6 Extending social protection to informal workers

Using the OECD Key Indicators of Informality based on Individuals and their Household (KIIbIH) database, the OECD Global Revenue Statistics Database, and new evidence from Women in Informal Employment: Globalizing and Organizing (WIEGO) and the International Labour Organization (ILO) on global experiences in extending social insurance to informal workers, this chapter reviews the current de facto social protection coverage for informal workers across developing and emerging economies. It explores individual and household characteristics of informal workers to identify policy options for extending social protection to informal workers; and discusses possible methods of, and constraints to, financing the extension of social protection.

Overview of current coverage of social protection schemes

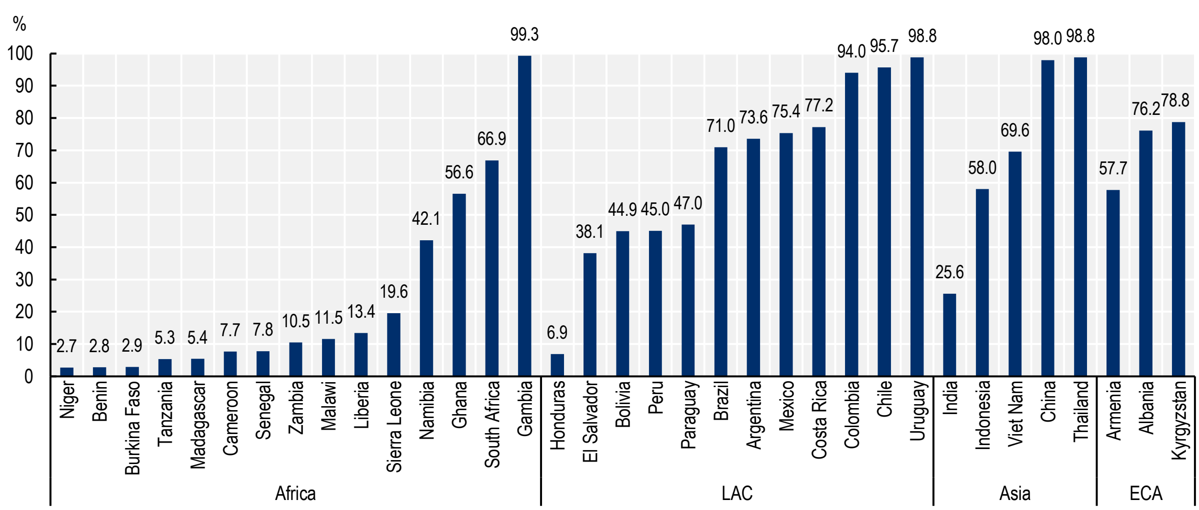
Universal social protection constitutes an essential component of the global agenda for sustainable development and is one of the key policy priorities in several regional and national commitments. Yet, the road to universal social protection remains difficult in many countries. One common challenge in most developing and emerging economies with a large informal economy is to remove the many legal, economic and institutional constraints that informal workers face in accessing social protection and to install funding mechanisms that are appropriate, fair, efficient and sustainable.

Throughout the world, social protection coverage for workers is often inconsistent and sparse

Evidence from KIIbIH data indicates that social protection coverage for workers is limited in most developing and emerging economies, although significant differences can be found across countries. The percentage of workers who benefit from social protection, either directly or indirectly through a household member, is lowest in countries in Africa and relatively higher in countries in Latin America and the Caribbean (LAC), Europe and Central Asia (ECA) and Asia (Figure 6.1).

Figure 6.1. Social protection of workers lags in some parts of the world

Percentage of workers receiving at least one form of social protection



Note: Social protection programmes include contributory pensions, employment-based health insurance, unemployment insurance, programmes providing universal health coverage and/or unconditional/conditional cash transfers (including non-contributory pensions). Coverage rates are calculated for direct and indirect beneficiaries of social protection programmes and contributors to social insurance programmes. Surveys for some countries do not include specific questions on all of these programmes, and this can affect cross-country comparisons. It is important to note that coverage rates provided here for any particular country are only estimated to the best extent possible given data quality and are not necessarily indicative of adequate targeting or adequate benefit levels. In many of the countries discussed here, social protection coverage refers to whether an individual is a direct beneficiary or a contributor to or indirect beneficiary of at least one social protection programme within the past month or past year. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia. Bolivia refers to the Plurinational State of Bolivia (hereafter: Bolivia); China refers to People's Republic of China (hereafter: China).
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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African countries have relatively fewer resources to sustain social protection systems, and programme coverage is therefore lowest on this continent. In the ECA sample of countries included in the KIIbIH database, some form of social protection, such as mandatory privately funded pensions, is found in all countries. In many parts of Asia, social protection coverage is low, but countries provide a large mix of programmes, which results in high coverage estimates (see note below Figure 6.1). In LAC, social protection systems are generally well funded with a variety of programmes, ranging from insurance and cash transfers to other forms of protection.

Box 6.1. Social protection coverage in the KIIbIH database

The KIIbIH database is a new OECD database that provides information on informal workers and their households in developing and emerging economies (OECD, 2021[1]). Building on household surveys, the KIIbIH database provides comparable indicators and harmonised data on informal employment, and the well-being of informal workers and their dependents. It currently covers 42 countries across North and sub-Saharan Africa, ECA, Asia and LAC. However, the sub-set of KIIbIH countries included in this chapter covers only 15 African countries, 12 LAC countries, 5 Asian countries, and 3 ECA countries for which sufficient information on social protection is available.

The definition of informal employment used by the KIIbIH database is the same definition currently used by the ILO, following standards agreed at the 15th and 17th International Conference of Labour Statisticians (ICLS): employees are informal when they are not affiliated with social security (such as a pension fund, unemployment benefit or health insurance), and do not benefit from some type of pension, paid leave or paid sick leave from their job; and employers and own-account workers are informal when they belong to the informal sector, which is defined as a group of production units composed of unincorporated enterprises owned by households, including informal own-account enterprises and enterprises of informal employers (typically small and non-registered enterprises). Contributing family workers are always considered informal.

Based on the information available and the nature of the underlying data, the definition of social protection coverage in this chapter includes contributory pensions, employment-based health insurance, programmes providing universal health coverage, unemployment insurance and/or unconditional/conditional cash transfers. Coverage is based on reported direct beneficiaries of social protection programmes or contributors to contributory schemes and indirect beneficiaries.

Social protection is then further divided into two sub-categories:

- Contributory social protection constitutes voluntary or mandatory contributory (usually employment-based) pensions, employment-based health insurance and unemployment insurance.
- Non-contributory social protection constitutes unconditional and conditional cash transfers, including non-contributory pensions.

Source: Authors' compilation.

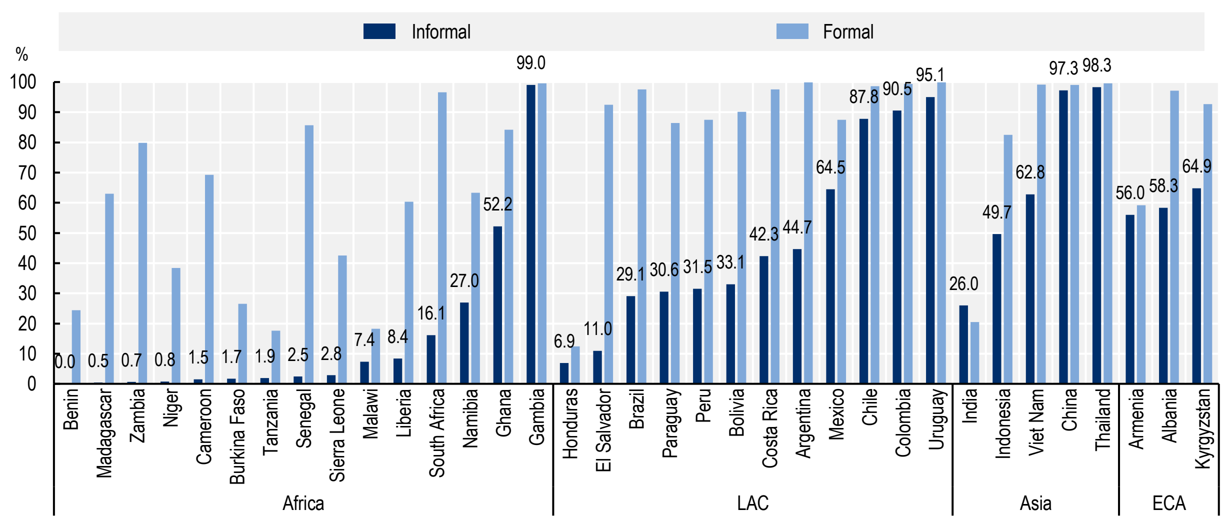
In most countries, informal workers experience a social protection gap

Formal workers are better covered by social protection than informal workers are in most countries, according to KIIbIH estimates. More than 70% of formal workers across the surveyed countries benefit from or contribute to at least one of the following programmes: contributory pension, employment-based health insurance, programmes providing universal health coverage, unemployment insurance or unconditional/conditional cash transfers (hereafter, collectively constituting social protection coverage)

(Figure 6.2). In comparison, only about 37% of informal workers benefit from one of these programmes. There are also large disparities across regions and countries. The coverage gap of informal workers is particularly significant among the sample of African countries, and is less pronounced in the sample of LAC, Asian, and ECA countries.

Figure 6.2. Informal workers are half as likely as formal workers to be covered by social protection

Percentage of workers contributing to and/or benefitting from at least one form of social protection



Note: Social protection programmes include contributory pensions, employment-based health insurance, unemployment insurance, programmes providing universal health coverage and/or unconditional/conditional cash transfers (including non-contributory pensions). Coverage rates are calculated for direct and indirect beneficiaries of social protection programmes and contributors to social insurance programmes. Surveys for some countries do not include specific questions on all of these programmes, and this can affect cross-country comparisons. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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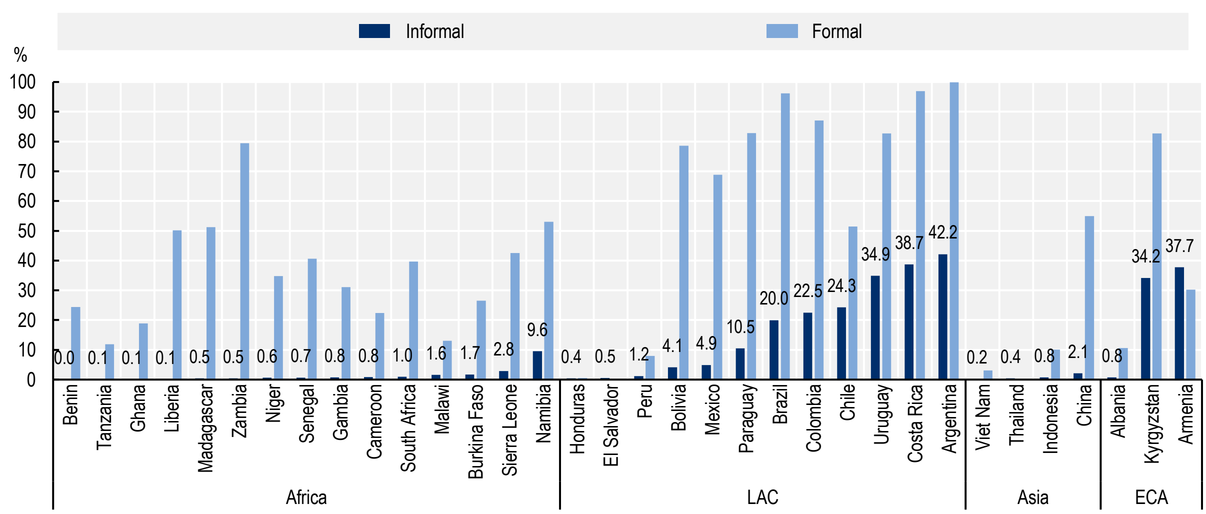
The large social protection gap between formal and informal workers is largely due to a gap in contributory schemes

The large social protection gap between formal and informal workers mirrors, to a large extent, the coverage gap of informal workers with regard to contributory schemes. Formal workers benefit more often from contributory programmes (43.7%) than informal workers do (8.9%) (Figure 6.3). Most contributory schemes are traditionally employment based, and informal workers are usually unable to access them either because they are excluded from the scope of social security or because they are excluded from it in practice, due to the non-payment of contributions and lack of capacity to contribute to them, among other things. Yet, informal workers can (and, as evidenced, do) benefit from some contributory schemes, often on a voluntary basis, thanks to certain programmes[1] that have eased barriers to participation for specific categories of informal workers, such as those who are self-employed.

In contrast, the coverage of non-contributory programmes across workers does not seem to be linked to their formal/informal status. This may reflect the fact that informal workers are more likely to receive lower pay or to live in poorer households, which would make them or their household eligible for means-tested social assistance programmes and are therefore more likely than formal workers to rely on government assistance (non-contributory programmes) to meet basic needs. Yet, the coverage non-contributory programme coverage varies depending on the country. In the sample of African countries, an average of 29.4% of formal workers and 17.2% of informal workers benefitted from non-contributory programmes; in the sample of Asian countries, an average of 62% of formal workers and 66% of informal workers benefitted from non-contributory programmes (Figure 6.4). The sample of countries from LAC is a notable exception, with the average non-contributory programme coverage for informal workers (33.1%) far outstripping the average coverage for formal workers (24.7%), probably reflecting the extension of cash transfers to poor households, which are more likely to be in the informal economy.

