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'Accelerating the achievement of gender equality and the empowerment of all women and girls by addressing poverty and strengthening institutions and financing with a gender perspective'

Expert Group Meeting

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Gender, Taxation and the Informal Sector

* The views expressed in this paper are those of the authors and do not necessarily represent those of the United Nations.

Gender, Taxation and the Informal Sector

Framing the issues

Tax justice has recently become a key part of the development agenda. High profile discoveries such as the 'Panama papers', greater awareness of the breadth and depth of illicit financial flows, and a general desire for greater accountability have focused attention on issues of fairness and equity in taxation (Keen, 2008, 2012; Sampere, 2018). Much of the advocacy and research work on tax justice has been aimed at the national and international levels and, in particular, on whether large multinational companies (often in the fossil fuel or mining industries) are meeting their tax obligations to their host countries. This is important for efforts to achieve gender equality and to narrow the gender poverty gap. More precisely, the redistribution of both the burden and benefits of taxation in developing country context requires a more gendered lens.

Related to the above, somewhat less attention has been devoted to tax justice at the local government level and on how local issues of tax can be linked with the broader international tax justice movement (Sampere, 2018). For many informal workers across the Global South, concerns with the proliferation of tax havens or tax breaks granted to large multinational companies are far removed from the realities of their daily experiences with taxation (Sampere, 2018). This is important since 61% of the world's workers are in informal employment and, among developing countries such as those in Sub-Saharan and Western and Eastern Africa, 89% and 92%, respectively, of employment is informal (ILO, 2018). This is not to suggest that global tax justice is not important. Tax justice at all levels- international, national and local- is at the core of principles of social justice, equity and sustainable development.

In broad terms, tax justice refers simply to fairness and equity. A key feature of tax equity is that all taxpayers pay their fair share and that wealthier individuals (and companies) pay more[1]. Tax equity, in large part, refers to the tax rate or the proportion of income that individuals and companies pay in tax. Policy debates, and particularly those that relate to informal workers often concern discussions of flat taxes (with no concern for percentage of income) and methods of progressive taxation (where the tax rate increases for higher income earners). Moreover, these tax issues are particularly relevant for 'local' tax justice and, as such, also hold the potential to impact meaningfully on the livelihoods of women informal workers in cities across the Global South.

Mobilising revenue

One of the most notable shortcomings in the tax structures of developing countries is the low level of personal income tax. Personal income tax, on average, accounts for only about 10 per cent of total tax revenue in developing countries (compared with an average of 25 per cent in developed countries)[2] and this is largely through the taxation of employees from the public sector and large private firms (Keen, 2012: 10). Against this backdrop, the need for revenue mobilisation is, arguably, the main motivation for taxing the informal sector in most developing countries. The International Monetary Fund argues that a widening of the national tax net to include the informal sector is key to improved 'revenue mobilization' (IMF, 2011). It estimates that, on average, developing countries need to increase their tax to GDP ratios by about four percentage points in order to meet their development objectives and current infrastructure needs (2011: 4). These pressures have only increased since the COVID pandemic and much of the recent evidence suggests that progress towards poverty reduction has stalled or been reversed.

[1] This is an example of **vertical equity**- i.e. where the concern is with redistributing income within society. In taxation terms it means that people with higher incomes should pay more tax. **Horizontal equity** is concerned with treating people in an identical situation in the same way. Put simply, taxpayers who earn the same amount of income should pay the exact same amount of tax and there should not be discrimination in terms of race, gender, class or type of work. Workers in the informal sector should, therefore, not pay more (or less) tax than workers who earn the same income in the formal sector.

[2] In some respects, however, this is a false equivalence as the structure of the economy in developing countries is very different to high income countries. Most developing countries with low tax to GDP ratios, for example, also have low per capita incomes, a low ratio of international trade to GDP and high levels of agricultural activity (Moore, 2014).

