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**LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM - Session I:
Informal Economy in Latin America and the Caribbean: Implications for
Competition Policy**

- Contribution from the Dominican Republic -

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Session I: Informal Economy in Latin America and the Caribbean: Implications for Competition Policy

- Contribution from the Dominican Republic* -

1. The development of the definition of the **informal economy** by theorists and the authorities responsible for market regulation in the Dominican Republic has resembled its equivalent development in the other jurisdictions around the world, with a focus on changing the criteria used to classify the commercial activities conducted by economic agents operating outside the formal institutions, regardless of the type of economic activity, the size of undertaking or the market segment concerned. In developing economies such as the Dominican Republic, the relative impact of the informal economy is high, and the considerable individual benefits it can generate compare unfavourably to the potential obstacles it poses to productivity, to the detriment of the economic development strategies pursued by the State to ensure public welfare.
2. Since 2016, the Central Bank of the Dominican Republic, the body responsible for compiling statistics on the local labour market, has used the definition of informal employment proposed by the International Labour Organization (ILO) in 2013, namely that informality exists when a worker *“does not have access to social security as a result of his work, regardless of the sector concerned”*.
3. The adoption of this approach was an improvement on the previous situation which described informality as encompassing *“all wage and salary earners working in establishments with fewer than five employees as well as own-account workers and employers belonging to the following occupational groupings: farmers and livestock breeders, operators and drivers, craftspeople and workers in related trades, merchants and salespeople and unskilled workers. Additionally it includes domestic service workers and unpaid workers”*; it therefore had no regard to informality within formal businesses and focused solely on a business’s size, regardless of the fact that a small business could well be formalised and thus not be properly accounted for. The current approach is therefore a better indicator of formality since it is a more faithful reflection of economic behaviour and is more closely in line with international parameters.

* This contribution was prepared by the National Anti-Trust Commission (PRO-COMPETENCIA) of the Dominican Republic.

1. Causes, features and size

4. In line with the World Bank's conclusions¹, the Dominican Republic, like other countries, exhibits factors and features associated with the informal market that foster commercial activities outside the formal institutional framework and poorer quality jobs. These mainly include high operating costs associated with the work force and infrastructure in the formal sector; the tax burden and the shortage of good public services; a complex, fragmented legal framework; the normalising of informal activity because the expected penalties are mild; the lack of programmes promoting entrepreneurship; and, in some cases, the opportunity to earn more in informal employment.²

5. The Dominican Government is therefore introducing programmes to reduce informality on the national market on an ongoing basis; these include "Formalízate" [Go Formal], a project delivered via a Single Window that makes the process of formalisation easier for economic agents while providing information on the benefits of doing so. Another example is the recent launch of the "National Regulatory Improvement Plan"³, which aims to remove unnecessary costs associated with the formal sector in order to encourage formalisation of the economy.

6. Through projects such as these, the Dominican State acknowledges that formalisation programmes must take into consideration a complex strategy of institutional reform and introduce effective measures to simplify the process of incorporating informal agents into the legal framework, while adjusting the tax system to include tax contributions appropriate to the profiles of stakeholders in this segment of the economy, and establishing formal mechanisms for accessing sources of finance.

7. According to research conducted by the Chamber of Trade and Production of Santo Domingo in 2012, many informal businesses understood neither the formalisation process nor its benefits and instead regarded it as burdensome and confusing⁴; hence the need to explain, redefine and simplify. For instance, the payment of tax on gross sales one year in advance, known as "payment on account", was referred to as an obstacle because it generated cash-flow problems for traders.⁵

¹ The root causes of informality are "Overly stringent and expensive government regulations in the labor, product, and land markets, and an ever increasing tax burden imposed on an ever shrinking formal sector." Available at: http://siteresources.worldbank.org/INTEXPCOMNET/Resources/FIAS_Note_298.pdf.

² "Algunas consideraciones sobre la Informalidad y los Ingresos en el Mercado Laboral de la República Dominicana". [Remarks on Informality and Income in the Labour Market of the Dominican Republic.] Central Bank of the Dominican Republic. 30 June 2014. Open Page Forum. Available at: <https://gdc.bancentral.gov.do/Common/public/pagina-abierta/documents/bc2014-06-30.pdf>.

