



POVERTY AND FREEDOM

RESEARCH REPORT



RESEARCH TEAM

Written by:

Luis Colmán Allende – Fundación Paraguaya

Noelia Téllez – Fundación Paraguaya

Collaboration:

Cecilia de la Guardia – Duke University

Laura Searcy – Tulane University

Diana Vázquez – Universidad Nacional de Asunción

Review:

Nancy Ramos – Fundación Paraguaya

Lourdes Agüero – Fundación Paraguaya

Translation:

Carolina Mussi – Fundación Paraguaya

Victoria Peroni – Fundación Paraguaya

Cecilia de la Guardia – Duke University

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FORMALIZATION OF MICROENTERPRISES IN PARAGUAY

MULTICASE STUDY. 2021.

ABSTRACT

Informality is related to multiple factors, some of them transversal to the different contexts, and others specific to a particular type of economic unit, in this sense, it is complex for the government to design and implement public policies aimed at the heterogeneous group of independent micro-entrepreneurs. For this reason, the main objective of this report is to identify the barriers that affect microenterprises, taking into account the diversity of characteristics and circumstances of these economic units. Through this objective, we seek to combine formalization incentives that promote the benefit of entrepreneurial potential as a means to achieve the economic empowerment of vulnerable populations. The methodology used is the descriptive social study, mainly based on field research and complemented by documentary research. The investigation reached a descriptive level and the approach used is the mixed concurrent triangulation design. The main result of the study is that formalized companies enter the formal economy due to external pressures such as the client's demands and not so much for the benefits that formality provides. Therefore, policies that encourage formality through the promotion of such benefits may not be sufficiently effective for those firms whose level of productivity and competitiveness are low. Given the evidence that businesses become formal as they grow, it is recommended that policies be applied to promote improvements in the capabilities of microentrepreneurs, which could generate a significant improvement in business performance that would translate into their entry to the formal economy in the medium or short term.

I. INTRODUCTION

The consideration of the informal economy as a relevant issue has its background in the Philadelphia's Declaration in which it is established that "all human beings, irrespective of race, creed or sex, have the right to pursue both their material well-being and their spiritual development in conditions of freedom and dignity, of economic security and equal opportunity" seeking to deal with the great number of workers and companies that are often not recognized nor protected by judicial and regulatory frameworks (ILO, 2002). This implies for workers a lack of social protection, work rights and decent working conditions; for companies, low productivity, and lack of access to credit, and for the government, impacts on public revenues, the scope of the government action, the consistency of institutions and fair competition (Bonnet & Leung, 2021) resulting in a high degree of vulnerability and poverty (ILO, 2002). Even though not all informal workers are poor, poverty is a cause and a consequence of informality.

Informality is related to multiple factors, some of them are transversal to the different contexts such as deficient public entities and inappropriate macroeconomic frames, while others are specific to an economic unit: microbusiness; groups of workers; or employer's categories (ILO, 2019). Considering the latter, in Paraguay, until 2018, of the 870,598 economic units, 844,481 (97%) are microbusinesses, of those 607,492 (72%) are informal. Of the total economic units, 329,620 (37,86%) are self-employed of which 89,7% are informal (DGEE/MIC, 2018) (Annex 1-3).

Therefore, the design and implementation of formalization policies for the government is complex due to significant heterogeneity in the group of the self-employed, because it is made up of employers and self-employed workers with different levels of qualification and income-generating capacities (Bertranou, et al., 2011). As a result, the transition from the informal economy to a formal economy needs to take into account the diversity of characteristics, circumstances and needs of workers and economic units, as well as the need to address this diversity through specific approaches, as established in the "Transition from the Informal to the Formal Economy Recommendation, 2015 (no. 204)" (International Labor Conference, 2015).

For this reason, the objective of this research is to identify the barriers that affect microenterprises in achieving formality, so that through this information, a balanced approach can be established that combines incentives and measures for compliance with legislation, as well as the use of entrepreneurial potential, creativity, dynamism, labor competitiveness and innovation capacity of workers and economic units in the informal economy.

In order to achieve the objectives outlined, and taking into account the importance of social dialogue as an indispensable tool for proposing policies to address informality, the gathering of data has been carried out through participatory methodologies such as focus groups in 10 cities around the country.

As the most important limitation at the time of data collection, the difficulty for all focus group participants to comply with the characteristics established in the research protocol stands out, especially considering the criteria of what is considered formal. Nevertheless, the diversity among the group members brought to the research different perspectives of the different actors of society that provided content to the research task.

The relevance of this research is that the information provided will serve as an input for public policy makers, public or private institutions, organizations and all actors involved in the implementation of strategies to promote formality.

The structure of the report consists of 6 parts, beginning with a theoretical review of informality and its implications, followed by the normative framework that regulates the population studied, the methodological design, then the presentation of the results, which consists of two divisions and subdivisions, where the empirical evidence is observed on the one hand and the bibliographical review of the case studies on the other, followed by the conclusions and finally the recommendations.

II. CONCEPTUAL FRAMEWORK

It is a fact that the term informality and therefore the people who develop their activities under this modality called "informal", are commonly associated or related to small economic units that border on subsistence economy. However, in practice, according to (Rosenbluth, 1994) informality covers from those small forms of commerce and services to those that generate income even higher than salaried workers.

The first theoretical definition of informality was established in the “Resolution and conclusions concerning decent work and the informal economy”. Adopted by the 90th session of the International Labour Conference (2002), which states that: “Informal economy refers to all economic activities by workers and economic units that are – in law or in practice – not covered or insufficiently covered by formal arrangements” (ILO, 2002).

The document states that informality cannot be associated with a sector of the economy since it is transversal to different companies and workers in different sectors, therefore the term "informal economy" is preferable to "informal sector". Furthermore, this definition was expanded in the "ILO Recommendation concerning the transition from the informal to the formal economy, 2015 (No.204) (ILO, 2015), which states that the term does not cover illicit activities, and that within economic units are included: a) units employing labor; b) units belonging to self-employed persons, either alone or with the help of unpaid auxiliary family workers; and c) cooperatives and units of the social and solidarity economy.

