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Item 5 of the provisional agenda

THE INFORMAL SECTOR:

AN ANNOTATED OUTLINE FOR NEW TEXT IN THE 1993 SNA, REV.1<sup>1</sup>

Submitted by UNSD

The meeting is organised jointly with Eurostat and OECD

**EXECUTIVE SUMMARY**

1. The ISWGNA concluded that a chapter should be devoted to an expanded discussion of the informal sector in the *1993 SNA, Rev. 1*. The following document presents an annotated outline of what might be included in such a chapter.

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<sup>1</sup> This paper has been prepared by Ivo Havinga (UNSD) and Carol Carson (Project Manager of the SNA Update) for the Fourth Meeting of the Advisory Expert Group on National Accounts, 30 January-8 February 2006, Frankfurt and is subject to possible changes following the discussion at the meeting. The views expressed in this paper are those of the authors and should not be attributed to the United Nations. Vu Viet collaborated in the preparation of the series of papers presented by UNSD during 2005. The authors benefited from the comments and assistance of Ralf Hussmanns of ILO.

2. The draft annotated outline is meant to indicate the topics that might be covered and something about the material that might be brought in. The outline does not aim at originality; it draws liberally on existing material. It is meant as a point of departure for discussion at the AEG, and then with the AEG's comments, to be discussed with the Delhi Group and the ILO.

*Annotations are in square brackets*

I. Introduction [The Editor proposes that each chapter begin with an "introduction," meant to provide an overview of the chapter. This outline proposes topics that might be considered in the spirit of such an overview.]

A. The purpose of this chapter is to cover topics that will be useful to national accountants in preparing statistics about a subset of economic activities that are a significant part of the economy in many countries and are highly relevant for policy analysis and formulation.

B. The *1993 SNA* introduces the definition of the informal sector that, just months before that volume's completion, had been agreed by the International Conference of Labour Statisticians. The research agenda (*1993 SNA*, page xliii) noted that the distinction between informal and formal activities is widely recognized as useful and identified further collaboration with the ILO, which is the lead agency for this work, as an area of further research.

C. This chapter is organized as follows. [Sketch main headings.] Throughout, in recognition that there are players from several different fields involved in statistics of the informal sector, it attempts to trace history, note conceptual as well as practical considerations, and compare and contrast as a way to build bridges among them.

II. The informal sector: a broad statistical perspective

A. The words "informal" and "sector" have several meanings, and this has sometimes lead to confusion, tension and misunderstanding.

1. Informal: As descriptive of the sector, the term refers to such as (1) units that are unregistered and unrecorded in official statistics and (2) activities that are undertaken within a very small and with very low level of organization.

2. Sector: The term came into use in the 1970's outside national accounts and became very popular. The term was carried over to national accounts even when it did not quite fit with the strict meaning of institutional sector in the *SNA*.

B. The informal sector, it is generally agreed, can be described in terms of the units involved. [The paragraphs that follow are from the resolution of the 15<sup>th</sup> ICLS, paragraphs 5.1 - 5.3. They were quoted in the *1993 SNA* and still remain valid.]

5. (1) The informal sector may be broadly characterized as consisting of units engaged in the production of goods or services with the primary objective of generating employment and incomes to the persons concerned. These units typically operate at a low level of organisation, with little or no division between labour and capital as factors of production and on a small scale. Labour relations -where they exist - are based mostly on casual employment, kinship or

personal and social relations rather than contractual arrangements with formal guarantees.

(2) Production units of the informal sector have the characteristic features of household enterprises. The fixed and other assets used do not belong to the production units as such but to their owners. The units as such cannot engage in transactions or enter into contracts with other units, nor incur liabilities, on their own behalf. The owners have to raise the necessary finance at their own risk and are personally liable, without limit, for any debts or obligations incurred in the production process. Expenditure for production is often indistinguishable from household expenditure. Similarly, capital goods such as buildings or vehicles may be used indistinguishably for business and household purposes.