In the context of post-pandemic economic crises, countries around the world face increasing fiscal pressures. In 2021, the IMF[3] estimated that low-income countries alone would need at least USD200 billion to recover to pre-pandemic levels and an additional USD250 billion to make any progress towards catching up with income levels high-income countries. At the same time, the pandemic has exposed shortfalls in social protection coverage and particularly for workers in the informal sector. The financing of adequate social protection floors, while crucial, will place an additional strain on low-income countries with low levels of personal income tax (PIT). Coupled with this, national debt levels in 2020 increased by 12 per cent in low-income countries to a record level of USD860 billion[4]. In seeking to fill revenue gaps, policymakers in a number of countries have had an increasing incentive to find new tax revenues – with some now looking toward the informal sector through presumptive tax regimes (PTRs).[5]

Also known as simplified tax regimes, presumptive tax regimes (PTRs) levy taxes on 'presumed' income in contexts where it is difficult or impractical to observe actual levels of income or turnover—in particular, as with micro and small businesses in the informal sector in low- and middle-income contexts. These regimes are used in many low- and middle-income countries where a large share of employment (and particularly womens' employment) is in the informal sector. Presumptive tax rates tend to be lower than in the standard tax system (e.g. PAYE) and often vary depending on the size, location, or sector of the firm. However, there are so far relatively few guidelines for best practices or empirical evaluations of presumptive tax regimes in low-income contexts. This is surprising both given their widespread usage and the indications that they have often been accompanied by severe practical challenges. Perhaps most critically, presumptive tax regimes are 'gender blind' in their design. If a particular segment, such as market trading, of a country's informal economy is dominated by women, then the presumptive taxes scheduled for market traders will not only be regressive but also gender 'unequalising'.

This note draws on a recent study of informal sector taxation through a large and geographically representative survey of the informal sector in Ghana's capital city, Accra[6]. In Accra, small informal activities are taxed at the national level by a presumptive tax through the "tax stamp", where informal sector operators pay a fixed tax per quarter. This is designed with a progressive rate schedule that differentiates by category and size of business. At the same time, local governments collect a range of payments from informal businesses. These fall largely into two types. The first set of payments varies the rate of payment by category and size of the enterprise; this includes, most notably, business operating licences. The second type are fixed fees payments that are levied regardless of income or type of economic activity. This includes, for example, the "daily toll", which is paid predominately by market traders or traders operating in the immediate vicinity of urban markets. The gendered differences in taxation are outlined below with a particular focus on the burden of taxation.

Gender and employment in Accra's informal sector

In Accra, as in many other Sub-Saharan African contexts, women are disproportionately represented in the informal sector. In the survey of informal sector operators, women account for about 74% of informal activities and are particularly concentrated in sectors such as market trading. This means that, where informal sector taxes (as outlined above) are regressive, women are disproportionately affected. Moreover, within the informal sector in Accra, women and men work in different occupations and sectors. As Figure 1 below demonstrates, women are far more likely (62.8%) to work in the trade sector which is largely dominated by retail. Street vendors and market traders are the most prevalent occupations within this sector. At the same time, men are far more likely to work in manufacturing (42%) and the services sector (31.4%) than women.

[3] IMF. 2021. "Cameroon Article IV Consultation." IMF Country Report 22/75. IMF.
[4] World Bank. 2021. International Debt Statistics 2022. The World Bank. https://doi.org/10.1596/978-1-4648-1800-4.
[5] African Caucus. 2023. "The Sal Declaration." African Governors of the IMF and the World Bank Group. https://africancaucuscaboverde.gov.cv/api//uploads/The_Sal_Declaration_67775ca17a.pdf.
[6] https://www.wiego.org/sites/default/files/publications/file/working-paper-45-taxation-socialprotection.pdf