Now, from the point of view of employment, informal employment refers to jobs, in the informal or formal economy, that are not covered by labor regulation, taxation, social protection or other labor benefits (ILO, 2019). That said, the independence between the formality of economic units and informal jobs is evident.

In Paraguay, the definition of informal employment or informal occupation adopted by the National Statistics Institute (INE in Spanish) includes the following: (a) public employees and workers who do not contribute to the retirement or pension system; (b) private employees or workers who do not contribute to the Retirement or pension system, regardless of the status of the company where they work; (c) employers whose company is not registered in the Taxpayers Identification Number (RUC in Spanish) of the Treasury; (d) self-employed workers whose company is not registered in the Taxpayers Identification Number (RUC) of the Treasury; (e) unpaid family workers: Whether or not the company where they work has a RUC ; and f) domestic employees who do not contribute to the retirement system (Bonnet & Leung, 2021).

For research purposes and given the characteristics of the participants of the focus groups being employers, self-employed or unpaid family workers, the criterion of formality will be defined as the registration in the single taxpayer registry, since most of them do not have employees. Since this is considered the first stage (or instance) of formalization, to look at informality from the tributary point of view is the first step to understand the complexity of the issue. Likewise, in this report we will briefly mention informality from the employment point of view, since it also has a negative impact on social welfare.

III. LEGAL FRAMEWORK

This section details the different regulations related to the population under study, in this case MSMEs, as well as the different strategies adopted by the different Ministries that have within their scope of action the fight against informality.

First, Law 4,457/12, for micro, small and medium-sized enterprises (MSMEs), which aims to promote their creation, development and strengthening, to include them in the structure of the Ministry of Industry and Commerce, as a Vice – Ministry to regulate them and incorporate them into the formal structure producing goods and services, taking into account their potential as an engine of growth for the country.

Relevant points arising from this law include:

- Parameters for the categorization of MSMEs, based on the number of workers employed and the amount of annual gross invoicing, carried out in the previous fiscal year. (It is worth mentioning that Decree 3,698/20 updates the quantitative parameters of the amount of annual invoicing in correspondence with the accumulated variation of the consumer price index),
- The creation of the Vice-Ministry of Micro, Small and Medium Enterprises (MIPYMES in Spanish), which will be in charge of coordinating, systematizing and executing support policies for the creation, promotion, strengthening, management, technification and development of MSMEs, among other functions,
- The simplification of procedures for the opening and registration of MSMEs, in order to reduce costs and bureaucratic requirements,
- Benefits within the tax regime, for micro-enterprises, which will be able to exercise their commercial activity with a basic accounting system, with exemption from the obligation to have accounting record books and certain taxes, and for MSMEs in general with differentiated taxes.
- The financing and financial support mechanisms for MSMEs, such as: preferential credits, the establishment of a basic budget within the General Budget of the Nation, with accumulable resources in an operating fund called FONAMYPE, among other alternative means of financing.
- Fixed-term employment contracts, which micro and small enterprises may benefit for a term of up to twelve months, renewable for an equal term, and at expiration they can be terminated without the obligation to give prior notice or indemnification, and including, for micro enterprises, the payment of salaries on a basis of not less than 80% (eighty percent) of the legal minimum salary established for unspecified diverse activities, during the first three years counted from their formalization, all of this within the labor regime.

The Social Health Insurance of the Social Security Institute is mandatory for MSMEs under the social security system established for all companies in the country and their employed dependent workers.

The Law 4,933/13 authorizes the voluntary incorporation of self-employed workers, employers, housewives and domestic workers to the social security - Retirement and Pension Fund of the

Social Security Institute. The beneficiaries of this law are those who will contribute to the Social Security Institute 13% (thirteen percent) calculated on a taxable base not less than the value of 1 (one) legal minimum wage for unspecified diverse activities, being able to receive long-term benefits for advanced age and for disability and survival.

The Law 4,986/13 which creates the Unified System of Business Attention for the Opening and Closing of Companies (SUACE in Spanish), in order to facilitate, accelerate and make transparent the processes of opening and closing of companies, through a mechanism by which the applications for registrations, legally required of all commercial companies, will be processed.

The Law 5,628/16 creates the Guarantee Fund for micro, small and medium-sized enterprises, in order to improve access to credit for formalized MSMEs, generators of employment and wealth creators. To grant additional and/or complementary guarantees when those offered by MSMEs are insufficient at the discretion of the entities that grant credit to them.

Subsequently, Law 5,656/16 on the Promotion of Entrepreneurial Culture was enacted, which aims to promote the entrepreneurial spirit and culture in all educational levels of the country and to establish the instruments to carry out the research, development and sustainability of entrepreneurial projects, creating support, economically and financially. And through the creation of the National Office of Entrepreneurship (DINAEM in Spanish) and the National Registry of Entrepreneurs under the Ministry of Industry and Commerce and the Vice-Ministry of MSMEs should, among other important functions, promote innovative ideas and projects that arise from entrepreneurs, seek investors who want to stake in entrepreneurial projects, generate conditions with concrete proposals for the emergence of angel investor funds, seed capital funds and risk capital funds to support new ventures.

In addition, the need to promote activities such as: Youth Job Fairs, Business Rounds for new entrepreneurs, Business Contests for social and commercial entrepreneurs and others. To provide the Ministry of Education and Culture (MEC), Universities and Higher Education Institutes with the necessary tools for the implementation of the promotion of entrepreneurial culture, entrepreneurship and technological innovation with constant training for educators. Also, to articulate these tools for the educators of the Ministry of Labor, Employment and Social Security, the National System of Professional Promotion (SNPP in Spanish), and the National System of Labor Education and Training (SINAFOCAL in Spanish).

Law 5,741/16 establishes a special system of benefits from the social security system (Instituto de Previsión Social, IPS) to micro-entrepreneurs, with the purpose of incorporating into the system the owners and/or those responsible for a Micro-enterprise, which as of the effective date are not yet registered in the Social Security administered by the Social Security Institute (IPS). All this in a joint program for the formalization and regularization of unregistered micro-enterprises.