Figure 6.3. Formal workers are more likely than informal workers to benefit from contributory schemes

Percentage of informal workers and formal workers contributing to and/or benefitting from contributory social protection



Note: Contributory social protection programmes include contributory pensions, employment-based health insurance and unemployment insurance. Coverage rates are calculated for direct and indirect beneficiaries of social protection programmes and contributors to social insurance programmes. Surveys for some countries do not include specific questions on all of these programmes, and this can affect cross-country comparisons. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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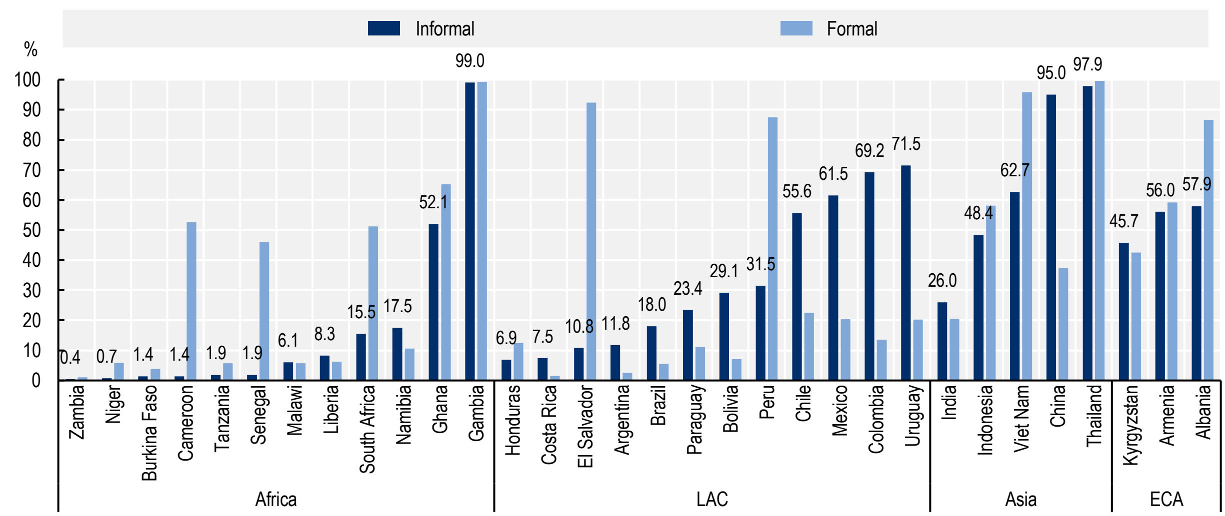
Figure 6.4. Non-contributory programme coverage of workers does not seem to be linked to their formal/informal status

Percentage of informal workers and formal workers covered by non-contributory social protection



Note: Non-contributory social protection programmes include programmes providing universal health coverage and/or unconditional/conditional cash transfers (including non-contributory pensions). Coverage rates are calculated for direct and indirect beneficiaries of social protection programmes and contributors to social insurance programmes. Surveys for some countries do not include specific questions on all of these programmes, and this can affect cross-country comparisons. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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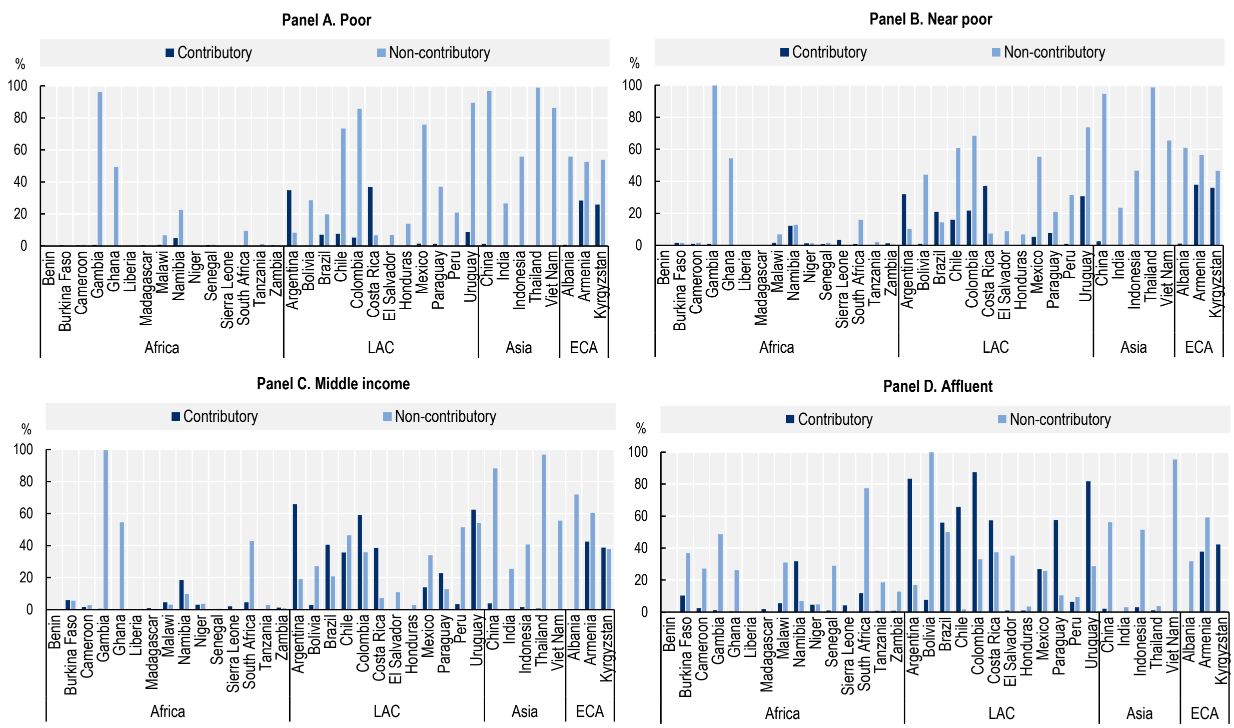
Contributory schemes tend to benefit relatively better-off informal workers, while non-contributory schemes typically benefit poorer informal workers

Social protection coverage tends to vary among the household income classes of informal workers,[2] leaving a large segment of workers belonging to the near poor and middle-income categories largely uncovered. Contributory schemes tend to benefit relatively richer informal workers more than poorer ones, while non-contributory schemes typically benefit poorer informal workers rather than richer ones (Figure 6.5). Overall, in the sample of countries for which data are available, an average of only 5% of poor informal workers are covered by some type of contributory scheme compared with about 20% of more affluent informal workers. Likewise, about 39% of poor informal workers are covered by a non-contributory programme compared with nearly 31% of higher-earning informal workers.

Coverage levels also differ across countries. In the sample of countries from LAC and Asia, non-contributory programmes are targeted at the most vulnerable informal workers, whereas in the sample of African countries, affluent informal workers are more likely to be covered by both contributory and non-contributory schemes.

Figure 6.5. Contributory schemes tend to benefit relatively better-off informal workers, while non-contributory schemes are relatively pro-poor

Percentage of informal workers contributing to and/or benefitting from social protection, by economic class category



Note: Contributory social protection programmes include contributory pensions, employment-based health insurance and unemployment insurance. Non-contributory social protection programmes include programmes providing universal health coverage and/or unconditional/conditional cash transfers (including non-contributory pensions). Coverage rates are calculated for direct and indirect beneficiaries of social protection programmes and contributors to social insurance programmes. Surveys for some countries do not include specific questions on all of these programmes, and this can affect cross-country comparisons. Economic classes are based on four absolute per capita per day welfare thresholds, which differ by per capita household income level. Low-income countries (LICs): poor: international dollar (int'l dollar) 2.15/day or less; near poor: int'l dollar 2.15-4/day; middle: int'l dollar 4-8/day; affluent: int'l dollar 8/day or more. Low- and middle-income countries (LMICs): poor: int'l dollar 3.65/day or less; near poor: 3.65-7/day; middle: int'l dollar 7-20/day; affluent: int'l dollar 20/day or more. Upper middle-income countries (UMICs) and high-income countries (HICs): poor: int'l dollar 6.85/day or less; near poor: int'l dollar 6.85-15/day; middle: int'l dollar 15-70/day; affluent: int'l dollar 70/day or more.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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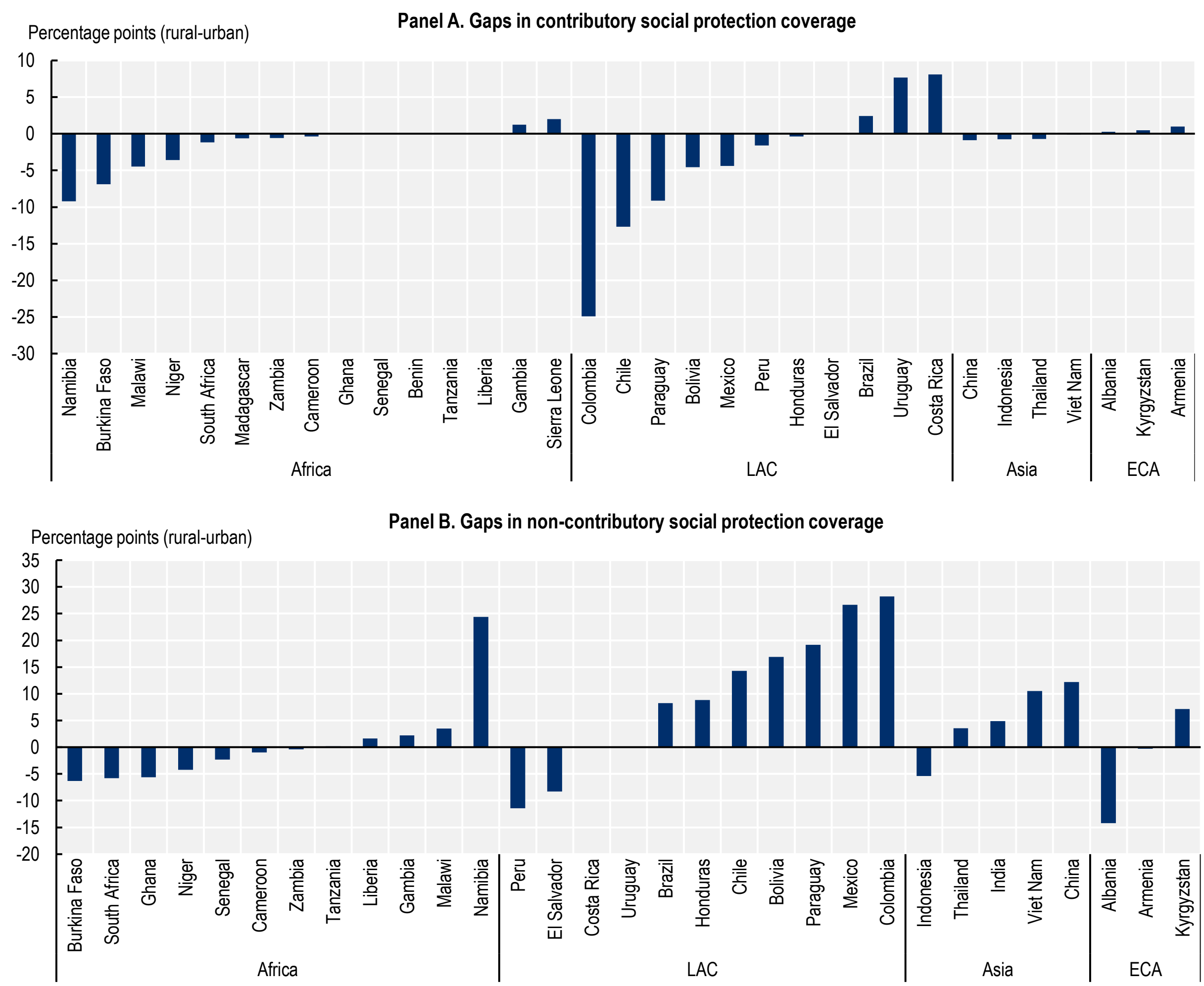
In the majority of the sample countries, urban informal workers have better access to contributory programmes, but rural informal workers are better covered by non-contributory programmes

Informal workers also appear to benefit from different types of social protection when they live in rural rather than urban areas. Urban informal workers have better access to contributory programmes, but rural informal workers are better covered by non-contributory programmes (Figure 6.6). In two-thirds of the countries for which information is available, urban informal workers were more likely than rural informal workers to benefit from contributory programmes (Figure 6.6, Panel A).

In most countries (with the noticeable exception of the sample of African countries), rural informal workers reported better coverage by non-contributory schemes than urban informal workers did (Figure 6.6, Panel B). This is likely due to the long-standing disadvantage of rural areas with regard to access to services, infrastructure and information, and much of the rural labour force is precariously employed in agriculture. Not only is it harder to distribute and manage contributory schemes in rural areas but informing eligible participants about schemes can also be more difficult in rural areas than in urban areas. Cash or in-kind transfers are usually provided in rural areas to help households meet basic needs. This rural-urban difference in the type of social protection coverage may also reflect the higher prevalence of employees in urban areas and self-employed individuals in rural areas.

Figure 6.6. Informal workers benefit from different types of schemes in rural and urban areas

Difference in contributory and non-contributory social protection coverage between informal workers in rural and urban areas



Note: Contributory social protection programmes include contributory pensions, employment-based health insurance and unemployment insurance. Non-contributory social protection programmes include programmes providing universal health coverage and/or unconditional/conditional cash transfers (including non-contributory pensions). Coverage rates are calculated for direct and indirect beneficiaries of social protection programmes and contributors to social insurance programmes. Surveys for some countries do not include specific questions on all of these programmes, and this can affect cross-country comparisons. The difference in coverage rates (measured in percentage points) is determined by subtracting the coverage for urban informal workers from the coverage for rural informal workers. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.

Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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Access to social protection may also be influenced by whether informal workers hold citizenship in the country where they work. Using KIIbIH data, we find a relative disadvantage in accessing social protection between foreign-born informal workers and native-born informal workers. Compared with native-born informal workers, foreign-born informal workers are less likely to benefit from social protection. Such a gap does not seem to reflect a disadvantage in terms of contributory schemes, however. Since few informal workers have access to contributory schemes, the differences in contributory coverage between foreign-born informal and native-born informal workers tend to be small. Rather, the relative overall social protection disadvantage of foreign-born informal workers mirrors a gap in non-contributory schemes, which is particularly visible in countries where access to non-contributory schemes is more important. For instance, in China and Chile, foreign-born informal workers were about half as likely as native-born to benefit from non-contributory programmes.

Extending non-contributory schemes to informal workers

The previous section documented the extensive gaps in social protection for informal workers. Social protection for informal workers will need to be based on a combination of contributory and non-contributory schemes. Country experiences show that very few countries have achieved both universal social protection coverage and adequate benefit levels by offering only one of these types of social protection. Universal social protection will most likely be achieved over time through progressive expansion, even if some countries have been successful in expanding their non-contributory schemes quickly, such as universal pensions or universal health coverage (ILO, 2018[2]).

Non-contributory schemes do not require contributions from individuals who benefit from social protection and are mostly financed directly from a government's general budget – that is, from general taxation, non-tax revenue, or external grants or loans. There are many types of non-contributory programmes, such as universal schemes that benefit all individuals (e.g. a national health service), categorical schemes covering certain broad groups of the population (e.g. social pension or universal child benefit schemes) or social assistance schemes that provide benefits for groups of the population living in poverty (usually based on a means test, a proxy means test or other targeting mechanism).

Non-contributory schemes play a key role in ensuring a basic level of protection within the social protection system for poor and vulnerable groups who do not have access to contributory social protection. Non-contributory schemes are an essential component of any nationally defined social protection floor.