³ Decree 258-18 establishing the National Regulatory Improvement Plan.

⁴ One informal micro entrepreneur in the beauty sector described it thus: "The processes are too complicated to understand; you waste loads of time on them and neglect your business." Results available at: https://acento.com.do/wp-content/uploads/la_informalidad_en_rep_dom.pdf.

⁵ The payment on account of Services and Industrialised Goods Transfer Tax (ITBIS) is the greatest source of irritation where tax is concerned and was referred to by all formal entrepreneurs as having negative repercussions on business cash flow and the ability to stay in business. *Ibid.*

2. Size

8. According to the files and statistics held by the Central Bank for 2017, informal employment in our country currently accounts for approximately 58.6% of the economy⁶, an increase on the figure of 56.9% recorded for 2016.

9. The Central Bank of the Dominican Republic includes among the frame of reference for informality farm and livestock workers, operators, drivers, craftspeople, workers in related trades, merchants, salespeople and domestic service workers.⁷ It also states that the sectors that account for the greatest share of informality are wholesaling and retailing; hotels, bars and restaurants; construction, transport, communications and farming.⁸

10. Apart from failing to register their work force on the social security system, these informal economic agents are not entered in the trade registers or the tax system. This makes it difficult to include them in the analyses necessary in order to determine the size of the markets in which they pursue their activities, which in turn makes it difficult to define those markets with a view to observing the conditions of competition and conducting PRO-COMPETENCIA investigations, especially in cases involving anti-competitive practices.

3. Market productivity

11. In view of the weight of the informal sector and the diverse range of activities it encompasses, there is significant interaction with the formal sector. There are currently no general statistics or data covering that interaction, but it is nonetheless important to note that there are other branches of the economy where, owing to the formality required for tax records, such interaction does not appear to occur.

12. Despite the fact that there are no reliable data on this area, some sectors of the economy take their complaints of unfair competition to the press and the State, as has occurred in respect of automotive parts and foodstuffs.^{9,10,11} This is because informal economic agents do not comply with regulatory and fiscal requirements and thus have an

⁶ Average for the four quarters of the year, Ongoing National Labour Force Survey of the Central Bank of the Dominican Republic.

⁷ “Metodología de la Encuesta Nacional de Fuerza de Trabajo” [Methodology of the National Labour Force Survey], p. 20, Central Bank, available at: <https://gdc.bancentral.gov.do/Common/public/estadisticas//documents//metodologia.pdf>.

⁸ The five sectors responsible for informal employment in the DR, <https://www.eldinero.com.do/44777/los-cinco-sectores-responsables-de-la-informalidad-laboral-en-rd>.

⁹ “Piden regular venta de repuestos usados” [They seek regulation of the sale of used parts] in *Listín Diario* newspaper, 28 September 2011. Available at: <https://www.listindiario.com/economia/2011/09/28/205100/piden-regular-venta-de-repuestos-usados>.

¹⁰ “DGA enfrentará el comercio desleal” [Customs DG will tackle unfair trade] in *Listín Diario* newspaper, 14 June 2017. Available at: <https://www.listindiario.com/economia/2017/06/14/470071/dga-enfrentara-el-comercio-desleal>.

¹¹ “Vendedores de alimentos proliferan sin control en calles SD” [Uncontrolled proliferation of food vendors in Santo Domingo’s streets], *El Nacional* newspaper, 9 October 2016. Available at: <http://elnacional.com.do/vendedores-de-alimentos-prolifera-sin-control-en-las-calles-de-sd>.

advantage over established suppliers and future investors by hampering the expansion of the former and the market access of the latter.

13. The lack of market information generated by informal agents' activities represents a significant barrier to new businesses because it results in information asymmetries that make it impossible for businesses entering the market to be aware of the situation in the sector. Moreover, the impact of the informal food retail sector (front-room stores called *colmados* and *bodegas*) is so great that formal businesses require significant distribution capacity because the fragmented marketing chains are such that accessing the market is difficult, implying that informality can interfere with access to supply chains.