In order to improve the country's tax system, Law 6380/19 on the modernization and simplification of the national tax system was enacted to facilitate the formalization of MSMEs through the establishment of simplified system for the liquidation of the Corporate Income Tax (IRE in Spanish) for the taxpayers of this sector according to their level of invoicing. The simplified regimes are:

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- Simple Regime, for taxpayers whose annual turnover does not exceed G. 2,000,000,000, the same liquidation criteria are used as those established in the current Small Income Taxpayer; and
 - Resimple (Very Simple) Regime, for taxpayers whose annual turnover does not exceed G. 80,000,000, it is settled by paying 0.1% of their income on a monthly basis. Resimple taxpayers do not pay tax (IVA) and will issue sales slips for their operations.

Law 6480/20, which creates the Simplified Joint Stock Company (EAS in Spanish), completes the legal regulations that support the sector, with the main objective of promoting the formalization, simplification and modernization of the administrative management as well as the reduction of the cost for the start up.

In summary, the laws that specifically affect MSMEs are:

1. Law 2,051/03 on Public Procurement, Article 7.
2. Law 4,457/12 for micro, small and medium-sized companies (MSMEs).
 - a. Decree No. 3,698/20 updating the quantitative parameters of the amount of annual turnover, for the purposes of the categorization of micro, small and medium-sized companies, established in Article 5 of Law 4,457/12.
3. Law 4,933/13 which authorizes the voluntary incorporation of independent workers, employers, housewives and domestic workers to the Social Security - Retirement and Pension Fund of the Social Security Institute.
4. Law 4,986/13 which creates the Unified System of Business Attention for the Opening and Closing of Companies (SUACE).
5. Law 5,628/16 which creates the Guarantee Fund for micro, small and medium-sized companies.
 - a. Law 6,579/20 which amends articles 1,3,8,9,10,12,16 and 17 of Law 5,628/16.
6. Law 5,741/16 which establishes a special system of benefits from the social security system (Instituto de Previsión Social, IPS) to micro-entrepreneurs.
7. Law 5,656/16 on the Promotion of Entrepreneurial Culture.
8. Law 6.380/19 on modernization and simplification of the national tax system.
9. Law 6.480/20 creating the Simplified Joint Stock Company (EAS).

IV. METHODOLOGY

4.1. Research type

This report used the descriptive social study method since it seeks to specify properties, characteristics and important profiles of the social groups in question working on factual realities (Gallardo, 2017). This was done with the objective of investigating incidences and values in which one or more variables are manifested to locate, categorize and provide the vision of a community, an event, a context, a phenomenon or a situation. For this purpose, the field modality was used and, in order to complement the research and provide theoretical support to certain economic and social phenomena, so was the documentary-bibliographic modality. The level reached corresponds to descriptive research and the approach used is the mixed approach of the concurrent triangulation type, in which both qualitative and quantitative data have equal priority and whose integration occurs in the data interpretation stage.

4.2. Data Collection

In regards to data collection, primary sources of information were used: semi-structured questionnaires, with open and closed questions, referring to characteristics, circumstances and needs of these workers and their corresponding economic units, as well as the motivational aspects regarding their incorporation into the formal economy and possible obstacles. These were applied through group interviews carried out in 10 cities of the country (See Annex). The secondary sources were based on written documentary reviews of local official institutions such as the National Statistics Institute (INE in Spanish), the Ministry of Industry and Commerce (MIC in Spanish) and international organizations such as the International Labor Organization (ILO) and the World Bank (WB).

4.3. Participants

The number of participants consisted of 88 people divided into groups of between four and twelve. The duration of each meeting was approximately 45 minutes and the instruments used were an interview guide and audio recordings via cell phone.

4.4. Content Analysis

For qualitative data analysis, the NVIVO software was used, which allows coding of cases and identification of patterns and relationships between variables. For quantitative data and databases' analysis, SPSS statistical software was used for the microdata of the Continuous Permanent Household Survey and MS Excel for smaller databases.

The structure of the report consists of a previous literature review of each section, followed by empirical evidence provided by the fieldwork.

V. RESULTS

5.1. Socioeconomic characterization, entrepreneurial motivation and entrepreneurial performance

5.1.1. Findings

5.1.1.1. Group interviews

The members of each group interviewed are clients of the Fundación Paraguaya organized in communal banks, mostly low-income and self-employed, whose main motivation for entrepreneurship is unemployment, the need to generate additional income for their families, and the possibility of economic independence. These enterprises are mostly led by women with a low level of education, who are engaged in part-time economic activity and whose business operations are carried out from their homes. They then combine these jobs with housework or other jobs with fixed remuneration. These enterprises do not have employees, and if they do, they are family members or people hired on a seasonal basis in case there is a high demand for products.

The economic activities they carry out are quite diverse, most of them are dedicated to the purchase and sale of products of various items, such as clothing, footwear, food (groceries), beverages (bodegas), personal care (perfumes and cosmetics), and cleaning products. Among those engaged in productive activities, food processing (catering services) stands out, followed by craftswomen, garment makers, women engaged in agriculture and poultry raising (sale of chickens and homemade hens), fish farming, and carpentry. In the area of services, the following stand out: decoration and rentals, hairdressing and body esthetics (massages and physiotherapy), and domestic and professional services. All of which were strongly affected by the pandemic due to sanitary restrictions.

This type of enterprises' characteristics coincides with what the FEPAME (2010) considers as survival microenterprises: those that have very low productivity and only pursue the generation of income for immediate consumption purposes; they work on the logic of survival.

An equally important fact is that many of the enterprises considered in the group interviews were affected by the economic crisis generated by the COVID-19 confinement measures; some of them had rented physical premises and were forced to move their businesses to their homes to reduce costs, others have definitively closed down their activities and changed their line of business, while others have decided to start up businesses as a result of unemployment.