The extension of non-contributory programmes for the poor would cover a large share of informal workers

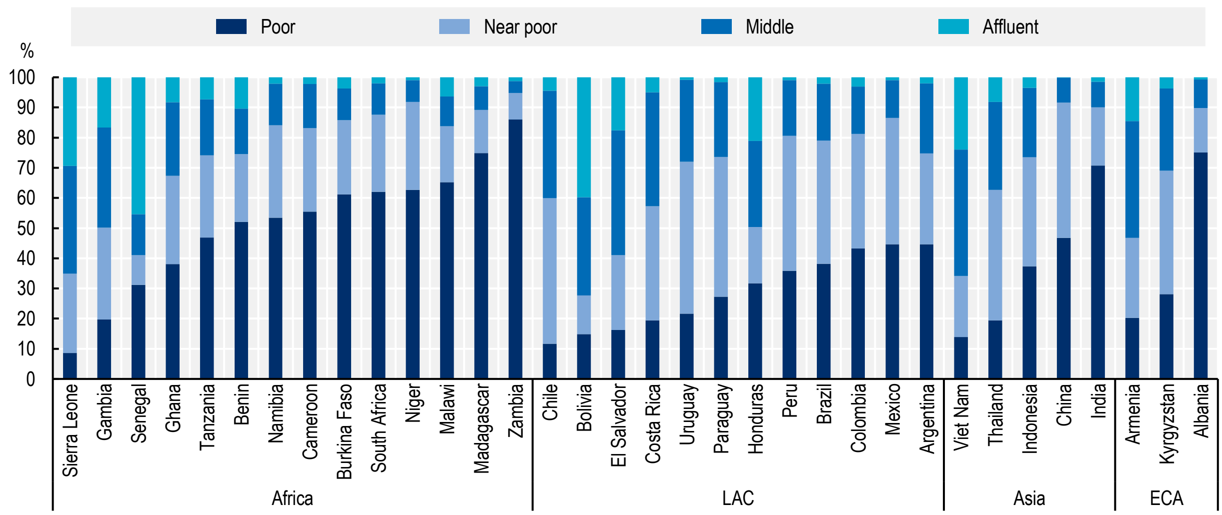
In many countries, reaching a consensus for using non-contributory, tax-financed programmes to reduce the social protection gap for the poor is often possible. It is therefore useful to assess the proportion of informal workers that could be covered through non-contributory programmes targeting the poor.

The extension of anti-poverty programmes would cover a large share of informal workers in many countries. According to KIIbIH data, and using international poverty lines for comparison purposes, around 86% of the informal workers in Zambia would be covered if anti-poverty programmes were successful in covering all informal workers who are poor (with a maximum daily income of int'l dollar 2.15/day), with similarly large proportions for Madagascar (75%) and India (71%) (Figure 6.7).

Yet, while a consensus for using non-contributory, tax-financed programmes to reduce the social protection gap for the poor may exist, in some countries this is not necessarily the case for informal workers who are not considered poor. In designing an approach to increase coverage for non-poor informal workers, countries face a host of difficult decisions, including whether to offer universal entitlements or use other coverage mechanisms, such as voluntary or mandatory public social insurance; how to develop processes for identification and enrolment of the non-poor; and how to create attractive social insurance schemes to collect voluntary contributions, and whether to subsidise contributory schemes.

Figure 6.7. Informal workers are predominantly poor, but some belong to the upper quartiles of income distribution

Percentage of informal workers by income class



Note: Economic classes are based on four absolute per capita per day welfare thresholds, which differ by income level. LICs: poor: int'l dollar 2.15/day or less; near poor: int'l dollar 2.15-4/day; middle: int'l dollar 4-8/day; affluent: int'l dollar 8/day or more. LMICs: poor: int'l dollar 3.65/day or less; near poor: 3.65-7/day; middle: int'l dollar 7-20/day; affluent: int'l dollar 20/day or more. UMICs and HICs: poor: int'l dollar 6.85/day or less; near poor: int'l dollar 6.85-15/day; middle: int'l dollar 15-70/day; affluent: int'l dollar 70/day or more. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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Child benefits and social pensions can play an important role in lifting informal sector workers and their families out of poverty

According to KIIbIH data, more than one-half of children (60%) and older dependents (57%) live in households where all workers are informal (see also Chapter 5). This points to the key role that child benefits and social pensions could play as a supplementary mechanism to extend social protection to informal workers. If properly deisgned, these benefits could contribute to reducing the vulnerabilites that households with informal workers face.

Non-contributory social protection aimed at workers in the informal economy can play an important role. Emergency income support measures implemented during the COVID-19 pandemic showed that non-contributory social protection aimed at workers in the informal economy can play an important role in mitigating income risks. Brazil's emergency income support programme, the Auxilio Emergencial (AE), showed the positive economic impact of incorporating informal workers into non-contributory income support programmes. The scheme was implemented in April 2020, with the benefit level set at BRL 600 (Brazilian reals) (int'l dollar 120) per worker initially, which later decreased in subsequent iterations. Importantly, the income threshold for access to the programme was raised to three times the minimum wage per household. As a result, millions of informal workers who lost their income because of restrictive measures adopted during the COVID-19 crisis gained access to the programme. Subsequent research has shown that this initial phase of the AE lifted 13 million Brazilians out of poverty and reduced inequality by offsetting poverty among Afro-descendant and indigenous people in the country (Lusting and Trasberg, 2021[3]).

South Africa's COVID-19 Social Relief of Distress (SRD) Grant also initially incorporated informal workers. The South African government introduced the grant in April 2020. The eligibility criteria excluded those in formal employment, those aged under 18 years and over 59 years, those in receipt of any other grants or Unemployment Insurance Fund (UIF) benefits, and those in receipt of a stipend from the National Student Financial Aid Scheme (NSFAS). In this way, the SRD Grant partially addressed a large gap in the social security system by including those of working age in the informal economy. This iteration of the SRD Grant came to an end in April 2021 and was re-introduced subsequently with income threshold eligibility criteria which generally exclude informal workers. Research indicates that the initial design of the SRD Grant had positive economic impacts, including: (i) an increase in customer demand for the goods and services provided by informal traders, (ii) support for informal businesses, enabling them to survive in an environment of extreme economic stress and even to build businesses, and (iii) support for the circulation of people, goods and money, thus stimulating higher transaction intensity in different sectors and across value chains (Plagerson et al., 2023[4]). At ZAR 350 (South African rand) (int'l dollar 20 per month) the SRD Grant was too small to reverse many of the negative impacts of the COVID-19 economic crisis, but it was assessed to have acted as an effective shock absorber, indicating the potential for such interventions to support informal workers and local economies over the longer term (Plagerson et al., 2023[4]).

Extending contributory schemes to informal workers

Contributory social protection schemes constitute a key element of the extension of social protection to informal workers. Contributory schemes are based on the payment of contributions by workers and, in the case of employees, by their employers, which gives rise to acquired rights. As such, these schemes play an important role in the financing of social protection systems and can reduce the fiscal pressure on a government budget by offering a reliable and stable financing mechanism. Moreover, the level of protection offered by contributory schemes is usually higher than for many non-contributory schemes.

In most developing and emerging economies, contributory scheme coverage remains, by definition, limited to formal employees assuming a defined employment relationship based on a written contract and remunerated through regular wages, and with contributions typically shared between workers and employers. However, several contributory schemes also include other categories of workers, such as employers and own-account workers (ILO, 2021[5]).

A crucial step in the extension of contributory social insurance to informal workers has been the extension of social and labour rights to domestic workers through a combination of legal reforms and enforcement and simplification measures; the inclusion of self-employed workers in social insurance schemes through adapted mechanisms and simplified registration, tax and contribution payment mechanisms; the adaptation of contribution calculation and payment modalities to the capacities of workers and employers; and the use of digital and mobile technology to facilitate access to social protection.

As countries look at ways to extend contributory schemes to informal workers, they need to address several questions. One question is whether the extension of contributory schemes can be linked to an identifiable employment relationship between an employer and a dependent worker so that co-payments from the side of both employers and employees could presumably be an option. Another question is whether potential contributors may have the contributory capacity to enrol in contributory schemes. There is also the question about the extent to which the extension of contributory schemes can be best achieved through voluntary or mandatory enrolment.

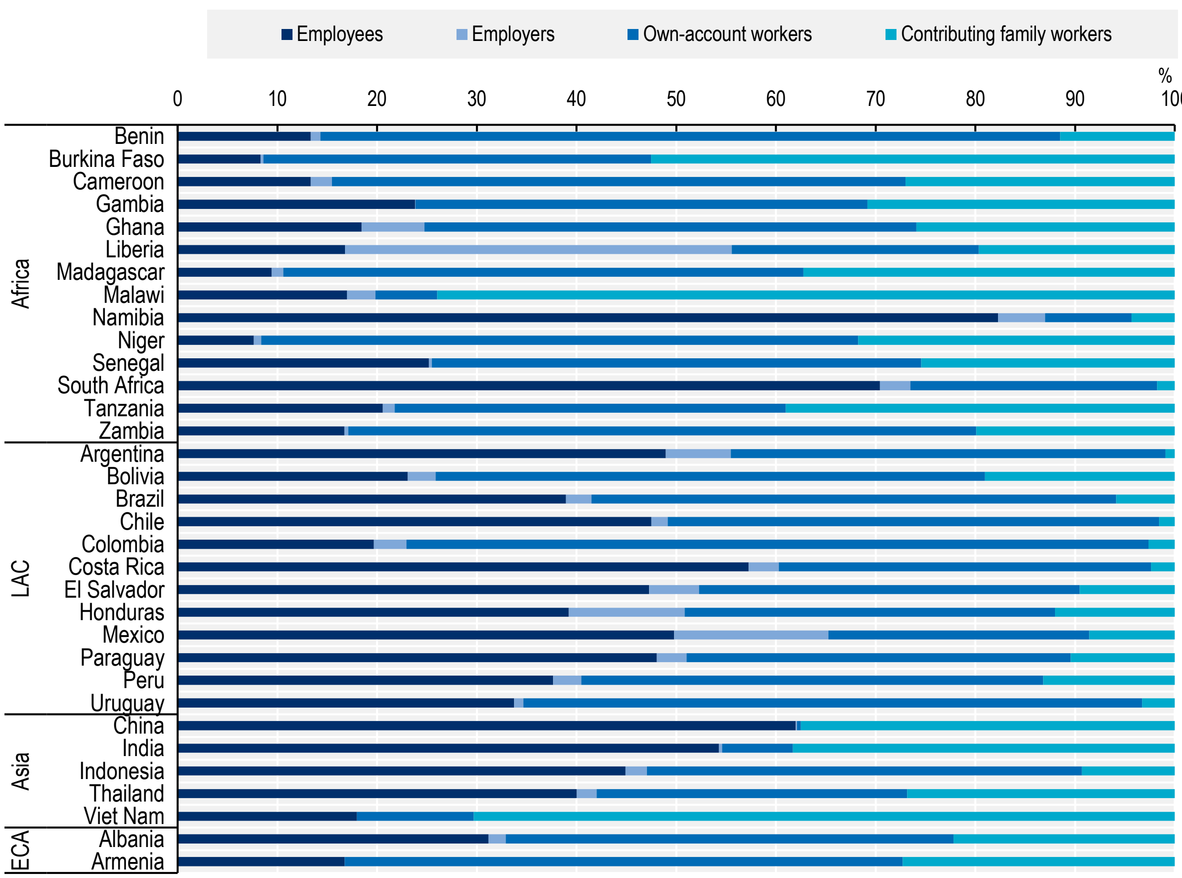
Finally, in contexts where a significant number of informal workers live with formal workers and where transitions into and out of informal employment may take place, the extension of social insurance to informal workers through other household members who are formally employed and the portability of contributory schemes throughout the life cycle of workers need particular attention.

While a large share of informal workers do not have co-payment possibilities, the scope exists for employer or employee contributions for certain types of informal workers

Status in employment is an instructive indicator for examining which actors should have responsibility for paying for the extension of social insurance to informal workers. As shown in Figure 6.8, a large share of informal workers in KIIbIH countries are own-account workers (39.0%) with no co-payment possibilities.[3] However, another significant share of the informal worker population is composed of employees (32.5%) for whom co-payments from the side of both employers and employees could theoretically be a possible option.

Figure 6.8. Most informal workers are employees and own-account workers

Distribution of workers by status in employment



Note: In Viet Nam, there is no way to distinguish between employers and own-account workers. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

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The contributory capacity of informal workers appears limited overall, yet some informal workers have a contributory capacity at the individual or household level

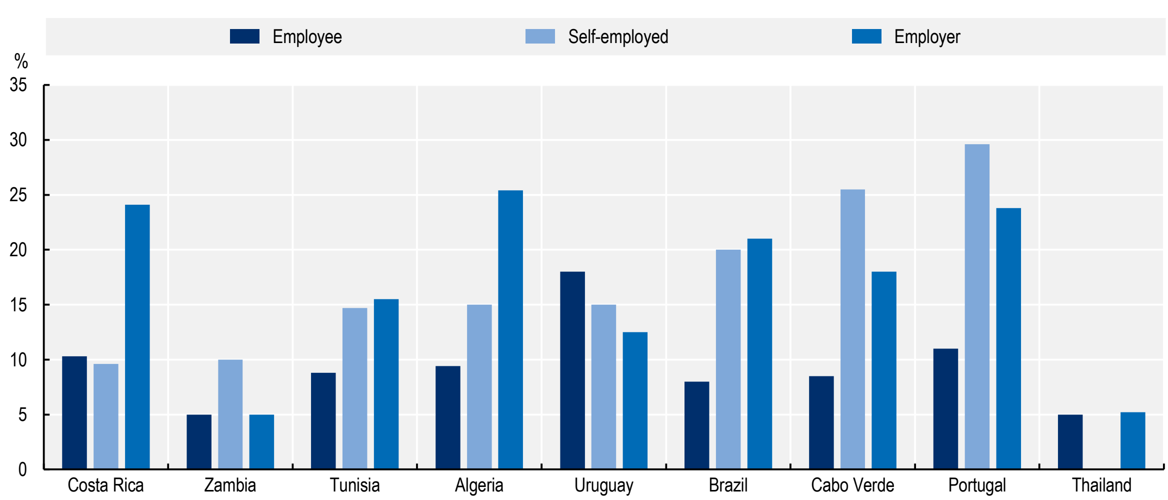
Recent experiences with the development of social insurance schemes for informal workers show that affordability issues need specific attention in the design of such schemes. Therefore, looking at the individual contributory capacity of informal workers as well as that of their household is critical. As shown in Chapter 2, information on the level of earnings of informal workers within the country sample indicates that a large number of informal workers have low earnings. These workers may lack the contributory capacity to pay for social protection, and contributory schemes would either have to be subsidised by the government and/or complemented with employer contributions when possible. However, a significant proportion of informal workers – between 18% and 90%, depending on the country – have medium or high earnings. As a result, these informal workers may have some individual capacity to contribute to social insurance schemes.