4. Public services and the formal economy

14. Except where access to credit by financial institutions is concerned, traditional public services do not appear to provide an incentive for formalisation because they are supplied regardless of an economic agent's status. This may be the consequence of the fact that not all public services supplied by the State are confined to the formal economy (such as security, electricity, access to justice and others). Accordingly, the informal market generally weighs up the costs of working as part of the formal market and sometimes formalises just one area of its activity in order to benefit from those services.

15. However, economic agents have recently been encouraged to become part of the formal economy by the State's roll-out of the public procurement system which makes eligibility to bid to supply products and services to the extensive state market contingent upon certain aspects of formalisation. Additionally, it provides opportunities for suppliers to export the goods that they produce¹²; the enterprise programmes developed by the Ministry of Industry, Trade and Small and Micro-sized Businesses (MICM) that promote business formalisation through programmes such as Go Formal (see above) allow businesses to go through the formalisation process online.

5. Application of competition policy

16. The General Law on the Defence of Competition No. 42-08 states that operating as an informal business potentially constitutes an anti-competitive practice. The fact that an economic agent "is not in compliance with the rules" is deemed unlawful where the aim of that non-compliance is the illegitimate distortion of consumer demand. The Law empowers the injured party to report such behaviour to PRO-COMPETENCIA for an investigation to determine whether any anti-competitive practice has occurred.

17. As a result, PRO-COMPETENCIA has acted as the post box for certain complaints about economic agents in regulated sectors and has passed them on to the bodies whose rules are the subject of the infringement (whether in relation to taxation or health records) so that the relevant administrative processes can be completed. So far, although PRO-COMPETENCIA has received complaints, it has not yet brought any administrative penalty proceedings against an informal economic agent.

¹² See: <https://www.formalizate.gob.do/Formalizarse/ventajas>.

18. However, in the event that it were necessary to punish an informal economic agent in the absence of any statistical records of its transactions, it is highly likely that PRO-COMPETENCIA would draw on the best practices of other jurisdictions and implement Propensity Score Matching techniques, thus enabling the most similar formal business in the same market to act as a benchmark using observable variables such as sales in order to establish the level of the fine. In the event that no similar business was in operation, a scaling system could be drawn up based on a variable such as number of employees in order to draw a comparison with a formal business in the sector and determine a figure for sales in relative terms.

19. In 2017, in the context of applying competition policy to informality, and in view of the considerable number of informal bakeries in the Dominican Republic, PRO-COMPETENCIA carried out a study on the conditions of competition in the market for bread. The main difficulty here was the systemic lack of information, especially historic information, and the absence of any systematic records on production processes and costs; that difficulty was highlighted in the study and offset by drawing on data from private businesses selected through a sampling survey. The difficulty in accessing measureable, reliable information acted as a significant constraint on the institution's work and prolonged the time taken to obtain evidence and proof which is, in any event, limited in law to 12 months for a complaint-led investigation. Note, however, that the absence of systemic records is also an issue in the country's formal businesses.

6. Informality and market definition

20. Since it has proved difficult to rely on official statistics when a large percentage of economic agents work in the informal economy, when defining such a market we must take care to rely not only on the data provided by official institutions, e.g. the General Directorate of Domestic Taxation: to do so would risk failing to identify the market and the economic agents correctly. As a result, the absence of official statistics from those agents may result in greater market power being ascribed to formal businesses because they are more under the spotlight. Similarly, businesses' very informality makes it difficult to analyse the effect of a given role in a market with high levels of informality.

21. In terms of the impact of informality on economic growth, it is clear that, in several respects, the informal sector can act as a safety valve that relieves pressure on indicators such as unemployment and fosters a less costly form of entrepreneurship, thereby stimulating economic performance. Furthermore, widespread tax evasion leads to low tax revenues, prompting fiscal policies that increase tax pressures on the formal sector and thus giving rise to market inequality between economic agents that can amount to between 10% and 30% of the cost of sale of a product or service.¹³ Consequently, as informal activities become more entrenched, they encourage the expansion of low-productivity activities that have no accounting system and tend to invest less in R&D and human capital. The effect on economic growth would therefore appear to be no trivial matter.