Figure 1: Industry group disaggregation in Accra's informal sector, by gender

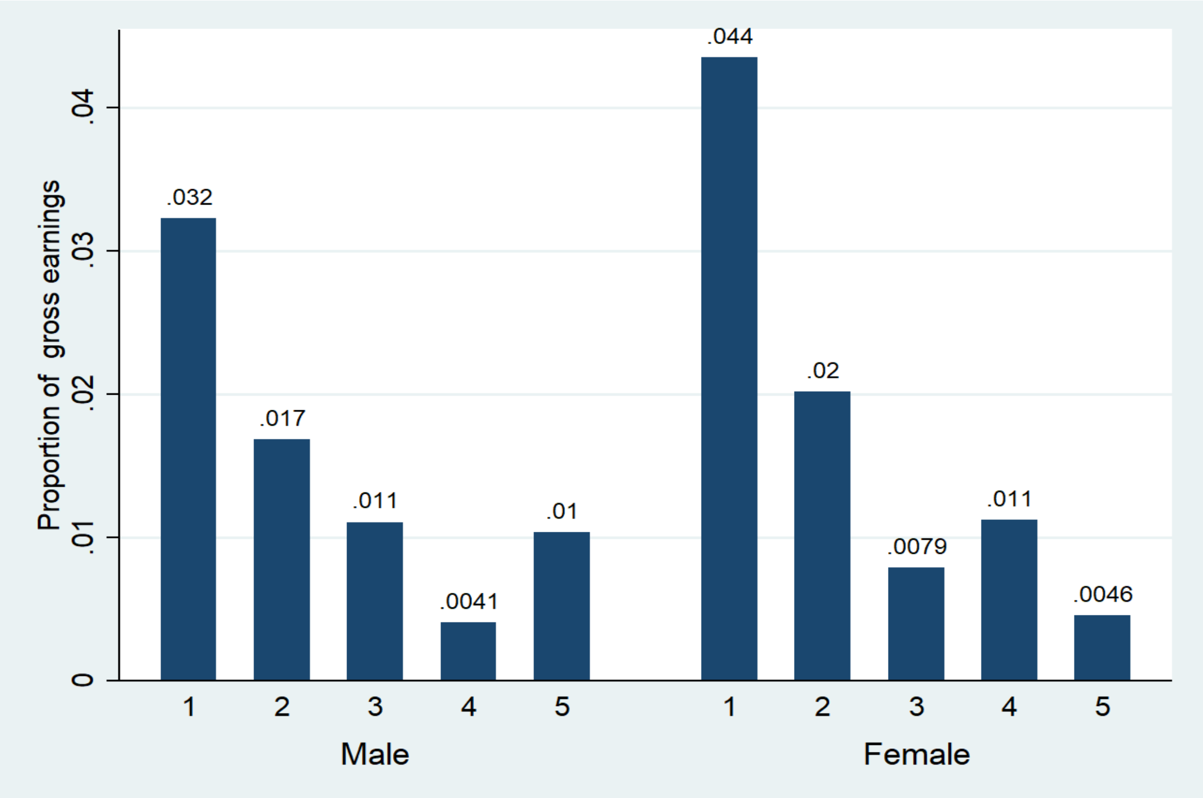
Notes: The data are weighted. Source: Authors' calculations from the WIEGO/ICTD/ISSER Informal Sector Taxation Survey (2022)

These gender differences in occupations and sectors matter a great deal for taxation. Taxes such as the daily toll and payments such as market fees and licenses are more common in the trade sector where women are over-represented. The result is that the design of Accra's tax system (both local and national) is gender blind since women are over-represented in sectors in which specific taxes are more prevalent.

Gender and tax regressivity

Figure 2 below shows how the structure of taxation in Accra's informal sector differ between women and men. Again, keeping in mind that roughly 75% of Accra's informal sector operators are women, the result is that taxes are a larger burden for women than men. Among the lowest earners (quintile 1) men pay about 3.2% of their gross (pre-tax) earnings on taxes while the lowest earning women pay about 4.4%. For both women and men, the tax structure is regressive in that the higher earning informal sector operators pay a smaller share of their earnings in taxes.