When these microentrepreneurs were asked about the greatest challenges faced in carrying out their businesses, the majority responded that the main barrier is insufficient capital, which in turn prevents them from having the infrastructure and scale necessary for their businesses to become competitive in terms of costs, delivery times, installed capacity, logistics, and more. They also pointed out that while credit is a barrier, so are payment terms, since given the characteristics of the businesses they carry out, it is difficult to meet deadlines and interest rates are high.

Another obstacle pointed out by participants are the difficulties in managing their businesses; many of them say that "they do not see the profits", others that their costs are very high and that the profit margin is low. In addition, they expressed the need for training courses in various areas.

Another group stated that there is insufficient demand for their products and the need to enter new markets, especially those involved in handicrafts.

5.1.2. Literature Review

Barron (2020), who mentions Gindling & Newhouse (2012), state that in low and middle income countries, self-employed workers represent the absolute majority, and that they opt for this modality out of necessity and due to the lack of opportunities in salaried employment. This means they are rarely prepared with the necessary skills to carry out their businesses, which translates into low profits and limited growth opportunities, a situation that reduces them to the informal sector.

In fact, Gindling & Newhouse (2012), through a compilation of case studies, distinguish two types of microentrepreneurs: the innovative and successful entrepreneurs with higher growth potential and ambition and the less successful self-employed. This study reveals that successful entrepreneurs are mostly older people, with higher levels of education, likely to work in retail and services. On the other hand, they distinguish two types of unsuccessful entrepreneurs in several West African cities, the first type have the same profile in terms of age, education and sector of work as the more successful entrepreneurs, however, they do not possess significant capital. The authors attribute that the lack of success in this case is due to personal and environmental constraints, such as inadequate skills and experience, access to capital, or physical infrastructure. The second type of unsuccessful self-employed business-owners do not share the same characteristics as successful entrepreneurs, so they are constrained by their age, education, sector of work, unobserved characteristics of their work, skill set and the external environment.

Nevertheless, Koellinger & Block (2009), through empirical evidence studies on entrepreneurial motivation establish 3 important conclusions:

- 1) There is a strong association between financial success and satisfaction with start-up which suggests that financial motives are an important incentive for people to engage in entrepreneurship;
- 2) Entrepreneurs who started their business after a long period of unemployment and due to a lack of better job alternatives (necessity entrepreneurs) are significantly less satisfied with their start-up, if the decision was made as a result of an exercise of free will, entrepreneurs are significantly more satisfied, therefore, the circumstances leading to the start-up decision influences the satisfaction of nascent entrepreneurs;
- 3) There is a procedural utility in which individuals show higher levels of satisfaction with the start-up if they have achieved a certain high level of independence and creativity.

Therefore, an important reason for people to start their own business seems to be the possibility of achieving self-realization and self-determination. For these people, the "path" seems to be the "goal" as these entrepreneurs extract utility from their work, beyond the utility they obtain from the monetary rewards of their enterprise.

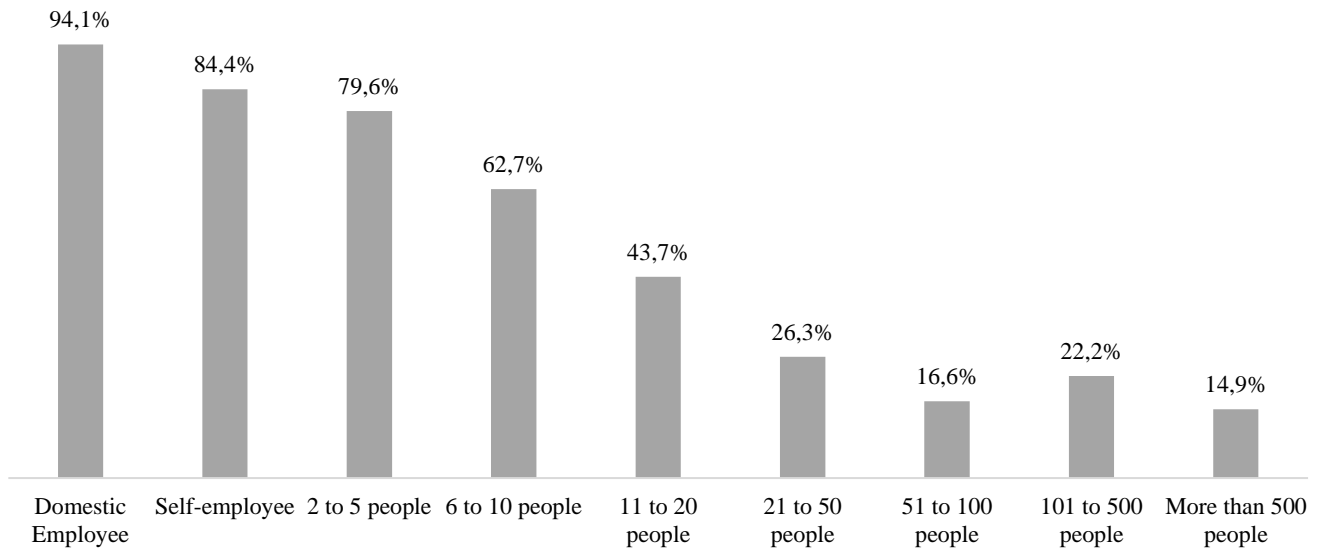
5.2. Formality

5.2.1. Findings

5.2.1.1. Macroeconomic Data

From the point of view of employment, Graph No. 1 shows that informality falls as the size of the companies grows. Since employees in the domestic and self-employed sectors belong between 80 to 90% to the informal sector, this figure decreases as the companies have more employees, reaching 14.9% in those with more than 500 employees.

