a certain threshold; the employer is an unregistered enterprise or a person in a household; or the employee's place of work is outside the premises of the employer's or customer's enterprise. Employees with informal jobs can be employed in informal sector and other enterprises (matrix cells 4 and 8).

Remarks: The above definition of informal employee jobs relates effects to their causes. It covers employees such as: illegal or clandestine workers; persons engaged in casual or odd jobs; employees without employment contracts or with short-term contracts; paid domestic employees; employee outworkers (homeworkers);

and fictitiously self-employed persons (unless they are classified as own-account workers).

The definition corresponds to the definition of unregistered employees as specified in paragraph 9 (6) of the informal sector resolution adopted by the 15<sup>th</sup> ICLS (*ILO, 2000b*). It encompasses the ICSE-93 definitions of non-regular employees, workers in precarious employment (casual workers, short-term workers, seasonal workers, etc.), and contractors (*ILO, 2000a*).

Labour force surveys appear to be the most appropriate survey instrument for applying the definition. However, the operational criteria of the definition, as well as the relevant sub-categories of informal employee jobs, will have to be specified in accordance with national circumstances. In order to define informal employment in operational terms, some countries have used the following criteria: lack of coverage by the social security system, or lack of entitlement to paid annual or sick leave.

Depending upon the national definition of the informal sector (e.g., when the informal sector is defined only in terms of the size of the enterprise) or due to lack of an administrative link between the registration of employees and the registration of their employers, there may be cases of employees working in informal sector enterprises and having formal jobs (matrix cell 5). In most circumstances, however, the number of such employees is likely to be small. Where the number is significant, it may be useful to define the informal sector in such a way that enterprises employing formal employees are excluded. Such a definition has been proposed, for example, for Argentina (*Pok, 1992*) and is in line with paragraph 9 (2) of the 15<sup>th</sup> ICLS resolution, which includes the non-registration of the employees of the enterprise among the criteria for defining enterprises of informal employers (*ILO, 2000b*).

(v) *Members of producers= co-operatives*: Producers= co-operatives, which are formally established as legal entities, are incorporated enterprises and, hence, part of the formal sector. Members of such formally established producers= co-operatives are considered to have formal jobs. Producers= co-operatives, which are not formally established as legal entities, are treated as private unincorporated enterprises owned by members of several households. Persons working in such informal co-operatives are included in one of the other status-in-employment categories, and their jobs classified accordingly.

(vi) *Paid domestic employees* will be included in matrix cells 4 or 5, if the households employing them are included in the national definition of the informal sector. Otherwise, paid domestic employees may be included in matrix cell 8, depending upon their conditions of employment and work.

(vii) *Outworkers (homeworkers)* are included in matrix cells 1 or 2, if they constitute enterprises of their own as self-employed persons, and if these enterprises meet the criteria of the informal sector definition. Persons working for such informal outworking enterprises as contributing family workers are included in matrix cell 3, and persons working for them as employees are included in matrix cells 4 or 5. Outworkers (homeworkers) working as employees for formal sector enterprises are

included in matrix cell 8, if they have informal jobs. Thus, all outworkers (homeworkers) are captured by the proposed framework.

*Employment in the informal sector* is represented by the sum of matrix cells 1-5. It comprises all persons who, during a given reference period, were employed in at least one informal sector enterprise, irrespective of their status in employment and whether it was their main or a secondary job.

*Informal employment* is represented by matrix cells 1-4 and 6-8. It refers to the total number of informal jobs, or the total number of persons engaged in informal jobs, during a given reference period. In other words, informal employment comprises employment in the informal sector (minus formal jobs of employees in informal sector enterprises, if relevant), plus jobs of contributing family workers and informal jobs of employees in other sectors, plus the activities of persons engaged in the own-account production of goods for own final use by their household. If necessary, the sum of matrix cells 6-8 may be called *informal employment outside the informal sector*.

### 3. Points for discussion

Participants of the workshop may wish to discuss the following questions:

- (4) Is it useful to complement the definition and measurement of employment in the informal sector with the definition and measurement of informal employment, and is the time ripe for doing so?
- (5) If yes, are the basis and logic of the conceptual framework outlined in the present paper acceptable?
- (6) Is there agreement with the proposed classification of informal vs. formal jobs of own-account workers, employers, contributing family workers, and members of producers= co-operatives?
- (7) Is there agreement with the proposed definition of informal jobs of employees? Is the definition complete? If no, how can it be refined? Which operational criteria can be used to apply the definition (e.g., in labour force surveys)? Which are the most relevant sub-categories of informal employee jobs?
- (8) Is the possible existence of informal sector employees with formal jobs (matrix cell 5) considered to be a problem? If yes, how should the problem be solved?
- (f) Are participants of the workshop willing to test the proposed framework in their countries, in completing the table attached as Annex 2 to this paper? Are data available in their countries that would make it possible to disaggregate the table by sex and by other characteristics of employed persons (e.g., age groups, educational level)?

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