The affordability of schemes is particularly challenging for self-employed workers

The affordability of schemes for informal workers will also vary depending on their status in employment. A key issue for self-employed workers is the affordability of contributions. The fact that they do not have an employer who can share the cost means that self-employed workers are often required to contribute a higher share of their earnings to finance social insurance benefits. High contribution levels are particularly concerning, as many self-employed workers have low and often fluctuating incomes.

As a result, even when self-employed workers are legally entitled to access social insurance through voluntary or mandatory schemes, many of them are unable to afford contributions, which tend to be much higher – often twice as high – for self-employed workers than for employees (OECD, 2019[6]; OECD/ILO, 2019[7]). As Figure 6.9 shows, contributions from self-employed workers can often be higher than those paid by employees.

Figure 6.9. Statutory contribution rates for formal workers, by status in employment, in selected countries



Note: Rates are for statutory schemes covering workers in the private sector. Rates reported may not be comparable or fully representative, as rates may vary according to income level and degree of risk and may be assessed on different reference earnings. Flat-rate contributions are not included in the totals. When a range of rates is reported, the lowest value is included.
Source: Analysis in (WIEGO/ILO, Forthcoming[8]), based on International Social Security Association (ISSA) country profiles (2018-19).

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Various options exist to improve the affordability of contributions for self-employed workers

To improve the affordability of contributions for self-employed workers, governments have pursued a range of strategies, including enabling a gradual scaling up of contributions, providing matching subsidies, adjusting contributions to income levels and facilitating the settlement of arrears. In Algeria and Uruguay, the government allows new self-employed contributors to begin contributing at a lower rate and then gradually increasing to the standard tax rates that apply (ILO/FAO, 2021[9]; Aguiar et al., 2023[10]).

In several cases, governments have provided matching subsidies. For example, in Mongolia, the government matches contributions of herders and other informal and self-employed workers at 13.5% of their declared earnings. In Costa Rica, the government implements a proportional matching subsidy, with rates that vary with the income of the contributor and an inversely proportional schedule of subsidies. Mandatory health insurance for self-employed workers requires contributions of 11,00%, and mandatory pension insurance for self-employed workers requires contributions of 7.75%. However, only those with earnings of more than ten times the minimum wage pay the full amount. Those earning around half the minimum wage only pay 3.75% for health insurance and 4.25% towards their pension. Between those two categories, there are five earnings categories, set as multiples of the minimum wage. As incomes grow, workers pay higher contribution rates and government subsidies decrease, while the totals always remain at 11,00% and 7.75%.

Members of Thailand's voluntary social security scheme for informal and self-employed workers (Social Security Fund Article 40) receive a contribution from the government, paid into their social security account. The government's contribution increases with workers' contributions. In the case of the most basic benefit package, workers pay a monthly contribution of THB 70 (Thai baht), complemented by THB 30 from the government. Those who opt into higher benefit packages pay THB 100 (with the government contributing THB 50) or THB 300 (with the government contributing THB 100) per month.

In Costa Rica and Mongolia, programmes to help self-employed workers settle social security arrears are likely to have helped bring back former contributors who had accumulated debt from periods when they had not made contributions. For example, in Costa Rica, the government has periodically implemented payment plans, moratoria and interest/fine cancellation, including following the COVID-19 crisis, when employers and self-employed workers were given 12 months to apply for cancellation of surcharges, interest and fines, which is expected to restore the rights of some 140 000 workers. In Mongolia, the Law on Repayment of Pension Insurance Premiums of Herders and Self-employed, implemented in 2020, enabled participants to settle arrears on favourable terms (including making back payments at a rate of 10% of the minimum wage). In Uruguay's social Monotax, accounts are frozen if registrants miss two months of contributions, but no late-payment interest is charged. The registration can be reactivated by paying the delayed contributions.

However, reducing contributions to address affordability challenges can have negative implications in terms of their adequacy, especially if not paired with subsidies that raise contributions to a sufficiently high level. In the case of Uruguay's Monotax, subsidised contribution rates enable low-income informal workers to access benefits that are limited when compared with those offered by the standard social security system. In particular, Monotax registrants note the low value of retirement benefits and occupational injury benefit. Members of Thailand's Article 40 scheme for self-employed workers also perceived the value of their benefits to be inadequate, especially regarding the scheme's sickness benefit and compared with the scope and quality of benefits offered to formal sector workers.

Low levels of adequacy appear to be a particular issue in stand-alone schemes for informal or self-employed workers when compared with countries where such workers can access the general social security system with rights and entitlements comparable to those of formal employees. ILO supervisory bodies have generally observed that schemes based on the capitalisation of individual savings fall short of

International Labour Standards on Social Security, in particular the principles of solidarity, risk sharing and collective financing, as well as the predictability of benefit levels (ILO/WIEGO, 2023[11]).

The low and often fluctuating earnings of most informal workers mean that the integration of informal workers in schemes not based on the principles of solidarity, risk sharing and collective financing will likely result in inadequate benefits. A recent evaluation of Rwanda's Ejo Heza long-term savings scheme highlights the challenges of achieving adequate pension levels for informal workers through voluntary savings schemes alone. The authors calculate that annual savings rates would have to increase by a factor of four to five – and be paid consistently for at least 25 years – in order to provide pensions equivalent to the poverty line for 240 months (Guven and Jain, 2023[12]). The capacity of general social insurance schemes to generate adequate and predictable benefits through solidarity, risk sharing and collective financing heightens the importance of reforms seeking to ensure their inclusiveness for informal workers.

For certain contributory programmes, the affordability of schemes can also be influenced by the level of household income

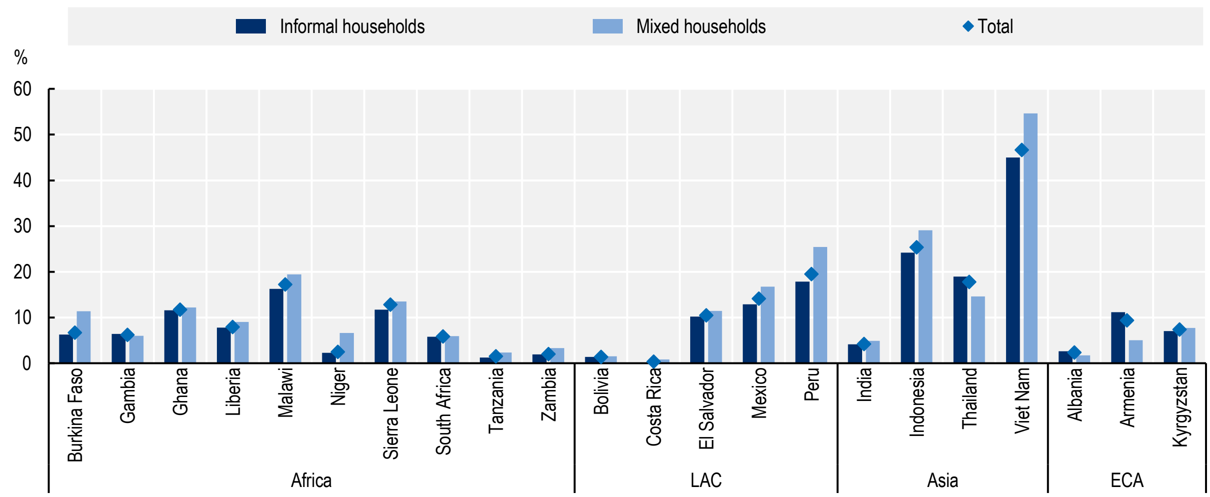
The contributory capacity to enrol in contributory schemes may also depend on household income, at least for some specific schemes such as health insurance. Examining the income category of informal workers is therefore essential. Evidence from KIIbIH data suggests that some informal workers live in non-poor households. Of these "non-poor" informal workers, between 27.7% (Zambia) and 94.8% (Sierra Leone) are in the middle or affluent class and could potentially be enrolled in non-subsidised contributory schemes if such schemes were available and/or enrolment compliance improved (Figure 6.7). Yet, between 8.8% (Zambia) and 50.4% (Uruguay) of informal workers are in the "near-poor" category and would most likely need to be supported through subsidised contributory schemes, as their contributory capacity to pay contributions on a regular basis may not be sufficient.

Remittances may also influence the contributory capacity of informal workers at the household level. They enable households to finance voluntary contributory schemes (Kolev and La, 2021[13]) and act as an informal insurance (Beuermann, Ruprah and Sierra, 2016[14]; Geng et al., 2018[15]). Relatively well-off recipient households may use the funds to participate in formal contributory schemes. In the case of Colombia, for instance, recent evidence shows that remittances are an important source of income that increases enrolment in contributory social insurance schemes among informal workers (Cuadros-Meñaca, 2020[16]). Moreover, remittance receipts can provide useful information to governments on the capacity of households to contribute to social insurance schemes such as health insurance.

An important question, therefore, is to what extent and under which conditions informal workers who receive remittances and who do not qualify for social assistance may be willing and able to channel some of their resources towards enrolling in formal social insurance schemes. According to KIIbIH data, 10.5% of informal workers live in a household that receives remittances and that is food secure (Figure 6.10). This suggests that the development of social insurance schemes targeting middle-class informal workers who receive remittances may be worthwhile.

Figure 6.10. Informal workers who receive remittances have some capacity to pay for social protection around 2018

Percentage of informal workers living in households that receive remittances and which are food secure



Note: Capacity to pay is estimated based on household food security (share of household consumption or expenses on food are less than 50%) and non-poor status (based on national poverty lines). Informal workers living in mixed households are those living with at least one other household member who is working in formal employment. LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

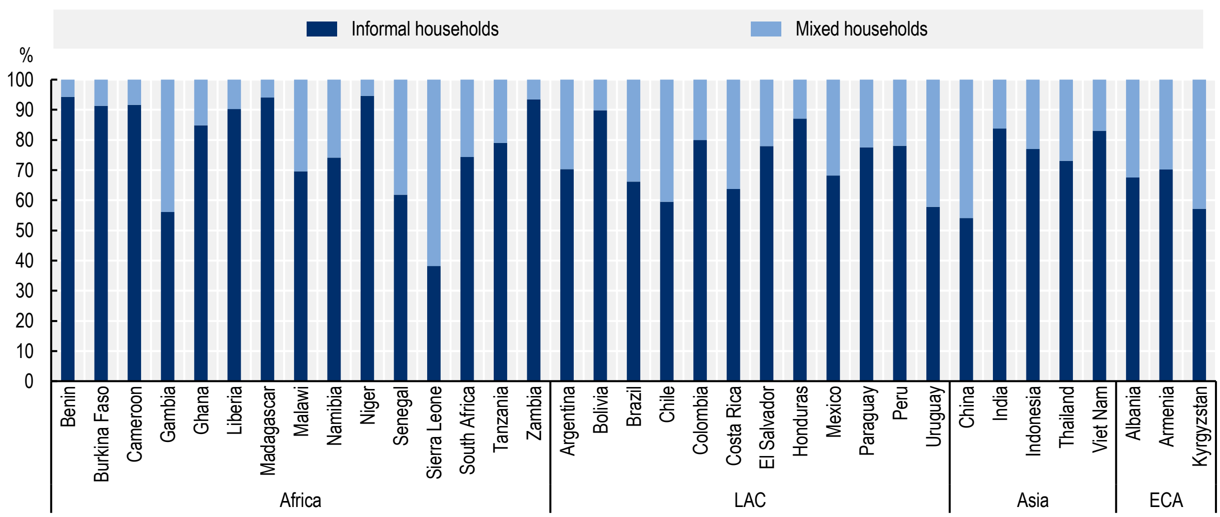
StatLink https://stat.link/zj1xw9

A small share of informal workers could be covered through formally employed household members

Looking at the presence of formally employed workers in informal workers' households can also yield useful information for the extension of social protection to informal workers. In principle, a small share of informal workers could benefit indirectly from the social protection coverage provided by formally working household members. One-quarter of informal workers live in households with other formal workers (so-called "mixed households"; 24.9%, Figure 6.11) and could presumably be covered indirectly by certain social protection schemes that they would not otherwise have access to (such as health insurance and old-age pensions). In LAC, for example, certain programmes like survivor pensions are paid for through contributions from the formal worker's salary but can benefit any informal workers who were part of the household unit when the formal worker passed away.

Figure 6.11. Informal workers are more likely to live with others who work in the informal economy, rather than with formal workers

Distribution of informal workers by degree of household informality



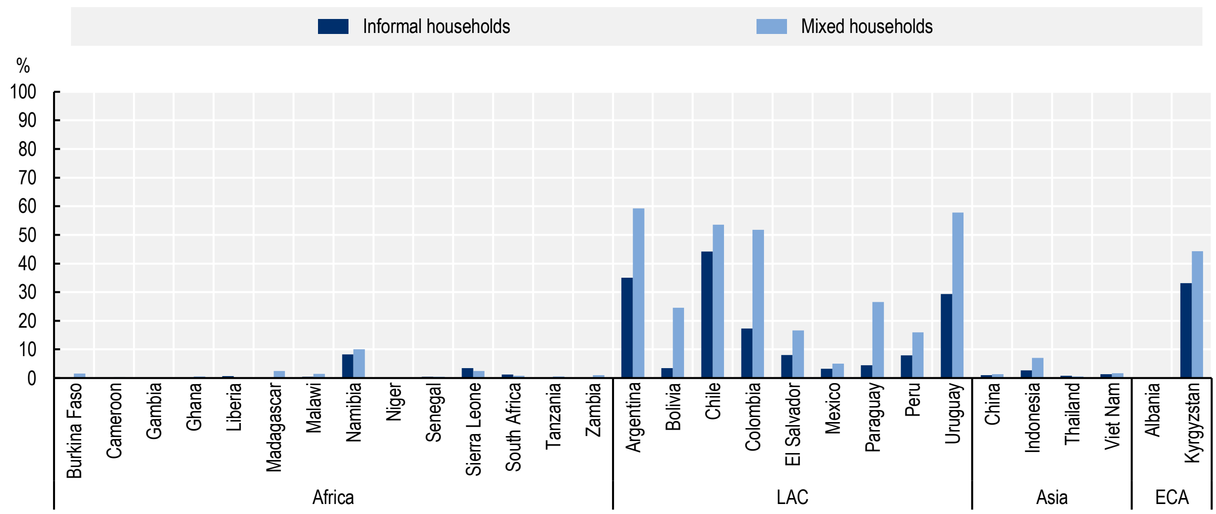
Note: LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

StatLink https://stat.link/4hnbar

Indirect access to social insurance through other formally working household members can be seen in, for example, health insurance coverage for informal workers. In a few countries, employment-based health insurance enables formal workers to add household members to their insurance plans, effectively covering them where they might not be entitled to any other insurance (Figure 6.12). According to KIIbIH data, health insurance coverage for informal workers in mixed households is higher than coverage for informal workers in informal households across many countries: for example, in Argentina, 59.2% of informal workers in mixed households benefitted from some form of employment-based health insurance coverage compared with 35,0% of informal workers in informal households. The findings are similar for Indonesia (7,0% in mixed and 2.6% in informal), Kyrgyzstan (44.3% in mixed and 33.2% in informal) and Namibia (10.1% in mixed households and 8.2% in informal households).