¹³ Transitioning from the informal to the formal economy; Report V (1), International Labour Conference, 103rd Session, 2014, ILO, First edition 2013, Geneva.

7. Advocacy

22. Given that, currently, the highest concentrations of informality are in the country's small and medium-sized enterprises¹⁴, the Dominican Government in the form of the Vice Ministry of MSMEs is constantly launching programmes to encourage formalisation and simplify obstacles. Worthy of note in that regard is the programme "Go Formal", which aims to provide information on the benefits of formalisation in order to facilitate the process; tools provided under the programme to simplify procedures include the Single Formalisation Window, the opening of centres providing advice on the formalisation process, and a reduction in the administrative fee for registering on the Trade Register.

23. Additionally, the Directorate of Domestic Taxation has drawn up the Tax Simplification Programme to make it easier for economic agents to formalise their structures. The Programme is currently undergoing review with a view to implementing further changes to improve users' experience. The Minister for Industry, Trade and MSMEs has recently stated that tax payments "on account", which businesses have described as problematic, are to be abolished for small enterprises. It is anticipated that this will help contribute to formalisation and simplify the tax system.¹⁵

24. The official strategy to formalise the economy has encouraged other initiatives that review the regulatory framework. To that end, the National Social Security Council has drafted a regulation which, once approved, will allow microbusinesses to join the Social Security system.

25. Through its advocacy work, PRO-COMPETENCIA also has a role in simplifying regulatory procedures that can have a negative impact on free and fair competition. We have a presence on a large number of standards-setting bodies within the National Quality Institute (INDOCAL), and also actively participate in and scrutinise regulations and laws with a view to removing any unnecessary barriers to which they give rise. Similarly, we have conducted studies to pinpoint barriers and state procedures that could be amended or abolished; these studies have been published and distributed across the country to promote the development of competition.

¹⁴ "Nine out of ten business people (89.8%) indicated that they operate as unregistered businesses with one (88.8%) or more than one owner (1%)" Ortiz, Marina; Cabal, Miguel; Mena Risa. *Micro, Pequeñas y Medianas Empresas en la República Dominicana* [Micro, Small and Medium-Sized enterprises in the Dominican Republic], Fondo para el Financiamiento de la Microempresa, Inc. [Microbusiness Finance Fund Inc.] (FONDOMICRO), 2014. Available at: https://pymes.do/static/media/attachments/FONDOMICRO_-2013.pdf.

¹⁵ "Gobierno dominicano anuncia fin del anticipo para las pequeñas y medianas empresas" [Dominican Government announces the end of payments on account for small and medium-sized enterprises], *El Dinero*, 3 August 2018. Available at: <https://www.eldinero.com.do/64930/gobierno-dominicano-anuncia-fin-del-anticipo-para-las-pequenas-y-medianas-empresas>.

8. Closing remarks

26. The structure of the informal economy includes non-compliance with the obligations imposed under the legal framework established by the State to ensure the responsible exercise of the basic right to free enterprise. In the Dominican Republic, the General Law on the Defence of Competition recognises that economic efficiency, effective competition and good will in business go hand in hand, and classifies the failure to comply with obligations as an anti-competitive practice.

27. Thus, in the exercise of its legal powers, PRO-COMPETENCIA places high priority on its work on government initiatives to design and implement public policy instruments that are likely to promote conditions that are conducive to shrinking and, ideally, stamping out the informal economy and its effects on free competition.

28. The aim of implementing our competition advocacy measures as part of these restructuring processes is to ensure that the design of the resulting programmes and regulations takes into account the range of markets affected by the informal sector and profiles of the economic agents concerned. In so doing, we are aware of the particular importance of taking an approach that can be applied across the board to identify such activities so that auditing and regulatory arrangements can be activated. Those general arrangements can be supplemented by programmes tailored to the individual features of each segment of the economic sector concerned that will convert and integrate the activities in question into the formal economy.