(3) Activities performed by production units of the informal sector are not necessarily performed with the deliberate intention of evading the payment of taxes or social security contributions, or infringing labour or other legislations or administrative provisions. Accordingly, the concept of informal sector activities should be distinguished from the concept of activities of the hidden or underground economy.

C. The informal sector manifests itself in different ways in different countries, in different regions within the same country, and even within smaller geographical areas. It encompasses different kinds of activities and different types of enterprises, and it stems from different motives. (Real world examples, such as cited in Hussmanns, in volume 1 of *Household Accounting Experience in Concepts and Compilation*.)

D. The informal sector presents statistical challenges.

1. Size: The informal sector represents a substantial portion of economic activity, especially in developing and transition countries. [Cite recent estimates, such as those in table 2.8 of *Women and Men in the Informal Economy: A Statistical Picture*.]
2. Growth and change: The informal sector has not only grown in recent decades, but has emerged in new guises and unexpected places in the wake of industrial restructuring, globalization, and financial crises. [Examples, such from the UNECE's *Non-Observed Economy in National Accounts: Survey of Practices*.]
3. Units: The units engaged in informal activities do not lend themselves easily to measurement: small size and large number of units, mobility of the units, turnover, seasonality, and scant record keeping. Important progress has been made in recent years in modifying traditional survey techniques and development of new methods (see section V).

E. The informal sector is of high policy interest in many parts of the world.

1. The informal sector is linked directly or indirectly to the main development objectives of increased production, job creation, and reduction of poverty. [Elaborate.]
2. The informal sector's characteristics are key factors in designing and monitoring specific support and assistance programs. [Examples.]

### III. Definition of the informal sector

A. At several points in the 1980s and early 1990s, researchers attempted to develop criteria to distinguish between formal activities and informal (or traditional/unorganized,

as they were sometimes called) activities. As well, some practical uses were made of the concept (such as the survey of country practices in estimating hidden and informal activities for national accounts made in 1991 by the UNECE).

B. The 15<sup>th</sup> International Conference of Labour Statisticians (ICLS), in January 1993, approved a resolution that provided a standard international definition of the informal sector. [This section, specifically points 2 and 3, draws heavily on *Measuring the Non-observed Economy: A Handbook*.]

1. Context: The resolution describes the informal sector in broad terms and provided the framework within which countries could formulate their own operational definitions (*Measuring the Non-observed Economy: A Handbook*).
2. Starting point: Informal sector is restricted to activities included in the SNA production boundary.
3. Core definition in terms of enterprises: The informal sector encompasses household unincorporated enterprises that are ...
  - a. Informal own-account enterprises (optionally, all or those that are not registered under specific forms of national legislation)
  - b. Enterprises of informal employers (optionally all those with less than a specified level of employment and/or not registered and/or employees not registered)
4. Additional provisions: The Resolution included recommendations regarding the scope of surveys and treatment of borderline cases.
  - a. Household unincorporated enterprises that are engaged exclusively in own-account production are excluded from the informal sector.
  - b. For practical reasons, agricultural production and related activities are excluded from the scope of informal sector surveys (it is recommended that they are measured separately).
  - c. For practical reasons, countries were given the option of collecting data on only on urban areas, leaving rural areas for later development.
  - d. Professional and technical services should be included or excluded in the informal sector on the same basis as other enterprises.
  - e. Outworkers should be included in the informal sector if the production units which they constitute as self-employed persons or for which they work as employees meet the enterprise-based criteria.
  - f. Paid domestic workers could be included or not as a country determination, but if included they should be separately identified to enhance international comparability. (See III.D.2 below.)

C. To build on this work, an Expert Group on Informal Sector Statistics, was set up as a “city group” under the auspices of the United Nations Statistical Commission in 1997. This group, the Delhi Group, exchanges experience in the measurement of the informal sector, documents the data-collection practices, including definitions and survey methodologies followed by member countries, and recommends measures for improving the quality and comparability of informal sector statistics. [Examples of work particularly relevant to national accountants, such as on methodology to estimate the contribution of the informal sector to GDP.]