Figure 6.12. Social protection for formal workers can benefit informal workers in mixed households

Percentage of informal workers covered by employment-based health insurance



LAC – Latin America and the Caribbean. ECA – Europe and Central Asia.
Source: Estimates based on (OECD, 2021[1]), *Key Indicators of Informality based on Individuals and their Household (KIIbIH)* (database), https://www.oecd.org/dev/Key-Indicators-Informality-Individuals-Household-KIIbIH.htm.

StatLink https://stat.link/zt3xg0

However, a social protection strategy based solely on the potential for informal workers to benefit from the coverage of formal workers may also come with some adverse incentives for formalisation and may not take into account the fact that informal workers tend to live only with other informal workers. Moreover, not all social protection programmes benefitting formal workers (contributory programmes) can be opened to other household members.

Although limited, employment transitions into and out of informal employment call for the portability of social insurance benefits

While this does not describe most of the workforce, some individuals tend to transition between status in employment and into and out of informal employment and the workforce (Chapter 3). As a result, provisions that allow workers to carry benefit entitlements across formal and informal forms of employment can reduce the likelihood that workers will lose their entitlement to social protection after transitioning to another job opportunity. Moreover, contributory social protection should be designed in such a way that it is able to manage workers' fractional contribution histories and additional payments at one point in time, so that workers are able to obtain access to benefits that have been paid for through both contributory and non-contributory schemes.

Overall, these results confirm that countries do have opportunities to develop strategies to extend contributory social protection to informal sector workers, and that these strategies need to take specific challenges and constraints at the individual or household level into account. Aside from the barrier of affordability and co-payment possibilities, some informal workers may be living in a household that comprises only informal workers, whereas others may be living in a household where at least one of the members has a contract in the formal economy. Other challenges include the fact that some informal workers may face difficulties in meeting administrative requirements; other categories of informal workers may simply not be covered by the applicable legislation; or the social insurance schemes may not be adapted to the specific needs of informal workers in different work and household environments. Finally, when specific contributory schemes are made available to informal workers, the level of benefits may be considered too low to make the schemes attractive.

Important lessons can be drawn from country experiences in extending social protection to self-employed informal workers

Despite these challenges, efforts by governments to expand contributory schemes to informal workers are gaining traction around the world. Lessons about what works to extend contributory social protection to informal workers can be learned from such attempts across a range of criteria, including affordability, attractiveness, access, awareness and association (ILO/WIEGO, 2023[11]). Table 6.1 provides a summary of ten short case studies collected by WIEGO and the ILO showcasing innovations in social insurance to better cover self-employed informal workers.

Table 6.1. Innovations in social insurance for self-employed informal workers in ten countries

Country	Scheme	Description and innovation
Algeria	Caisse nationale de sécurité sociale des non-salariés (CASNOS), or National Social Security Fund for Non-Wage Earners	In Algeria, CASNOS demonstrates the effectiveness of a long-established mandatory scheme for self-employed workers – supplemented by other government policies to encourage formalisation – in continuing to improve access through an online portal, which allows members to check their account and status, declare their activities and contribution base, consult their career statements, make payments online, and request documents. To improve affordability, new affiliates with the scheme can gradually increase their contribution levels and formalise their professional situation over a period of three years, allowing them time to adapt to the welfare impact of a contribution, thereby smoothing the transition from informal to formal employment.
Brazil	Previdência Rural (Rural Pension) scheme and Simples Nacional monotax regime	The expansion of the rural pension in Brazil has ensured that many rural workers will now benefit from affordable and accessible social insurance. Meanwhile, the introduction of the Simples Nacional monotax regime – which has facilitated a simplified system for tax calculations, declarations, and collection – and its accompanying attractive benefits has led to the improved access and affordability of social insurance. In 2017, 4.9 million micro and small enterprises (MSEs) were reported to have applied to the Simples Nacional regime, and between 2009 and 2015, the percentage of individual micro-entrepreneurs registered increased from 33,0% to 41.7%. However, there continue to be challenges with this approach, including the low levels of contributions requiring significant subsidisation by the government, the challenge of ensuring that incentives for enterprise growth re preserved, and the continued existence of high tax evasion.
Cabo Verde	Compulsory social insurance under Instituto Nacional de Previdëncia Social (INPS) and proactive outreach activities	In Cabo Verde, more than one-half of economically active people aged 15 years and over are contributing to social insurance. Social security coverage expanded from 39.8% to 55.3% between 2016 and 2020. Compulsory social insurance is complemented by affordable options for low-income workers. Attractive benefits have encouraged formalisation and the uptake of social insurance, and the reduction of administrative barriers has improved access. Efforts to expand coverage have been complemented by advocacy and association measures and broad approaches to awareness raising. These innovative strategies are accompanied by proactive efforts by the government to increase awareness of social insurance across the wider population. For this, TV programmes, radio shows, newspaper articles, workshops, and building alliances with self-employed workers' organisations are utilised.
Costa Rica	Mandatory insurance for the self-employed under the Caja Costarricense de Seguro Social (CCSS), or Costa Rican Social Security Fund, and collective insurance agreements	Between 2005 and 2009, registration for health insurance by the self-employed in Costa Rica increased from 30.5% to 59.9%, and registration for pensions increased from 15.9% to 44.8%. This case demonstrates the effectiveness of mechanisms to ensure the affordability of social insurance for workers, particularly the use of government subsidies for those with low contributory capacity. The establishment of collective insurance agreements which consider the productive activity of the worker to determine contributions and facilitate access by enabling co-operatives to collect and transfer the contributions of their members is an innovative strategy to expand coverage of social insurance schemes to self-employed workers, particularly for rural workers. These efforts are supported by the imposition of mandatory health and pension insurance as well as investments in human resources which further promote enforcement.
Mongolia	One-stop shop and subsidies for informal self-employed workers	Mongolia is a good example for governments committing to expanding access for informal, self-employed workers in a context that is characterised by geospatial and logistical challenges. The innovative consolidation and simplification of social security services

		through one-stop shops has facilitated access to social insurance for Mongolia's widely dispersed population. The introduction of mobile technologies and non-cash-based contribution payment methods provide innovative examples for expansion. Specific efforts have been made to ensure that social insurance is affordable. Such efforts have been complemented by advocacy and association efforts, in particular engaging with herders' co-operatives.
Portugal	New benefits for the self-employed and clarifying "economic dependence"	The case of Portugal demonstrates how the creation of a new scheme with attractive benefits and amendments to eligibility requirements can increase coverage of social insurance schemes. This case also exemplifies how the recognition of a sub-category of the self-employed can provide affordable social insurance through a rebalance of social insurance contributions between a self-employed worker and a contractor in a fairer way. The classification of "economically dependent self-employed" workers as a sub-category of the self-employed is used as an innovative strategy to effectively facilitate the co-contribution to social insurance by workers and contractors.
Thailand	Voluntary access to Social Security Fund (Article 40)	Thailand's Article 40 scheme allows self-employed workers to voluntarily join the country's Social Security Fund. Workers can choose between different contribution and benefit packages, starting with sickness, disability and survivors' benefits and including a lump sum old-age benefit and a child allowance for those contributing more. Affordability and level of benefits is improved by a subsidy provided by the government that increases with workers' contributions. Few documentation requirements and multiple access points, including convenience stores, ensure accessibility. Despite being in existence since 1990, coverage under Article 40 remains low and challenges with maintaining regular contributions persist, likely due in part to the scheme's voluntary nature.
Tunisia	Ahmini ("Protect Me") scheme	Tunisia is a rare example of an attempt at incorporating gender-responsive elements into social insurance extension mechanisms by making social security contributions accessible for informal and self-employed women workers. The Ahmini scheme demonstrates innovative uses of mobile technology to facilitate the inclusion of informal workers with high illiteracy rates, and further utilises ambassadors and volunteers to reduce administrative barriers and to raise awareness. The scheme was recently interrupted, and participants were transferred to an existing scheme for low-income workers. However, the scheme nonetheless provides instructive insights into the challenges and potential solutions for rural workers, particularly women, on irregular incomes.
Uruguay	Simplified tax and contribution regimes – *Monotributo* and *Monotributo* Social	Uruguay's level of informal employment is the lowest in Latin America, with significant reductions in informality over the last decades. A key factor in this is the emergence of the *Monotributo* regime. *Monotributo*, established in 2001 and expanded in 2006, is a simplified regime that combines social security contributions and income tax in a single payment. Self-employed workers can register as personal enterprises with no more than one employee, partnerships with up to two partners or family businesses with up to three partners and no employees. Monotax registrants cannot operate from more than one small business location, must be providing their services or products exclusively to end consumers, and have an annual income of up to USD 20 000. Since 2011, the *Monotributo* Social targets low-income self-employed workers. Under both the *Monotributo* and the *Monotributo* Social, contributions are calculated based on a presumptive monthly income. Benefits include access to retirement pensions, sickness pay, occupational accident insurance, maternity/paternity leave and child benefits.
Zambia	SPIREWORK and Extension of Coverage to the Informal Sector (ECIS) pilot schemes under the National Pension Scheme Authority (NAPSA)	Zambia is a potential good practice example of the inclusion of informal – including self-employed – workers in a low-income context, through increased affordability and awareness. The introduction of pilot schemes implemented by NAPSA demonstrates the use of innovative strategies, including a mix of short-term and long-term benefits; an e-registration platform; easily accessible payment and balance information; the alignment of contributions to seasonal income flows; advertisement and awareness raising through pamphlets and roadshows; and a proactive engagement with organisations of informal workers. The roll-out of the new informal sector schemes has been delayed due to the COVID-19 pandemic and publicly available data on coverage rates and impacts are scarce. The Government of Zambia has expressed a clear commitment to enabling informal (including self-employed) workers to exercise their right to social security.

Source: (WIEGO/ILO, Forthcoming[8]), *Inclusive social insurance – exploring real solutions to reach the self-employed*.

The affordability of schemes has been addressed by governments through several strategies, including a gradual increase in contributions for newly contributing workers; a reduction in contributions either by lowering the rates or removing a contribution and possibly by making contributions income dependent; providing matching subsidies; providing top-ups for care credits; and facilitating the settlement of arrears.

However, lowering contributions as a single strategy may result in inadequate benefits so that the attractiveness of the scheme to workers is compromised.

Matching subsidies from the government can play an important role in ensuring the adequacy of benefits while maintaining affordability. Costa Rica's Social Security Scheme 'CCSS) provides progressive matching subsidies according to income levels in order to ensure greater inclusion of low-paid workers in the informal economy. Another less well-explored strategy is to derive co-contributions from economic actors other than employers within the value chains in which informal workers are embedded. For example, waste pickers in Argentina are exploring ways in which to leverage extended producer responsibility legislation in order to generate finance designed to improve working conditions and social protection coverage (Cappa et al., 2023[17]). In India, the same sector has been successful in making claims for social protection benefits from various actors in recycling value chains, including municipalities, citizens and businesses (Chikarmane and Narayanan, 2023[18]). Such co-responsibility for financing has also been observed in Portugal for "economically dependent" self-employed workers, which are workers who receive more than 50% of their income from one contracting entity, such as certain gig and platform workers.

Contributions and benefit levels across schemes should be designed to ensure that incentives towards underdeclaration of income, disguised employment and illicit registration are minimised. In Brazil, steep increases in contributions between the individual micro-entrepreneur regime, the monotax regime and the general tax regime, while social protection benefits remained similar across all three, meant that there was little incentive in place for businesses to increase contributions as they grew (ILO, 2019[19]). In 2018, the country implemented a new, progressive tax schedule to address this issue.

While the affordability of contributory schemes is an important consideration for low-income workers, this is not the sole barrier to uptake. The attractiveness of benefits is an important area for consideration in the design of contributory social protection. In Thailand, an ILO (2022[20]) study noted that contributions to the voluntary Article 40 Social Security Fund fell well within the average savings capacity of more than two-thirds of the working age population. Nonetheless, membership in the scheme remains much lower than the proportion of the population who should have sufficient savings capacity to participate. Qualitative investigation into perceptions of the Article 40 Social Security Fund among informal workers found that key reasons for the lack of uptake included the benefits not being considered sufficiently attractive, concerns about administrative barriers and a lack of knowledge about the scheme.

One common strategy is to combine long-term benefits (such as pensions) with short-term benefits in order to provide benefits that are immediately relevant. This combination was the case for all of the countries listed in Table 6.1, with old-age benefits most commonly combined with disability and survivors' benefits. Maternity benefits and health insurance were also common short-term benefits, and in the case of Zambia, a weather index insurance was included in order to enhance the attractiveness of the benefits for small farmers.

Countries have also experimented with the inclusion of incentives aimed at MSEs in addition to a mix of social security benefits. In Cabo Verde, the Regime Especial das Micro e Pequenas Empresas (REMPE), or Special Regime for Micro and Small Companies, provides a favourable tax regime to MSEs, with a 30% reduction in taxes for the first year of membership and a 20% reduction during the second year. Subsidies for personal income tax (PIT), value added tax (VAT), fire tax and social security contributions (SSCs) for employees are also available.

Simplified registration and benefit claim procedures can be found in many countries as a strategy to improve access to contributory social protection. Brazil and Uruguay have implemented monotax schemes for specific groups of workers, where a single payment covers both tax and SSCs. See Box 6.2 for a more detailed discussion of business-related incentives in Uruguay. Brazil has also reduced the documentation requirements for registration and benefit claim procedures. Mongolia uses one-stop shops where workers can access a range of social security services, including mobile services for workers unable to travel and herders unable to leave their livestock.