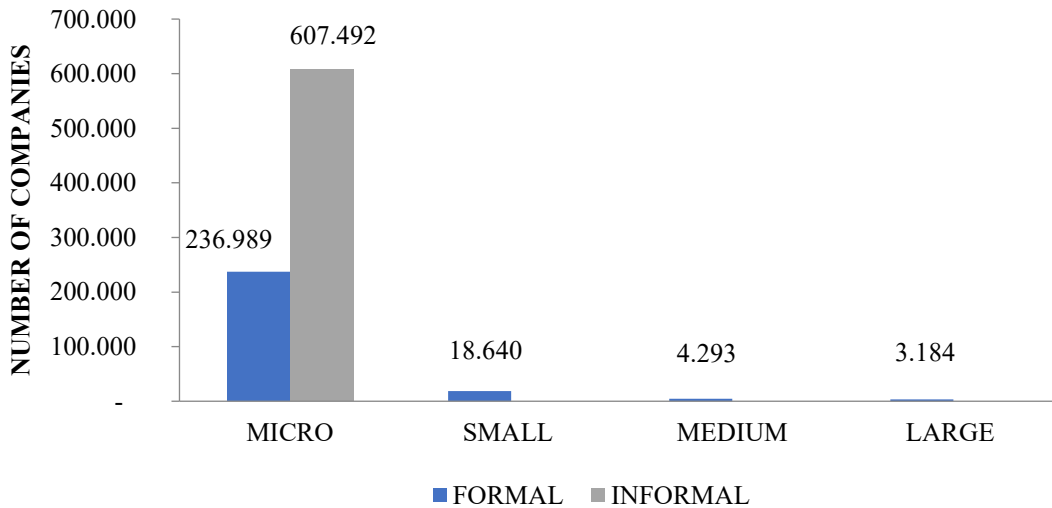
Graph N° 1: Population 15 years of age and older in informal non-agricultural occupations, by company size. Year 2020.



Source: Own elaboration based on (INE, 2021).

On the other hand, from a tax point of view, as shown in Graph N° 2, of the 844,481 existing micro-enterprises for 2018 (See Annex), 607,492 representing 72% are informal, while in larger companies such as small, medium and large, there is no informality in terms of RUC.

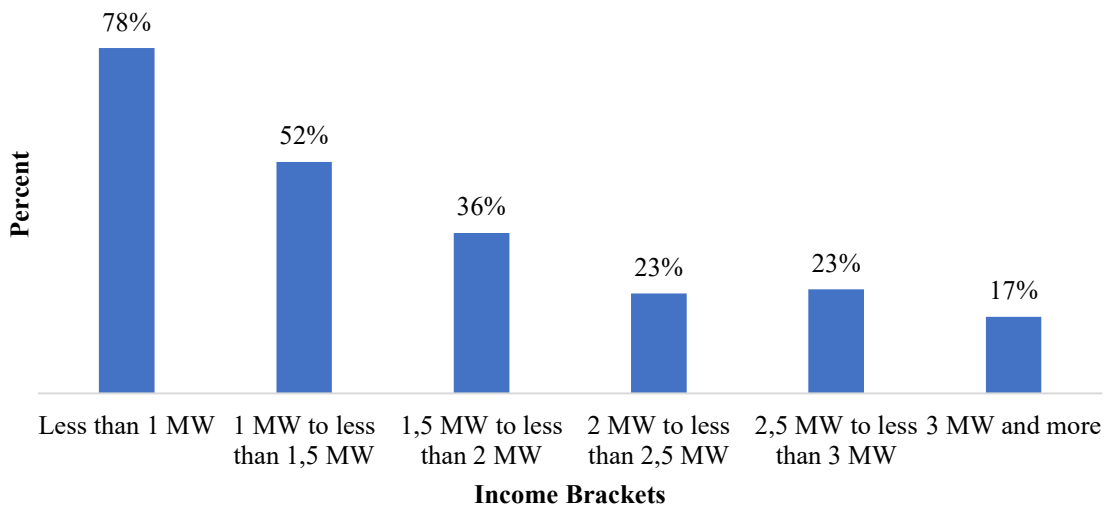
Graph N° 2: Formal and informal companies by category. Year 2018.



Source: Extracted from DGEEC/MIC (2018).

Considering income, it is evident that as income increases, informality decreases, since those who receive less than 1 minimum wage belong to informal occupations in 78%, while those who receive between 3 minimum wages and more belong to informal occupations in 17%.

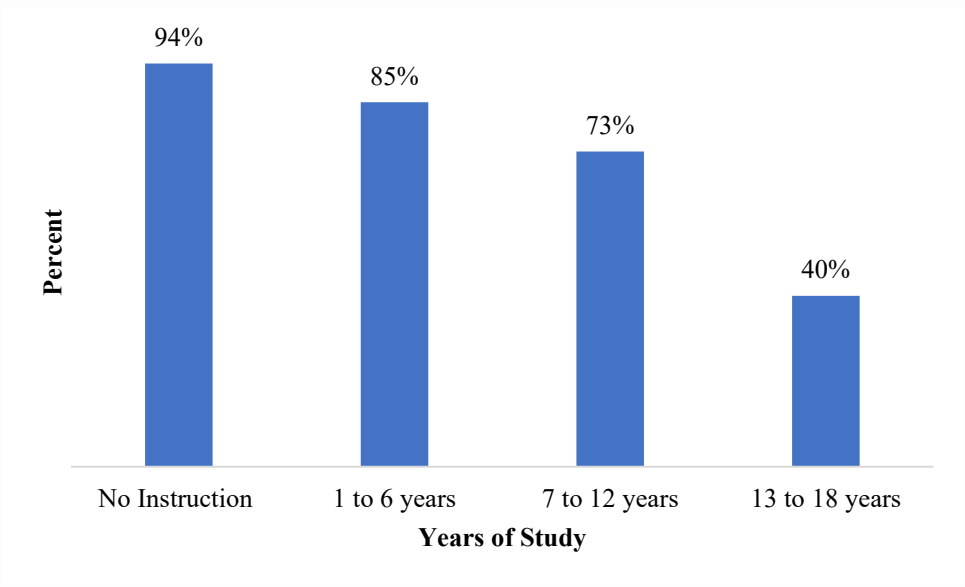
Graph N° 3: Population aged 15 and over, in informal non-agricultural occupations, according to monthly income brackets. Year 2020.



Source: Own elaboration based on (INE, 2021).

Also, taking into consideration the years of schooling, it is evident that as the years of schooling increase, the population in informal occupations decreases, as shown in Graph No. 4, 94% of those with no education belong to informal occupations, a figure that decreases to 40% for those between 13 and 18 years of study.