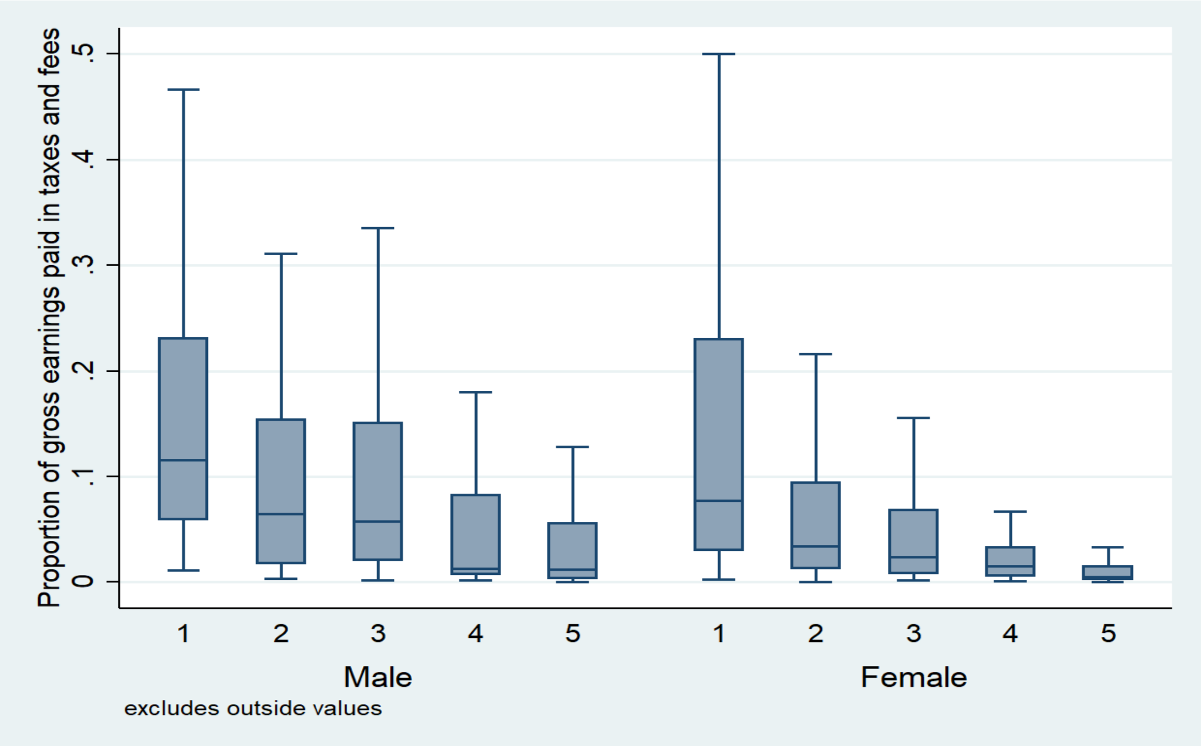
Figure 2: Relative tax payments in Accra's informal sector, by gender and earnings quintile



Notes: The data are weighted. Source: Authors' calculations from the WIEGO/ICTD/ISSER Informal Sector Taxation Survey (2022)

The data in Figure 3 show what happens when the picture is 'widened' to include a broader range of taxes and tax-like fees and payments. The broad pattern of regressivity is evident for both women and men with women in the lowest earning quintile paying up to 50% of their gross earnings in taxes and fees. These estimates suggest that the Ghana Revenue Authority's aim of achieving a highly simplified tax system has resulted in a fragmented and regressive tax structure which places a large burden on the lowest earners in the informal sector- and women, in particular. Moreover, these taxes are paid on top of user fees, licenses and operating permits and, to a much lesser extent, informal taxes and payments. The result is a clear case of over-taxation since the first quintile should not be paying any taxes based on any conceivable tax threshold (e.g. the PAYE tax table).