Tunisia's Ahmini ("Protect Me") scheme – affiliated to the Caisse Nationale de Sécurité Sociale (CNSS), or National Social Security Fund – provides insights into how to effectively use innovative technology to improve access to contributory social protection and facilitate contribution collection. The scheme specifically targeted low-income women working in agriculture, drawing on partnerships with telecommunications enterprises to provide an online application and payment service to members. In order to enable greater accessibility in a context of low literacy, the application could also operate through voice activation. In addition, community volunteers and "ambassadors" supported the collection of documents and the distribution of social security cards to those unable to use the mobile technology. This highlights the importance of offering flexibility and choice, with both manual and online options in place for registration and benefit claims.

Self-employed workers are not necessarily well informed about their social protection rights and obligations, and they are often underrepresented in processes that determine social protection rights and entitlements. The two challenges, and the solutions to address them, are mutually reinforcing: raising awareness about social security often requires the active engagement of community members, and vice versa. Several case studies, notably Cabo Verde, facilitated awareness raising through carefully designed and targeted communications campaigns. Government actors in Mongolia, Tunisia and Zambia have engaged with workers' organisations, and in Costa Rica, the use of collective insurance agreements stands out among the case studies as perhaps one of the most distinctive approaches to engaging self-employed workers and their representatives in the management of their schemes. For nearly 40 years, the CCSS in Costa Rica has enabled workers' co-operatives to collect and transfer contributions on behalf of workers.

The design of extension strategies often hinges on two key issues: first, whether to make schemes mandatory or voluntary, and second, whether to integrate schemes for self-employed informal workers into mainstream social protection schemes or to develop them separately. On the first issue, the case studies presented here point towards mandatory coverage being more effective (Brazil, Cabo Verde, Costa Rica and Uruguay). Voluntary schemes in Mongolia and Thailand were less successful in expanding coverage. However, the case studies also offered some evidence that mediating factors – such as the type and quality of benefits on offer, the degree and type of enforcement, and the existence of incentives – also had an impact on whether schemes were successful or not. Moreover, in the most successful case studies, extension was integrated into a wider whole-of-government approach to reducing informal employment. Where participation is mandatory, it must be accompanied by adequate investment in enforcement, as well as affordability and accessibility.

On the second issue, the case studies presented here tended towards the incorporation of self-employed workers into mainstream schemes, rather than creating separate schemes. However, there was wide variety and nuance in these two approaches. In several countries (Algeria, Cabo Verde, Costa Rica, Mongolia and Portugal) where self-employed workers were incorporated into the general scheme, specific mechanisms were put in place to encourage access for the self-employed. Conversely, in Brazil, Thailand, Uruguay and Zambia, separate schemes were established with specific adaptations for the self-employed, but within the institutional framework of the general system. This suggests that the reality is more nuanced than simply choosing between integrating self-employed workers into mainstream or specific schemes.

Box 6.2. Uruguay's Monotributo and Monotributo Social regimes: An informal worker perspective

Uruguay's Monotributo and Monotributo Social schemes represent the best-known examples of expansion of social protection to self-employed workers, who make up 26-29% of the country's total workforce (Abramo, 2022[21]). The Monotributo is a simplified regime that combines SSCs and income tax in a single payment. The regime covers MSEs with no more than one employee, up to two partners, or family businesses under limited conditions. The more recently implemented social Monotax scheme covers households below the poverty line or those in a situation of socio-economic vulnerability as defined by the Social Security Institution and who do not employ others within their business (i.e. they are own-account workers).

Several studies have described the institutional arrangements of the Monotributo regimes, but few studies (if any) have focused on the motivations and experiences of self-employed informal workers, a situation corrected by recent research from Aguiar et al. (2023[10]). Such studies are important because although the Monotributo regimes are in many ways success stories, coverage is still limited to between 14% and 23% of the target population. Better understanding the perspective of informal workers may help to develop further innovations to increase access. The findings of the research cut across the dimensions of affordability, attractiveness, access, awareness, and association.

Affordability: Efforts have been made to keep the minimum contribution for both regimes relatively affordable, and under the Monotributo Social scheme, participants can begin at a reduced rate, gradually increasing contributions over a four-year period. While some interviewees stated that in general the payments were not considered too high, several also mentioned that it was sometimes difficult to pay in months with low earnings. Monotributo Social registrants further emphasised that payments could become onerous on reaching the full payment amount. This is related at least in part to the fact that while the Monotributo Social scheme reduces informal employment, it does not necessarily increase job security, meaning that precariousness remains pervasive.

Attractiveness: In general, the workers consulted felt satisfied with being Monotributo registrants, identifying themselves with pride. The primary reason for registering under the regimes was to leave informal employment, mainly out of obligation or to gain access to new clients. In the period since the creation of the regimes, there has been a change in the general business environment in Uruguay, with a growing demand for formality. Many workers mention an improvement in the quantity and quality of customers, and other benefits such as peace of mind in the face of tax inspections, access to banking tools, and a capacity to adapt to a growing demand for formality.

Social protection benefits include access to a pension, sick pay, occupational accident insurance, maternity/paternity leave and newborn care subsidies. These benefits were a secondary reason for registering according to study participants. Both the pension and maternity benefits were assessed positively, but in general there was a sense that the benefits were too limited, and the absence of an unemployment benefit was noted. More affordable health insurance contributions, and the ability to progress to higher-level payments, were two recommendations to remedy this situation.

Access: Most workers interviewed considered that the various improvements and adaptations made to the regimes since 2011 when they were introduced had increased accessibility. At present, the procedures to register are generally considered simple and can be completed either online or in person.

Awareness: The issue of lack of awareness and information regarding the schemes' benefits was raised repeatedly during the study. Even those who were registered often did not know that they had access to a family allowance, sick pay and occupational accident insurance. Many also did not know the amount of pension they would receive. The focus group discussions repeatedly saw participants finding out about their benefits from one another. This suggests that there is great scope for more awareness raising and information campaigns.

Association: There was a strong sense that the regimes could do more to ensure greater worker representation in the schemes. It was argued that the schemes emphasise entrepreneurship status over worker status, individualising (and potentially also isolating) registrants. The regimes do little to contribute to a self-perception of registrants as workers or to promoting their involvement in the collective processes of organisation and ownership of the schemes.

Source: (Aguiar et al., 2023[10]), *Monotributo y Monotributo Social en Uruguay: Apreciaciones de trabajadores y trabajadoras monotributistas*.

Overall, across the case studies, the most common enabling factor was a strong institutional and governance framework. Strong institutions were cited in Algeria, Brazil, Costa Rica, Mongolia, Tunisia, and Uruguay, and were also significant factors in Cabo Verde and Portugal. After strong institutions, the legal and policy environment was highlighted as an important enabling factor in Brazil, Cabo Verde, Costa Rica, Tunisia, and Uruguay. Several of the case studies – specifically Brazil, Costa Rica, Mongolia, Portugal, and Uruguay – indicated high administrative capacity as a key enabler of success. Less frequently, but not less importantly, additional important enabling factors in each country included relatively high levels of trust in government or expressed willingness to contribute (Algeria and Zambia); the involvement of international actors (Mongolia and Zambia); and the strength of workers' movements and organisations (Costa Rica). No single factor is sufficient to explain or enable success on its own, but rather worked in tandem with others, the strategies employed by governments and the idiosyncrasies of the unique historical, political, economic and institutional contexts and legacies of each country. But a combination of high institutional capacity, strong legal and policy frameworks, and high administrative capacity appeared to be powerful determinants of success in countries such as Brazil, Costa Rica and Uruguay.

Financing the extension of social protection to informal workers

Closing the global social protection coverage gap, including for informal workers, requires a step change in financing strategies. According to estimates from the ILO and the Overseas Development Institute (ODI), the funding gaps for social assistance alone, and excluding healthcare, range from USD 34 billion to USD 36 billion per year (United States dollars) for all low-income countries. As a result of the COVID-19 crisis, the ODI estimates that nearly all low-income countries and some lower-middle-income countries will not be able to afford even one-half of the required costs by 2030 (Evans et al., 2023[22]).

Designing the domestic social protection system in a way that encourages informal workers with some contributory capacity to contribute (for example, through the schemes discussed in the previous section) could be one way to mobilise revenues and finance the expansion of social protection.[4] Supporting the inclusion of informal workers in social insurance schemes would not only provide higher levels of protection for previously excluded workers and their dependents, but also has the potential to increase their productivity and incomes through formalisation. However, even in the best-case scenario, the number of previously informal workers who register with the social security administration will only increase gradually. In order to achieve universal social protection, most governments will have to find strategies to mobilise significant tax revenue in addition to supporting the inclusion of informal workers in social insurance schemes. Additional tax revenue may be necessary to finance universal social protection floors or to design the type of contributory schemes that are both affordable and attractive and encourage informal workers to register.

Sustainably funded social protection systems are challenging to build when informal employment is high, but several options exist

High rates of informal employment suggest that relying mostly on the revenue generated from traditional contributory social insurance is not sufficient. As discussed in the previous section, few informal workers participate in contributory social protection schemes,[5] which implies that these systems generate neither enough revenue nor adequate coverage for informal sector workers. Relying solely on SSCs to finance a universal healthcare system does not appear to be a recommendable strategy from efficiency and equity perspectives according to several academic studies (Yazbeck et al., 2020[23]). Countries with high rates of informal employment may opt to first establish or expand social protection floors through universal non-contributory schemes that are financed by general tax revenue, which can be supplemented with contributory social protection schemes. While this approach may result in limited protection initially due to low tax revenue it may be the only feasible option for some countries (especially low-income countries) in the short term.

Over time, countries that have chosen this path can gradually increase the generosity of their social protection floors when they are able to collect more tax revenue and/or start introducing contributory schemes that would finance social services above the minimum floors. Countries that have chosen to finance a large share of their social protection system through general tax revenue will have to ensure that all individuals pay their fair share of general taxes. A large informal sector makes it difficult to raise the general taxation revenue necessary to finance adequate universal social protection benefits for all; informal workers who do not pay SSCs will also not file a PIT return; and a large informal sector will reduce the potential revenues from VAT and other indirect taxes.

Other countries might be able to provide universal social protection floor by further redesigning the existing contributory and targeted non-contributory schemes and by expanding their coverage to those currently lacking coverage. This may be a viable strategy in, for instance, countries where SSCs are paid by employees but are not paid by self-employed entrepreneurs. The preferred strategy has to be evaluated at the country level and will depend on country-specific structural features and options for reform. The strategy will also need to be dynamic in that it can and should adjust and change over time.

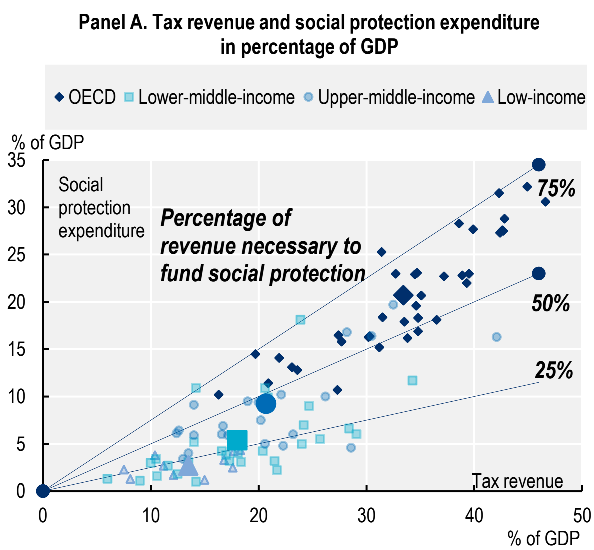
Whatever the strategy chosen, developing countries will have to mobilise significant additional revenues to finance universal social protection

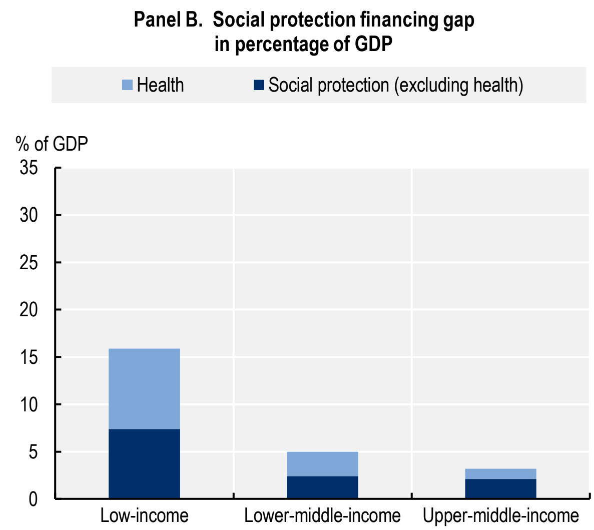
Additional revenues will have to be raised primarily through the domestic tax system (including SSCs) in order to be sustainable in the long term. Indeed, only domestic government resources will provide the reliable stream of sizeable revenues that are independent from other countries' priorities and necessary to sustain and further expand social protection over the medium and longer term.

Reprioritising government expenditure and increasing spending efficiency will not be sufficient to close the substantial social protection financing gaps that can be observed in developing countries (Figure 6.13). For instance, the social protection gap is estimated to be around 15% of gross domestic product (GDP) for low-income countries and 5% for lower-middle-income countries (Figure 6.13, Panel B). To close the gap, many low-income countries would have to spend more than 75% of their tax revenues on social protection (Figure 6.13, Panel A), more than the expenditure of OECD member countries with a much larger tax revenue base.

Lower-middle-income countries would need to spend around 50% of their current tax revenue on social protection alone, which will not be possible considering other pressing spending needs. Even though spending reallocation can be part of the strategy to close the social protection financing gap, it will not be sufficient on its own.

Figure 6.13. Tax revenue, social protection expenditure and financing gaps





Note: Total tax revenues is shown as a percentage of GDP in 2019. Social protection expenditure in 2020 or for the latest available year is shown as a percentage of GDP. Includes domestic general government health expenditure obtained from the World Health Organization (WHO) (Panel A). The graph indicates the share of tax revenue that would be necessary to fund the current expenditure levels on social protection. Countries may also use other sources of funding such as debt or grants. Average financing gaps for achieving universal social protection coverage in 2020 are shown as a percentage of GDP.

Source: (ILO, 2021[24]), *World Social Protection Report 2020–22: Social Protection at the Crossroads – in Pursuit of a Better Future*; (OECD, 2022[25]), *Revenue Statistics 2022: The Impact of COVID-19 on OECD Tax Revenues*; and (Durán Valverde et al., 2020[26]), *Financing gaps in social protection*.