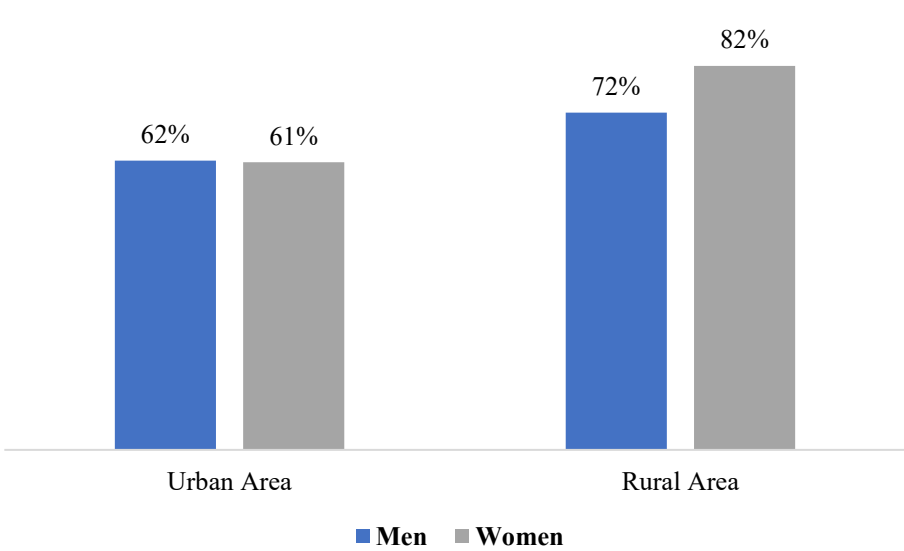
Graph No. 4: Population 15 years of age and older, in informal non-agricultural occupations, according to years of study. Year 2020.



Source: Own elaboration based on (INE, 2021).

Graph No. 5 shows that the rate of informality between men and women in urban areas does not show significant differences, while in rural areas, women face higher levels of informality than men.

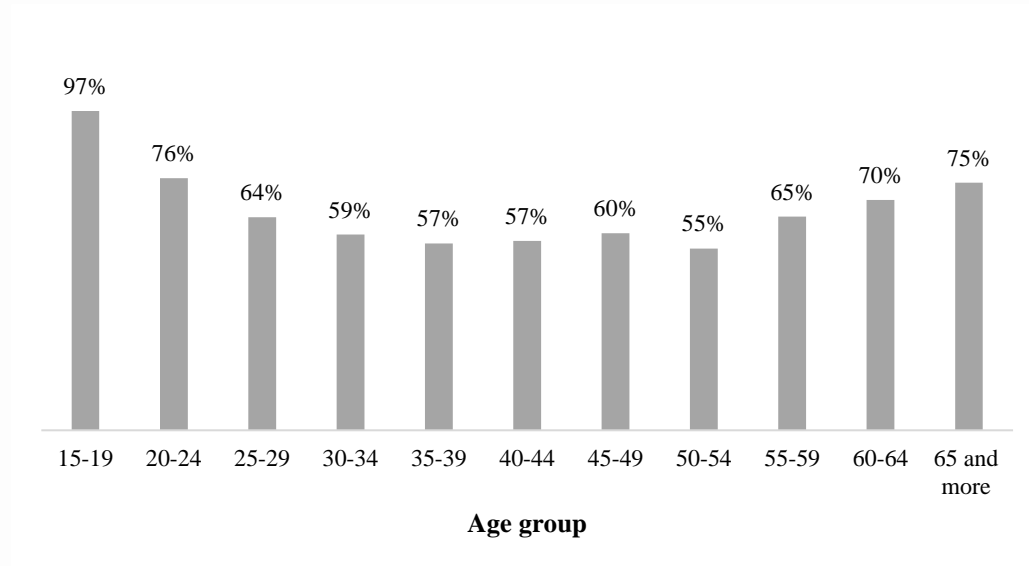
Graph No. 5: Population 15 years of age and older, in informal non-agricultural occupations, by sex and area of residence. Year 2020.



Source: Own elaboration based on (INE, 2021).

Finally, taking into account the age group, as shown in Graph No. 6, informal employment is found above all in the younger populations between 15-19 years of age with 97%, and in older adults aged 65 years and over with 75%. In fact, according to Ayala (2016), informality is present in all ages of workers, it crosses the entire working life cycle, and younger economic actors would be more likely to enter informal work.

Graph N° 6: Population aged 15 and over, in non-agricultural informal occupation, according to age group. Year 2020.



Source: Own elaboration based on (INE, 2021).

5.2.1.2. Group interviews

In each group interview, two situations were presented: one group of formalized entrepreneurs with a RUC and some other type of legal document such as a commercial patent, which according to the study will be considered "formal"; and another group that does not have any type of registration, considered "informal".

5.2.1.2.1. Formal

When the formal entrepreneurs were asked what was the incentive for formalizing their businesses, many of them responded that the main motivation was the requirement of legal sales receipts from their clients, and that not having them meant losing the sale, therefore, it depends to a great extent on the clients to formalize their businesses. They also pointed out that this receipt is necessary when carrying out large transactions, especially with companies and public institutions such as municipalities and governors' offices.

Another one of the reasons that drove these entrepreneurs to pay taxes is the ease of access to credit obtained from financial entities that require the presentation of proof of income, in this case the latest VATs. Finally, some of them pointed out that they prefer to work legally, which is why they decided to formalize their business.

When asked about the procedure to obtain the registration, most of them answered that they hire the services of an accountant, both for the opening and for the monthly liquidation of their taxes. On the other hand, those entrepreneurs who are part of cooperatives or production associations, formalize through the creation of a legal entity and carry out their commercial transactions through this figure.

Similarly, the participants were asked about the knowledge of the procedures carried out by the tax professional, to which the majority responded that they did not know them. Continuing with this order of ideas, they were asked about the possibility of accessing training that would allow them to carry out the procedures themselves, to which they responded that, even knowing these procedures, they would rather delegate this work to a professional, since there are barriers of various kinds, among them, the low level of education that the participants have. This makes it difficult to understand and fill out forms, both physically and online, and taking into account the latter, there are technological barriers for those participants who are not fluent digitally.