Figure 3: Relative tax payments in Accra's informal sector, by gender and earnings quintile



Notes: The data are weighted. The box plot identifies the minimum, first quartile (p25), median (p50), third quartile (p75), and maximum values. Source: Authors' calculations from the WIEGO/ICTD/ISSER Informal Sector Taxation Survey (2022).

Towards a gender equitable tax justice

Achieving the objective of 'strengthening institutions and financing with a gender perspective' requires a careful analysis of the distribution of both the burden and benefits of taxation. This note is concerned with the former and, in particular, with the way in which taxation tends to be gender blind when governments design tax systems for workers in the informal economy. Since informal employment is the dominant mode of employment, both globally and in developing country contexts, the taxation of informal workers is an important tool in poverty reduction and the narrowing of the gender poverty gap.

In particular, presumptive tax regimes, while increasingly popular in many low- and middle-income countries, require careful design in order to avoid a number of common pitfalls. First and foremost, PTRs should not be seen as tax instruments that can uncover a 'hidden goldmine' of revenue from the informal sector. Relatedly, the design of these regimes should not place an unnecessary tax burden on the lowest earners, many of whom are 'survivalist' in nature, in the informal sector. Moreover, in contexts such as Ghana where women are often over-represented in sectors which are over-taxed, the design of tax regimes have important implications for gender equality.

Some of the key lessons from the Ghana context suggest that PTRs should be designed so that they are not implemented 'on top' of local or city level tax regimes. One tangible recommendation would be to introduce a threshold to protect the lowest earners or, where identifying an appropriate threshold is not practical, presumptive rates could be set at very low levels. The Accra example also suggests that there is substantial scope for linking national tax registration with social security or health care so that the tax system offers a clear incentive for 'formalisation'. Both of these recommendations emphasise the need to avoid high tax burdens, particularly for the lowest earners who are often below the poverty line, while also offering a clear advantage in tax registration. Since women are often the beneficiaries of social protection, social spending and public services, linking taxation with these benefits could also be important for financing the narrowing of the gender poverty gap.

More broadly, there is a clear need for further research on the optimal design of PTRs in different contexts. This gap is likely to become increasingly important as the pressure for domestic resource mobilisation intensifies due to the growing levels of public debt in many low- and middle-income countries. The goal of better designed PTRs, in turn, requires more regularly collected and better sources of data to give policymakers the right information to make decisions about the design of presumptive tax regimes and their implications for gender equitable poverty reduction.

How to Design Fair and Effective Tax Policies for the Informal Economy

Informal workers are often willing to pay taxes if they are fair and transparent and if they receive something in exchange. While there is no one-size-fits-all solution to designing a good tax policy, the following principles and approaches, can help guide local governments and tax authorities.

1) **Understand the status quo, and particularly how women informal workers are taxed currently**: In structuring informal sector taxation policies, a careful analysis of gender, existing sources of taxation (both direct and indirect), heterogeneity in earnings within the informal economy, including between women and men, and the requirements of a progressive presumptive tax rate is required. Without understanding the existing structure of taxes, it is not possible to introduce new taxes on the informal economy in a fair and transparent way.

2) **Ensure that workers understand where their tax contributions go**: For many informal workers, the lack of public services in exchange for their tax contributions to local government revenues threatens tax compliance, undermines productivity and earnings and erodes the social contract. There is evidence that one of the main reasons that workers do not pay the taxes that they owe is because they do not receive anything in return. Particularly where workers are taxed in public spaces such as markets, it is important to ensure that tax contributions are used to maintain infrastructure and ensure access to basic services.

3) **Ensure that informal workers are involved in tax policy design**: Involving informal workers themselves is important in the design of tax policy which is both progressive and can improve the social contract between local government and urban informal workers. Research has shown that where worker's organisations are involved with the collection of taxes, compliance and tax morale are high.

4) **Protect the most vulnerable workers (often women)**: It is typically the most vulnerable groups of workers, often women, who are unable to avoid corruption, tax harassment and multiple taxation. Tax systems which target the most vulnerable workers are unlikely to be successful and will undermine the trust between tax authorities and workers.

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