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Raising additional general government revenue will be a key component of most countries' strategies. The tax policy measures aimed at raising additional revenues need to be carefully chosen and accompanied by tax administration measures as well as by efforts to build a taxpayer culture. Tax measures implemented to close the social protection financing gap should ideally not harm other development goals (e.g. they should not place an additional burden on the poorest, or increase inequality) and should not come at the cost of other key development expenditure (such as on the education system).

The impact of tax measures on economic development and investment must be taken into account as well. Economic growth will be necessary to finance high-quality social protection in developing countries. In a context of low levels of GDP, mobilising a higher share of GDP in taxes to finance social protection will ultimately not be sufficient to finance high-quality social protection, especially in low-income countries. Take, for example, the average GDP per capita of a lower-middle-income country in 2021, which was around USD 2 500 per year. Even a tax-to-GDP ratio of 50% (i.e. around in monthly per capita tax revenues) would not be enough to finance high-quality healthcare, adequate pensions and other pillars of social protection in addition to other pressing spending needs (e.g. education and infrastructure) if the level of income does not change. Economic growth is therefore unavoidably part of a strategy to finance the expansion of social protection to the entire population in a developing and emerging economy. As a result, any tax and SSC reform that aims at raising funds to finance social protection should, as much as possible, avoid creating hurdles to economic growth. For instance, taxes that are generally less harmful to economic growth (such as property taxes and indirect taxes) may be preferred (IMF et al., 2016[27]).

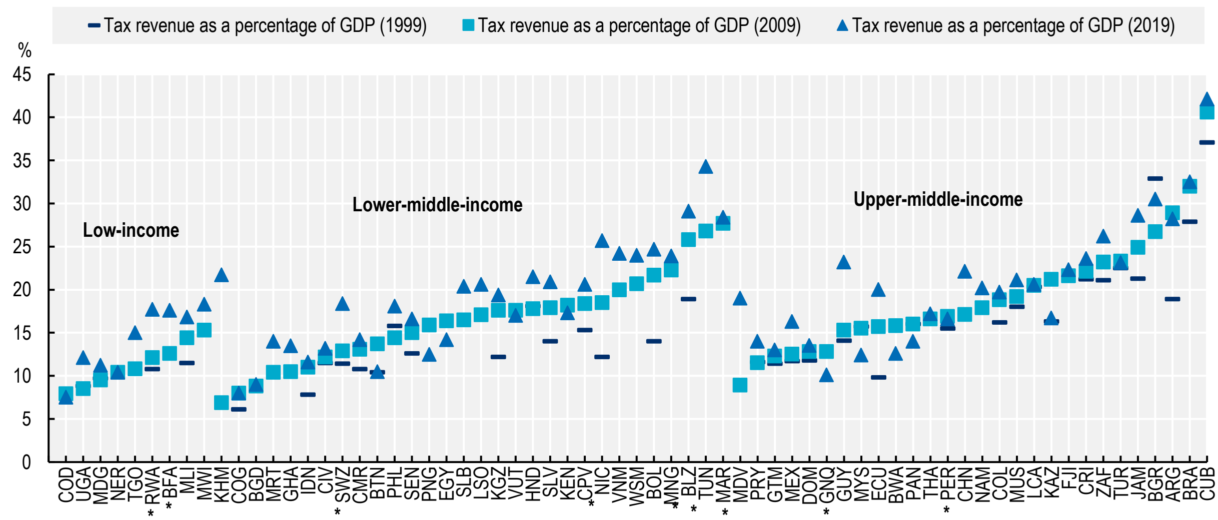
There is significant potential to increase revenues in developing countries, but careful tax reforms are needed

A preliminary frontier analysis (which compares current tax revenues to the estimated tax revenue frontier given a country's structural characteristics) reveals that there is significant room for increasing revenues in developing countries, even with the current level of income and informal employment. In low-income countries, the tax revenue frontier (i.e. the tax revenues attainable given a country's structural characteristics) is 5% of GDP higher than current revenue. These additional tax revenues are even larger in lower-middle-income countries, where they reach 9% of GDP on average. However, the tax revenue potential differs greatly across regions and countries.

Even if the theoretical potential for revenue growth is high, evidence shows that raising 5% of GDP – far below the actual financing gap in most low- and lower-middle-income countries – in additional tax revenue over a decade will already be challenging. Over the 1999-2019 period, fewer than ten developing countries in the OECD Revenue Statistics database managed to increase their tax-to-GDP ratio by more than five percentage points (Figure 6.14). According to the International Monetary Fund (IMF), increasing the tax-to-GDP ratio by five percentage points over a decade is an ambitious but feasible target for most developing countries (Gaspar et al., 2019[28]). Raising significant amounts of additional tax revenue over time in ways that are aligned with inclusive and sustainable economic growth objectives will require a country-specific tax reform plan that is carefully developed, implemented, and sustained over time.

Preliminary OECD analysis shows that, in countries with high informal employment, the short-term revenue potential is largest for indirect taxes such as VAT or sales taxes. Indirect taxes have the advantage of having a broad (and relatively inelastic) tax base. But increasing rates or broadening the base of indirect taxes to finance universal protection may increase the tax burden for the poorest members of society and could ultimately also have a negative impact on the size of the formal economy (by fostering the expansion of goods sold in the informal market). Recent evidence shows that, in some developing countries, poorer households mainly shop in informal markets, and thus consumption taxes are paid disproportionately by richer households, which offers an equity motive for relatively higher consumption taxes (Bachas, Gadenne and Jensen, 2020[29]). However, if the poorest members of society are not able to afford to pay the tax when they do consume (even a small fraction of their total expenditure) in the formal market, it would be an inadequate tool with which to finance universal social protection floors. Thus, the "affordability" of indirect taxes needs to be assessed with care depending on the country characteristics. One strategy to increase government revenue which limits the negative impact on the poor could be to decrease or abolish reduced VAT rates or VAT exemptions applied to non-essential goods and use the revenue to expand social protection programmes targeted at the poor. Tax expenditure reports typically show that the tax revenues forgone from reduced VAT rates and VAT exemptions are large in developing countries. Lastly, the paper trail generated by a VAT system leads to the fact that a greater enforcement of regulation upstream or downstream implies a higher probability of being formal (Ulyssea, 2020[30]).

Figure 6.14. Evolution of tax-to-GDP ratios between 1999 and 2019



Note: Stars under the countries' name indicate an increase in the tax-to-GDP ratio between 2009 and 2019 of more than five percentage points.
Source: OECD Global Revenue Statistics Database, (OECD, 2022[25]), *Revenue Statistics 2022: The Impact of COVID-19 on OECD Tax Revenues*.

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Health taxes, environmental taxes, fossil subsidy reform and tax expenditure reform are frequently included in the list of tax measures that can contribute towards raising more revenue for social protection in developing countries. Health taxes and environmental taxes or subsidies are mentioned in the context of social protection financing because of their direct link with health and social protection. However, the link does not imply that tax revenue from these sources would automatically be earmarked for social protection expenditure (as is the case with SSCs). The advantages and disadvantages of earmarking these tax revenues would have to be discussed in their own right. Options for tax expenditure reform can be identified by analysing the forgone revenue and the effectiveness and distributional impact of the tax relief provisions in place in each country. Priority shall be given to reform tax expenditures that are ineffective at achieving their goal. For example, certain tax incentives have been shown to have a limited impact on attracting investment or fostering growth (IMF et al., 2015[31]). It is also important to consider the distributional impact of tax expenditures. Income tax expenditures are often regressive and benefit high-income households disproportionately, which may constitute a rationale for reform.

Due to high informal employment and a lack of information and enforcement in low- and middle-income countries, third-best tax policies (such as taxes on inputs and turnover, which are usually not recommended in OECD member countries) need to be considered and evaluated in low- and lower-middle-income countries (Kleven, Khan and Kaul, 2016[32]). Ideally, the tax rate for each type of tax should be set at (or just below) the revenue-maximising tax rate. This revenue-maximising tax rate can grow over time by limiting tax evasion behaviour through better tax enforcement (Bergeron, Tourek and Weigel, 2023[33]).

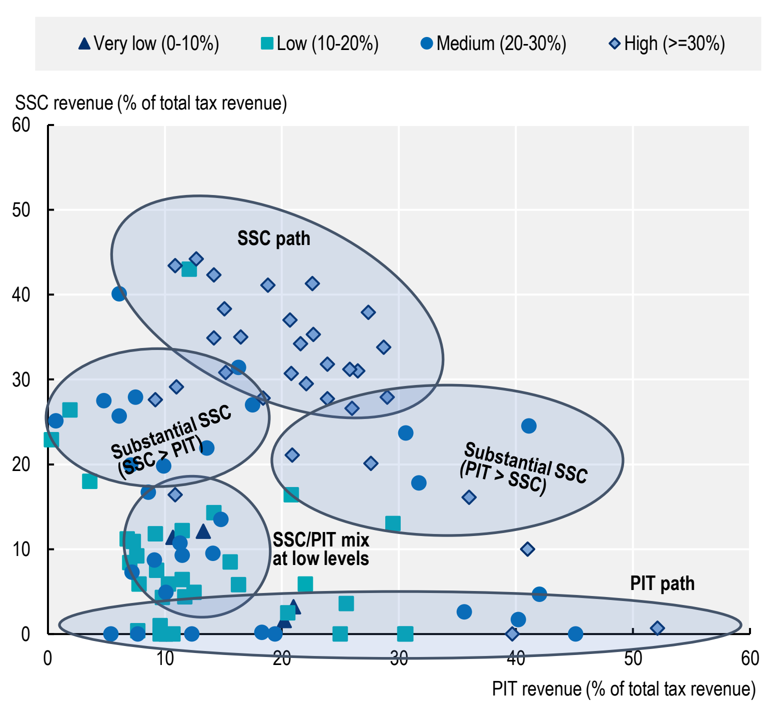
For each tax type, it is important to evaluate, at the country level, whether there is a potential to: i) increase compliance, ii) limit international leakages, iii) broaden the tax base and avoid domestic leakages, or iv) increase the rate or introduce a new tax. It is also key to evaluate the revenue potential of each tax measure. Such an analysis, at the country level, would be part of the four modules of the new Social Protection Tax Revenue framework (Box 6.4).

Identifying the most suitable tax revenue sources is critical

In the context of high levels of informal employment, choosing the most suitable tax revenue sources involves additional trade-offs that need to be carefully balanced, including the challenge that the tax measures should not further hamper the employability of workers. Despite the more nuanced perspectives on informal employment that proliferate (see Box 6.3), fostering formal employment and the employability of the workforce continues to be an important task for developing countries. Many countries have large informal economies where workers are trapped in low-quality jobs without opportunities to upskill and grow into more productive jobs that potentially also provide for better social protection. Informal employment makes workers and their families vulnerable to economic shocks and adverse life events. Mobilising revenues to enhance social protection and using the available resources in the most effective manner needs to go hand in hand with policies that increase the number of informal workers who enter the formal economy and, indeed, policies that stimulate sustainable economic growth and formal work.

OECD member countries with comprehensive social protection systems tend to rely mainly on direct taxes and SSCs to finance social protection (Figure 6.15). SSCs account for around one-quarter of total tax revenue, and income taxes (corporate income tax (CIT) and PIT) for more than one-third. SSCs are taxes that are earmarked to finance social protection and, in many cases, there is a link between contributions made and benefits received (e.g. unemployment benefits, pensions). In a setting where taxpayers perceive SSCs as payments to themselves, either in the future or as an insurance, they may be more willing to comply with their tax obligations. This line of reasoning offers a strong argument for keeping SSCs in the social protection financing mix (instead of relying predominantly on PIT or indirect taxes to finance social protection, for instance). Maintaining a balance between employee and employer contributions is also desirable.

Figure 6.15. Relative role of SSC and PIT revenues by tax-to-GDP ratio (clusters of revenue paths)



Note: Countries are grouped by their tax-to-GDP ratio in 2019 (very low, low, medium, high). Includes countries represented in the OECD Global Revenue Statistics Database.
Source: OECD Global Revenue Statistics Database, (OECD, 2022[25]), *Revenue Statistics 2022: The Impact of COVID-19 on OECD Tax Revenues*.

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Most developing countries will likely eventually have to reorient their social protection financing towards SSCs. SSCs continue to play a key role in ensuring a basic level of protection, according to the ILO. One way to gradually increase revenue generation through SSCs could be to introduce presumptive tax regimes. Under such a regime, small businesses could be allowed to pay one single tax that replaces as many taxes as possible, including SSCs. The collecting body would redistribute the funds internally among the various institutions, including tax administrations and social security funds (Mas-Montserrat et al., 2023[34]).

Social security contributions play a key role in financing social protection systems

Despite persistent informal employment, revenue raised through social insurance contributions has remained stable or even increased since the early 2000s and represent a major source of financing for social protection systems. Globally, SSCs accounted for 18.8% of total taxation or 5.7% of GDP in 2019 (for countries included in the OECD Revenue Statistics Database). In 2019, high-income countries raised on average 8.6% of GDP and 24.9% of total taxation via SSCs. Percentages were lower but still substantive for upper-middle-income countries (3.3% of GDP and 15.7% of total taxation), lower-middle-income countries (2.6% of GDP and 10.6% of total taxation) and low-income countries (1.3% of GDP and 8.1% of total taxation). From 2000 to 2019, SSCs as a share of GDP increased by 0.7 percentage points globally. Perhaps contrary to expectations, social insurance contributions as a percentage of GDP increased more in regions with higher levels of informal employment, such as LAC, Africa and Asia, albeit from a lower base (Calligaro and Cetrangolo, 2023[35]).

Replacing SSCs with PIT in developing countries that already rely partly on SSCs is therefore often not an appropriate strategy. Countries that struggle to raise revenues via SSCs face similar challenges when raising PIT given that it is a similar tax base (Figure 6.15). Abolishing employer SSCs would result in a significant reduction in tax revenue in many middle-income countries. The assumption that there will be full compensation and that wage levels will increase by the amount that employer social contributions were reduced, is also strong if the perceived link between contributions and benefits is low (Korkeamäki and Uusitalo, 2009[36]; Kugler and Kugler, 2009[37]; Bozio, Breda and Grenet, 2019[38]).

Voluntary private contributions can be complementary, but on their own (even if matched) they will fail to deliver universal and adequate social protection. Voluntary subsidised contributions have been suggested as a strategy to boost pension savings from the informal “missed middle” who are neither covered by contributory schemes nor receive universal benefits targeted at the poor (World Bank, 2019[39]). Examples of country experiences in which voluntary private schemes, on their own, managed to achieve universal and adequate social protection do not exist because social protection systems feature a redistributive component and are put in place precisely to address failures of private markets (such as adverse selection and externalities).