Finally, when asked why they prefer to delegate the paperwork and tax settlement to an accountant, most of them pointed out that the monthly cost, which is between Gs. 50,000 (US\$ 7.5) and Gs. 80,000 (US\$12), is a price they consider "cheap," and the set-up costs, which range from Gs. 100,000 (US\$15) and Gs. 250,000 (US\$37.5), "are worth paying", since they say that the opportunity cost of carrying out the procedures themselves, in terms of mobility, time and effort, fully compensates the amount paid to the accountant. In addition, most of these entrepreneurs combine their commercial activities with domestic and care work, so there are not only costs related to the procedures themselves, but also costs related to being absent from their homes. They also point out that if they were to do it by themselves, they would run the risk of making mistakes that could result in fines, which is why they choose to delegate.

5.2.1.2.1. Informals

When asked why these entrepreneurs do not join the formal economy, most of them answered that they do not feel the need to do so, that is to say that their clients do not require the issuance of sales receipts and this does not prevent them from carrying out their commercial activities.

Other entrepreneurs also state that, in the case of needing invoices, they borrow from other formalized persons in the same line of business, or from their spouses in the case of some participants.

And just like the formal entrepreneurs, when asked about the procedure they would follow if they wanted to join the formal economy, they said that they prefer to hire the services of an accountant, they consider that the cost of the procedures is affordable, and, as already mentioned by the formal entrepreneurs, they say that taking into account the time, effort and money needed to carry them out by themselves, they prefer to delegate the task to a professional.

5.2.2. Literature Review

Jayachandran (2020), states that small firms generally do not need or are not interested in the benefits that come with formalization such as access to credit or access to larger markets because these informal firms have low productivity and do not gain significant advantages by

joining the formal economy over already formal firms with higher productivity. In fact, most of these informal firms would not survive in the formal sector, so encouraging these firms to register will not promote their growth; rather, they cause the informal sector to contract and promote the growth of existing formal sector firms.

In this vein, a case study analyzing Brazilian firms by Ulyssea (2018), concludes that informal firms are not held back by their informality, and increasing enforcement is very effective in reducing informality, but reduces welfare in the economy. Continuously, the results of the study show that only 11.5% of firms formalize by reducing the costs of entering the informal sector and that 35.9% of informal firms choose informality to exploit the advantages of non-compliance even though they are productive enough to join the formal sector, the rest would not survive as formal firms.

Another point of view of Jayachandran (2020) who mentions De Soto (1989, 2000), is that informality limits the growth of microenterprises since they would have access to capital and product markets by formalizing and thus boosting their growth. The idea being that enterprises intend to formalize, but are deterred by the costs and bureaucracy of the process, or because they lack the necessary information on the benefits.

On the other hand, taking into account the gender perspective globally, the proportion of women in the non-agricultural informal economy matches that of men, but they differ in occupations as women mostly work as street vendors, unregistered domestic workers, unpaid family workers or manual laborers in informal factories, and in turn face a greater need to combine family and work responsibilities (Bonnet & Leung, 2021). In Paraguay, the proportion of women in informal non-agricultural occupations is 66.2% versus 64.3% for men, so it could be said that there are significant differences by sex (INE, 2021).

Finally, the point of view (Jayachandran, 2020) argues that the evidence found in the studies does not strongly support the optimistic view that formalization triggers microenterprise growth, so more evidence is needed on what specific benefits of formalization, such as access to larger markets or access to finance, convince firms to formalize and help their performance.

VI. CONCLUSION

According to the macroeconomic data and taking into account the theoretical review, it can be said that informality is present mainly in microenterprises, whose owners are self-employed, with incomes below the minimum wage and lacking a high level of education, especially in rural areas and with a higher incidence among women. Informality penetrates the entire working life cycle, but is more pronounced among young people and older adults.

The motivation for entrepreneurship, as in the case studies of Barrón (2020), is largely due to the lack of opportunities for waged employment. Taking into account the socioeconomic characteristics of these entrepreneurs, they do not have the capital or the administrative management skills necessary to carry out their businesses competitively, which turns them into survival businesses and reduces them to the informal sector.

Given that most of these businesses are led by women, another of the main motivations to start up is the possibility of generating additional income from their homes and having economic independence; however, given the low performance of their enterprises, these workers must necessarily combine family and work responsibilities.

The main motivation for formal entrepreneurs to join the formal economy comes from the demands of their own clients and the possibility of opening up to new markets, which in turn allows them to access capital markets. However, non-formal entrepreneurs do not feel the need to formalize given the lack of demand from their clientele, and in fact do not feel sufficiently attracted by benefits such as access to credit given the low profitability of their businesses that would not allow them to return the capital and interest, a situation that is supported in the case studies presented by Jayachandran (2020).

Formal entrepreneurs hire the services of an accountant to carry out formal procedures. In general, both formal and non-formalized entrepreneurs prefer to delegate the task even if they know the procedures. They consider that the opportunity cost (time, effort and money) of doing the formalities themselves is higher than paying an accountant, and they rate the service as accessible, so it can be said that there are no significant barriers to entry. This in some way could explain Ulyssea's (2018) results on low response to policies that encourage formality, such as trainings and promotion of benefits, and rejects De Soto's (1989-2000) idea that firms intend to formalize, but are deterred by the costs and bureaucracy of the process.

Finally, the study reveals that formalized firms enter the formal economy because of external pressures such as clientele demands and not because of mere knowledge of the benefits of formality. Therefore, policies that encourage formality through the promotion of such benefits may not be sufficiently effective for those firms whose productivity and competitiveness levels are low. Given the evidence that enterprises become formalized as they grow, an improvement in the capacities of these microentrepreneurs to develop could generate, in the medium or short term, a significant improvement in business performance that would translate into their incursion into the formal economy.