D. Subsequent developments in ILO’s work: The 17<sup>th</sup> ISLS clarified the concept of

informal employment within the framework of the informal economy, complementing the concept of employment in the informal sector.

1. A matrix that delineates the informal economy: This matrix, organized around production units by type and jobs by employment status, is useful in identifying segments of the labor-employing economy. [See the addendum to this outline.]
2. One specific change to the scope of the informal sector as outlined by the 15th ICLS: paid domestic workers. Households employing domestic workers to produce services for own consumption were excluded from informal sector enterprises (on recommendation of the Delhi Group).

E. In the section on “The household sector and its subsectors,” the *1993 SNA* noted that for some countries it is important to be able to distinguish between the informal and formal sectors of the economy.

1. The text (paragraph 4.159) referred to the resolution of the 15<sup>th</sup> ICLS as providing an international statistical standard definition of the informal sector and an Annex reproduced an extract of the 15<sup>th</sup> ICLS resolution.
2. The brevity of the text may have led to misunderstandings. [Elaborate if further work indicates that it would be helpful.]
3. Table/set of bullets [to be developed] identifies the features of the definition and provides some commentary, including relevant comparison and contrast with counterpart SNA terminology.

F. For the *Rev. I.*, ...[this section would cover whatever clarifications, re-emphases, updating (e.g., about paid domestic workers), or proposals for change or supplementary delineations—for example, a minimum coverage for international comparability—comes out of the Update.]

IV. Other concepts. The concept of informal sector production should be distinguished from some other concepts with which it is sometimes confused. [This section would draw heavily on the *Handbook on the Non-Observed Economy*. ]

A. Illegal production: Illegal production comprises the production of goods and services whose sale, distribution or possession is forbidden by law, and production activities that are usually legal but become illegal when carried out by unauthorized producers. The vast majority of informal sector activities provide good and services whose production and distribution are legal. Examples.

B. Underground production: Underground production consists of activities that are productive in the economic sense and quite legal, but that are deliberately concealed from public authorities for reasons such as avoiding paying taxes. Informal sector activities are not necessarily performed with the deliberate intention of evading taxes or social security contributions, or infringing labour legislation...Examples. In summary, although informal sector production and underground activities may overlap, the concepts need to be clearly separated.

C. Production for own final use: see section III.E.3.

D. Non-observed production: Non-observed production includes informal production, illegal production, underground production, production for own final use, and production missed due to deficiencies in statistical programs.

E. Informal economy: This ILO-defined concept comprises the informal economy and informal employment outside the informal sector.

## V. Measurement

A. Measurement of the activities of the informal sector are of interest in their own right as well as providing a contribution to achieving exhaustive measures of GDP and other main aggregates.

B. Several approaches may be used to record activity in the informal sector. The choice or combination will depend on the objectives. [This section would draw heavily on the *Measuring the Non-Observed economy: A Handbook*.]

1. Labour force surveys
2. Household income and expenditure surveys
3. Informal sector enterprise surveys
4. Informal sector mixed household-enterprise surveys

C. In recent years, a number of countries have undertaken substantial efforts to collect information on the informal sector. In a number of cases, they introduced innovative techniques. Several of the efforts, some highlighting the informal sector mixed household-enterprise surveys, may be sketched. [Thumbnails sketches of, for example, efforts in India, Kenya, Mexico, South Africa, or Tunisia, drawing on the ILO's *Women and Men in the Informal Economy: A Statistical Picture*.]

D. Further development of macroeconomic estimates and indicators of the contribution of the informal sector enterprises (and other household producers) to GDP and employment in the framework of the SNA could be built on several strands of work.

1. Segmentation of the household enterprises could be further explored and then further applied.
2. Guidance on the use of informal sector data by national accountants would help populate conceptual frameworks. [Draw on the chapter to be in the manual on *Surveys of Informal Sector and Informal Employment*.]

Methodologies are being tested. [Draw on Delhi Group papers, for example from India and Namibia.]

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