Attention is needed to ensure that greater financing for social protection systems does not increase the cost of formalisation

As mentioned in the previous section, the introduction of presumptive tax regimes has been one tool with which to gradually increase the coverage of non-standard workers in contributory schemes while at the same time raising some revenue and supporting formalisation. Presumptive tax regimes are often seen as a formalisation tool for enabling small businesses and self-employed workers to gradually become fully formal. However, badly designed regimes may have the unintended effect of discouraging businesses from growing in order to avoid sharp tax increases once they are subject to standard CIT or PIT, and may also encourage self-employment (Melguizo, Bosch and Pages, 2017[40]). Recent work by the OECD Centre for Tax Policy and Administration presents an analytical framework that characterises country-specific presumptive tax regimes and identifies best practices for the design and administration of such regimes (Mas-Montserrat et al., 2023[34]).

The impacts of social protection systems on labour markets with high levels of informal employment remain a concern for some policy makers at the international and national level. Existing evidence, however, does not necessarily support claims that social protection causes informal employment (Box 6.3). While the impact of social insurance contributions and payroll taxes is also a concern,[6] studies have found mixed results. Reviewing the existing literature on the impacts of reduced or subsidised social insurance contributions on labour markets, Calligaro and Cetrangolo (2023[35]) showed that most studies found no significant employment effect.[7] In his extensive review of the literature on informal employment, Ulyssea (Ulyssea, 2020[30]) reported that reducing the tax burden can induce some formalisation, although the elasticity seems to be low. The results depend on the relative level of SSCs compared with the productivity of workers in the economy and are therefore country specific. But experiences of countries cutting contribution rates – as part of structural reforms of pension or tax systems, during stabilisation programmes, and during crises, or to support the labour market participation of specific groups – have generally been disappointing in terms of generating formal employment, but have generated significant costs (Calligaro and Cetrangolo, 2023[35]).

Indeed, the fiscal cost of diminishing contribution rates might be sizeable. For instance, Egebark and Kaunitz (2013[41]) studied the payroll tax cut for young workers in Sweden in 2007-09 and estimated the cost per created job by comparing the cost of forgone payroll tax revenues due to the tax reduction with the increased tax revenues generated by the estimated employment and wage increases. The authors claim that the cost for each new job that was created was more than four times that of directly hiring workers at the average wage. More generally, any reduction in social insurance contributions creates an effective loss in government revenue in the short term. (Ulyssea, 2020[30]) concludes that reducing the costs of formality, in particular related to tax, has significant formalisation effects, but in general is not strong enough to be cost-effective, and has very limited aggregate effects.

Box 6.3. The evolving debate around social protection and informal employment

The impacts of social protection systems on labour markets with high levels of informal employment remain a concern for some policy makers at the international and national level. For some time there has existed an idea that mixed systems of social protection – which combine employment-linked social insurance with tax-financed social assistance for low-income informal workers – increase the levels of informal employment by establishing a financial incentive for workers and enterprises to exit the formal economy or remain informal.[8] The claim that social protection systems can cause substantial increases in informal employment (or not), or does not allow it to be lowered in countries where the rate of informal employment is very high, presents a challenge to governments' efforts to both expand social assistance to low-income workers and make social insurance systems more affordable through subsidies or matching contributions. Following this claim's logic, introducing social assistance benefits or subsidising social insurance contributions for those not in formal employment represents a subsidy of informal employment, as informal workers and their dependents can now access benefits on a non-contributory or subsidised basis, whereas formally employed workers and enterprises are required to pay full contributions. The provision of both social assistance and subsidised social insurance to informal workers is therefore assumed to increase the difference between the costs and benefits of informal and formal employment, resulting in enterprises and workers choosing informal employment.

The core of the evidence base consists of 11 experimental or quasi-experimental studies that aimed to estimate the effects of social protection programmes – contributory, non-contributory, cash transfers and health insurance schemes – on measures of informal and formal employment. Of those, seven found increases in informal employment or decreases in formality as a result of social protection interventions. However, impacts were mainly identified for specific sub-groups of the population, such as older people, parents with young children, men working in particular sectors, or vulnerable groups, and such impacts rarely affected the national average. Wagstaff and Manachotphong's (2012[42]) analysis of the effects of Thailand's universal health coverage (UHC) scheme found no statistically significant impacts on total formal employment, but did find a small, significant effect of 1.2 percentage points only after three years and in the manufacturing industry (Seira et al., 2023[43]). Indeed, effect sizes are generally small. For instance, Aterido et al. (2011[44]) found that Mexico's Seguro Popular programme (which provided health coverage for those outside the social security system) did not reduce formal employment, but did reduce entry into formality by a mere 0.4-0.7 percentage points. Bosch and Campos-Vazquez (2014[45]) found that Seguro Popular reduced formal employment, but the effect was only present for enterprises with fewer than 50 employees. The number of formal employers had decreased by 1.4% one year after implementation, and by 4.4% four years after implementation. The same authors estimated that, between 2000 and 2011, this translated into a cumulative reduction of 171 000 employees who would otherwise have formally registered with the country's social security system in an economy with close to 20 million formal jobs. Mexico's social protection system, and in particular Seguro Popular, remains central to the debate about social protection driving informal employment, but new evidence confirms the existing literature findings of no impacts on employment. Levy's (2008[46]) analysis of Seguro Popular placed concerns on the potential of social protection programmes to incentivise informal employment on the agendas of policy makers at the national and international level, and with it, Mexico's centrality in the research and debates on this issue (e.g. (IMF, 2021[47]; UNDP, 2021[48])). Indeed, the majority of studies exploring potential incentives towards informal employment focused on evaluating one of Mexico's social protection programmes: mainly Seguro Popular, but also other healthcare and prescription drugs programmes (Juarez, 2008[49]) or non-contributory pensions (Galiani, Gertler and Bando, 2014[50]).

Most of the evidence finds that Seguro Popular had no effect on informal or formal jobs (Alonso-Ortiz and Leal, 2018[51]; Campos-Vazquez and Knox, 2013[52]; Azuara and Marinescu, 2013[53]; Barros, 2009[54]). However, these papers are based on surveys and suffer from not being representative at the municipality level, where the programme is implemented. An exception on both counts is Bosch and Campos-Vazquez (2014[45]), who used municipal-level social security data. They found that Seguro Popular decreased formal employment in enterprises with fewer than 50 employees. However, using more detailed data and improved econometric methods, Seira et al. (2023[43]) found that Bosch and Campos-Vazquez's (2014[45]) research findings were not robust, and were highly dependent on the municipalities selected, the regression specification used and the identification strategy implemented; changes in any of these items negates their finding that Seguro Popular reduced formal employment In fact, Seira et al. (2023[43]) find no robust evidence of a decrease in formal employment, and also no effects on average salaries for jobs affiliated to the Instituto Mexicano del Seguro Social (IMSS), or the Mexican Social Security Institute, further suggesting that there were no strong shifts in labour supply from the formal to the informal sector. The authors conclude that "the most solid conclusion with the best available data and more robust methods is that Seguro Popular did not decrease the number of formal sector jobs in Mexico" (Seira et al., 2023[43]).

Source: Authors' compilation.

Tax compliance and enforcement play an important role

Increasing tax compliance and enforcement can also be an effective strategy to increase tax revenues for social protection. Evidence shows that taxes are often evaded by misreporting economic activities that are difficult for the government to observe. Improved information collection and information sharing combined with better enforcement can thus increase revenue collection. Increased enforcement efforts are not limited to enterprises and can be complementary to adjusting tax rates in raising tax revenues from individual taxes (Bergeron, Tourek and Weigel, 2023[33]). Several concrete strategies to increase tax compliance have been identified in the literature. Some experiments show that in-person visits and training on formalisation induce enterprises to formalise and can increase government revenue if the interventions are sufficiently well targeted. Using third-party information reports to assist taxpayers in meeting their tax return filing obligations could also allow governments to increase tax revenues, eventually fostering formal employment (Kleven, Khan and Kaul, 2016[32]). Evidence also shows that implementing simple and objective performance-based pay incentive schemes for tax collectors could bridge wider enforcement gaps and help deliver increased tax revenues for the government. Finally, simplifying procedures, e-filing and providing reminders can help levy more revenue when tax evasion is related to a lack of knowledge about when or how to pay the taxes owed (Cohen, 2020[55]). Whether any of these strategies is applicable would have to be assessed at the country level.

Building a taxpaying culture is a crucial prerequisite for mobilising more revenue. Tax systems generally rely on the voluntary compliance of taxpayers (OECD, 2019[56]; OECD, 2022[57]). Although tax audits, fines[9] and third-party reporting can increase tax compliance, tax administration resources are limited, especially in developing countries. Fostering tax morale (i.e. the intrinsic motivation to pay taxes) can play a key role in achieving significant revenue mobilisation. Work by the OECD shows that higher tax morale can typically be linked to taxpayers believing the tax revenues is spent effectively. Combining tax reforms with efficient and effective government spending allows countries to initiate a virtuous cycle of better-quality social protection services and higher tax revenues.

All of these dimensions are taken into account in the OECD Social Protection Tax Revenue (SPTR) framework, a country-specific tool that provides useful guidance in developing a tax reform roadmap for any country (Box 6.4).

Box 6.4. The OECD SPTR framework can help countries identify these appropriate tax measures

The OECD has developed a novel SPTR framework that can identify concrete tax policy measures (and their tax revenue potential) that developing countries could implement in order to close their social protection financing gap.

The SPTR framework is ready for implementation and consists of four modules which are applied sequentially to arrive at a set of tangible and realistic tax policy measures. The advantage of the framework is that it provides: i) the structure, ii) the tools and iii) an initial database based on which country-specific analysis can be carried out. Applying the four modules of the framework leads to a time sequence of country-specific recommendations, whereby the selected tax measures are highlighted in terms of their associated revenue raising potential.

The SPTR framework (financing side) will be jointly implemented with the OECD Social Protection System Review (expenditure side) in order to bring together the financing and expenditure sides of social protection in the form of collaborative country projects that build on the expertise of both the OECD Centre for Tax Policy and Administration and the OECD Development Centre.

Source: Authors' compilation.

Key policy messages

Overall, the evidence presented in this chapter shows that in most developing countries, social protection coverage for workers is often inconsistent and sparse. Formal workers are also better covered by social protection than informal workers, which largely mirrors a coverage gap in contributory schemes and the way informal workers are defined. Extending social protection to informal workers is possible, however. A strategy to extend social protection to informal workers will need to be based on a combination of contributory and non-contributory schemes and incentives to formalise. It will also require a step change in financing strategies.

Non-contributory schemes play a key role in ensuring a basic level of protection within the social protection system. In nearly all developing countries, the extension of social assistance programmes for the poor would cover a large share of informal workers. Extending child benefits and social pensions could also largely benefit workers in the informal economy and their families.

Contributory social protection schemes constitute a key element of the extension of social protection to informal workers. A key challenge to the extension of contributory schemes to informal workers is that a large cohort of such workers do not have co-payment possibilities, and their contributory capacity appears limited overall. The affordability of schemes is particularly challenging for self-employed workers who cannot share the costs. Yet, the scope for employer-employee contributions can be significant for many informal workers, and some of them have contributory capacity at the individual or household level. Moreover, various options exist to improve the affordability of contributions. In addition, for certain types of contributory schemes, such as healthcare or pension schemes, a small share of informal workers could also be covered through formally employed household members.

Closing the global social protection coverage gap, including for informal workers, will require a step change in financing strategies. Reprioritising government expenditure and increasing spending efficiency will not be sufficient to close the substantial social protection financing gaps that can be observed in developing countries, and additional revenues will have to be raised primarily through the domestic tax system. Sustainably funded social protection systems are challenging to build when the level of informal employment is high, but several options exist. Although developing countries will have to mobilise significant additional revenues to finance universal social protection, significant potential exists to increase tax revenue in developing countries, including through well-designed SSCs. Careful tax reforms are needed in order to identify the most suitable tax revenue sources, and tax compliance and enforcement will have to play an important role.

Notes

[1] For example, monotax schemes and others. Further discussion to follow later in the chapter.

[2] Depending on the country, income status used for this report is based on either household income or household consumption.

[3] Co-payment could actually be a possibility for some informal workers classified as own-account workers who may indeed be dependent contractors according to the new ILO definition of employment.

[4] The potential to increase financing of social protection systems through more inclusive social insurance systems is recognised by the *Joint Statement on the Principles for Financing Universal Social Protection* issued by the Global Partnership for Universal Social Protection to Achieve the Sustainable Development Goals (USP2030), which suggests that countries should seek to “increase revenues from social insurance contributions by expanding coverage of social insurance schemes to previously uncovered workers.”

[5] The few informal workers covered through contributory schemes are mostly self-employed persons who opt for voluntary contributions, or persons covered by their spouses (see the previous section).

6 (Packard et al., 2019[58]) assert that social insurance contributions and payroll taxes have a negative impact on formal sector employment" (p. 207). Similarly, the World Bank expresses its concerns that contributions present a "risk of creating incentives for workers to remain in the informal sector" (World Bank, 2022[59]).

7 Of the 16 empirical studies reviewed, 10 find no impact and the others observe an increase in formal employment (1 finds increases only for older women).

8 This argument was most clearly outlined in Santiago Levy's 2008 book on Mexico's social protection system, *Good Intentions, Bad Outcomes: Social Policy, Informality, and Economic Growth in Mexico* (Levy, 2008[46]). Recently, this line of thinking featured notably in the United Nations Development Programme's (UNDP's) 2021 Regional Human Development Report for Latin America and the Caribbean, which declares that "social protection policies contribute to informality" because they "tax formality and subsidise informality" (UNDP, 2021[48]). In the same year, the IMF's report titled *The Global Informal Workforce: Priorities for Inclusive Growth* dedicates significant space to making the case that "payroll taxation on formal sector workers […] increase[s] the cost of doing business and create[s] double taxation of labour, thus encouraging informality. Further, means-tested benefits […] generate severe disincentive effects and often create poverty traps" (IMF, 2021[47]).

9 Or, on the contrary, amnesty programmes for evaders (Londoño-Vélez and Ávila-Mahecha, 2021[60]).

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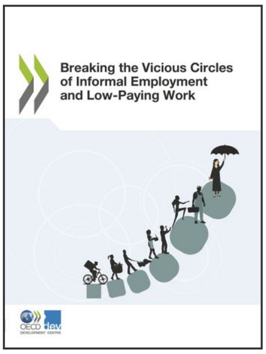

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