VII. RECOMMENDATIONS

In this section, an analysis has been made on the impact of interventions carried out in other countries through case studies. This was made in order to evaluate, according to the literature review, what type of policies would be the most effective to promote formality in Paraguay.

7.1. Literature review

Jayachandran (2020), states that assistance with the application process effectively increases the level of formalization, however, this type of policy targets a small proportion of firms that are already willing to formalize, so identifying and successfully targeting the subset of firms that would formalize could reduce costs and make the intervention more cost-effective.

The author states that many of the efforts to help firms formalize are not effective, as an example, he mentions the studies of Andrade (2013) in Brazil and Galiani (2017) in Colombia, where information and fee waivers have been provided, which has not increased the level of registration. The initiative only had short-term impact, then firms would let the registration expire. Similarly, Rothenberg (2016) in Indonesia, has found no impact of opening one-stop shops for registration. However, Jayachandran finds similar patterns of behavior, where he claims that information conveyed in person through trained staff is more effective than just leaflets.

Bonnet & Leung (2021), consider that the formalization process consists of seeking a gradual improvement of the legal and compliance framework with the law and international labor standards.

Ulyssea (2018) states that law enforcement is very effective in reducing informality, but it could have a negative impact on the welfare of the economy.

Barrón (2020), conducted an evaluation of two programs in Peru, his main finding was that both business training programs led to a substantial increase in formalization. Participants increased their registrations by 20-25%, and in addition, they increased labor demand and working hours per day in their businesses, which in turn is a strong indicator of higher business income.

Barrón, who cites Mano et al. (2012) and Sullivan (2000), states that management training whether at the basic or specialized level have significant and even long-lasting positive effects through the impact on long-term business performance.

Similarly, Barrón mentions Drexler et al. (2014) who presents a case study conducted in the Dominican Republic, where training is focused on informal financial training, aimed at entrepreneurs who lack management skills. Among the most significant findings of the study, is that formal financial training only works with highly skilled workers, and that informal training can increase the profits of entrepreneurs by 8% as well as reduce the likelihood of accounting or financial errors.

Likewise, Barrón mentions the studies of Cho and Honorati (2014) and emphasizes the need to offer financing to small entrepreneurs to counteract their lack of access to financial markets,

since, according to these authors, training alone does not improve the performance of enterprises, but rather a combination of these combined with financial support, especially among women entrepreneurs.

Finally, Barrón naming Benhassine et al. (2018), De Andrade et al. (2016) and (Piza, 2018), argues that the effect of providing information about the benefits of formalization and the registration process alone do not increase the probability of formalization of a firm, as the benefits of joining the formal sector are uncertain, and similarly, providing information about tax simplification programs alone also do not promote formalization. However, several studies find that some degree of success can be achieved if information is offered along with tax mediation services, financing, or individualized training.

7.2. Recapitulation

Taking into account the literature review and research findings, an assumption can be established that formality occurs as a result of business growth, and it is expected that such improvement will facilitate the transition to the formal economy and decent work, generating not only short term but also long term impact. The following is suggested:

The implementation of the Strategy for the Formalization of MSMEs in Paraguay (MIC) through a correct identification and targeting of the different subsets of enterprises that make up the informal economy, since as evidenced in the previous section, efforts must be adapted to the diversity of situations of economic units to ensure the success of interventions at the lowest possible cost.

These interventions should incorporate a comprehensive strategy, especially for those entrepreneurs whose businesses belong to the subsistence economy, combining: assistance in the application process, fee waivers, business training to improve their performance and competitiveness, accompanied by credit products and seed capital in line with the characteristics of the business and the needs of the target population in terms of educational level, purchasing power, gender and geographic location. This in addition to face-to-face training on tax filing and procedures to access simplified tax schemes such as those established in Law No. 6,380 "On Modernization and Simplification of the National Tax System" for the liquidation of taxes.

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IX. ANEX

Anex 1: Number of companies by category. Year 2018

Size	Total	Percent
Total	870.598	100,00%
Micro (2 to 10 people)	844.481	97,00%
Small (11 to 30 people)	18.640	2,10%
Medium (31 to 50 people)	4.293	0,50%
Large (51 and more people)	3.184	0,40%
Percent	100,00%	

Source: Extracted from DGEEC/MIC (2018).

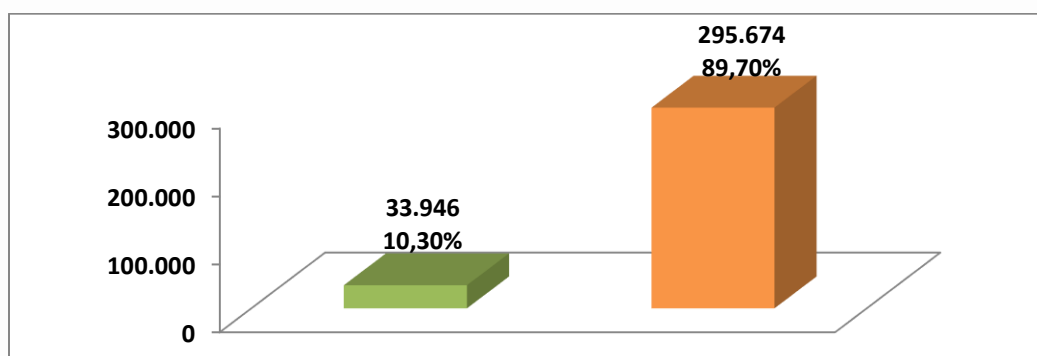
Anex 2: Number of formal and informal companies by RUC/SET status. Year 2018.

Sector	Total	Micro	Small	Medium	Large
Total	870.598	844.481	18.640	4.293	3.184
Formal (with RUC)	263.106	236.989	18.640	4.293	3.184
Informal (without RUC)	607.492	607.492	-	-	-

Source: Extracted from DGEEC/MIC (2018).

Anex 3: Formal and informal self-employed workers. Year 2018.

Tamaño	Total	with RUC	without RUC
Quantity	329.620	33.946	295.674
Percent	37,86%	10,30%	89,70%



Source: Extracted from DGEEC/MIC (2018).

