Easing the Transition: Proposing a Supranational Body to Facilitate Formalizing Economies

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I. INTRODUCTION

In the 1970s, a "microloan movement" began with the Grameen Bank in Bangladesh.¹ Between 1980 and 1998, microcredit provided by Grameen Bank and others helped over 10 million Bangladeshis rise out of poverty.² Those microloans, often of less than $100, have helped individuals and individual families earn a better living than they would have been able to earn otherwise.³ The difference of $100 may seem trivial, like "chump change" to

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1247
Americans; yet, to entrepreneurs in many developing countries, that difference can be enough to rise from poverty to relative prosperity through the purchase and use of materials and equipment for a small business.

Because the dollar amounts loaned to individuals are so small when compared to first-world notions of relative wealth, the potential returns on the loans to the microcredit lender and the returns on the capital provided to the borrower are likewise small, making it less likely that a first-world investor would engage in such lending. Similarly, because governments would likely expend more money in tracking these businesses for proper registration and taxation than they would receive in tax dollars, these microfinanced businesses most often operate in the “informal economy.”

Every nation’s economy has an informal sector. In developed countries, the informal sector’s share of the gross domestic product (“GDP”)

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5 Alyce Lomax, Tiny Loans, Tremendous Returns: Tales from the Microlending Frontier, DAILYFINANCE (Mar. 7, 2012, 12:46 PM), http://www.dailyfinance.com/2012/03/07/microloans-power-small-business-success-stories/. The article details the impact of $200 loans for two Costa Rican entrepreneurs. Id. One bought equipment for a bakery run out of her home; the other bought materials for garment making, which she also does from home. Id. The loans gave the entrepreneurs the capital they needed to create and sustain successful at-home businesses. Id.

6 For example, a Swiss citizen (of the first world) brings home, on average, $5,682.71 per month, and a Bulgarian citizen (of the developing world) brings home, on average, $483.00 per month. Rankings by Country of Average Monthly Disposable Salary (Net After Tax) (Salaries and Financing), NUMBEO, http://www.numbeco.com/cost-of-living/country_price_rankings?itemld=105 (last visited Apr. 13, 2016). These two investors will have very different ideas about what each expects from her return on investment and, thus, of which investments are worth each one’s time. See Opportunity Cost, INVESTOPEDIA, http://www.investopedia.com/terms/o/opportunitycost.asp (last visited Mar. 27, 2016). That is, the Swiss citizen and the Bulgarian citizen will assign different values to the same $10, as that dollar amount represents just 0.18% of the Swiss’s take home salary, but 20.7% of a month’s salary for the Bulgarian—making the $10 more valuable to the Bulgarian, relative to her existing wealth. See id. Additionally, because an investor incurs transaction costs with each investment made, it only makes sense that an investor will choose fewer and larger investments as opposed to many smaller investments to avoid those costs. See Michael S. Barr, Microfinance and Financial Development, 26 MICH. J. INT’L L. 271, 283 (2004) (“[T]he transaction costs in lending small amounts to lots of poor borrowers are high.”); Transaction Cost, BUSINESSDICTIONARY.COM, http://www.businessdictionary.com/definition/transaction-cost.html (last visited Mar. 27, 2016).


may be quite small and may be seen in unreported wages of day-laborers or the availability of cheaper goods produced by companies paying lower than the minimum-wage—cash wages, for example. In developing countries, the informal sector may be much more pervasive and may be seen in most small businesses at every level, from ownership and management to labor.

The informal sector presents some of the same problems to developed and developing countries: for example, the potential for human rights abuses is prevalent where labor conditions are not regulated, and the disparity between taxes paid and benefits received is worsened where taxes are evaded by some. These problems, though, are much more consequential in developing countries: where more of a population labors without meaningful regulation, abuses are more likely, and where more of a population evades taxation, those that are taxed pay more than their share relative to the benefits they receive. Because of these and other problems, there is great call for the formalization of informal economies in developing nations.

Formalization, though, is not automatically or even easily achieved for most informal sector participants. First, there is the question of whether an informal sector participant will choose to formalize, where that option is available—answering this question requires a cost-benefit analysis for a given informal sector participant. Second, there is the question of whether an informal sector participant has the means to formalize—answering this question requires, among other things, an analysis of what is required of an

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9 See Saskia Sassen, The Informal Economy: Between New Developments and Old Regulations, 103 YALE L.J. 2289, 2298 (1994) ("The consumption needs of the low-income population are met in large part by small manufacturing and retail establishments that rely on family labor and often fall below minimum safety and health standards. Cheap, locally produced sweatshop garments, for example, compete with low-cost Asian imports."); Guillermo Vuletin, Measuring the Informal Economy in Latin America and the Caribbean 3 (Int'l Monetary Fund, Working Paper No. WP/08/102, 2008), https://www.imf.org/external/pubs/ft/wp/2008/wp08102.pdf (offering the example of New Zealand as having "a low share of informal activity," with around 12% of that State's GDP).

10 See Benjamin Temkin, Informal Self-Employment in Developing Countries: Entrepreneurship or Survivalist Strategy? Some Implications for Public Policy, 9 ANALYSES SOC. ISSUES & PUB. POL'Y 135, 136 (2009) (discussing how some analysts include "street vendors as well as self-employed individuals owning microenterprises, their salaried employees and unpaid relatives" among the informally employed); Vuletin, supra note 9, at 3 (offering the example of Bolivia, the informal sector of which at one point represented approximately 65% of that State's GDP).


12 See Omar E. Garcia-Bolivar, Informal Economy: Is It a Problem, a Solution, or Both? The Perspective of the Informal Business 6–10 (Northwestern Univ. Sch. L., L. & Econ. Papers, Paper No. 1, 2006), http://law.bepress.com/cgi/viewcontent.cgi?article=5065&context=expresso. This question is addressed infra Part II.B.
informal sector participant to enter the formal economy in a given State, "with regulatory and administrative barriers standing out as a particular concern." This Note is primarily concerned with those barriers.

Presently, individual States develop mechanisms for formalization on an individual basis, developing States needing mechanisms more extensive than those in the developed world, which aim primarily to collect taxes owed and ensure minimal safety standards. While the "states as laboratories" approach

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13 In this Note, "State" (capital "S") refers to a sovereign State on the international stage, as compared to those "states" (lowercase "s") like West Virginia or California that comprise a federal State like the United States of America.

14 See EMERGING BEST PRACTICE, supra note 11, at 11. This question is addressed infra Part III.


16 The idea of "states as laboratories" was popularized in the United States by Justice Brandeis’s opinion in New State Ice Co. v. Liebmann, 285 U.S. 262, 311 (1932). Justice Brandeis wrote,

To stay experimentation in things social and economic is a grave responsibility. Denial of the right to experiment may be fraught with serious consequences to the Nation. It is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.

Id. The idea underlying this notion is that the competing "experiments" will respond to the particular circumstances present in the particular states and will yield the most data from which a decider (the federal government for Justice Brandeis) can choose the "best" option to apply uniformly across the system.

Here, the States (capital "S") are not a part of a federal system, but are parts of the international system and sovereigns themselves. Sovereign States may also, of course, experiment in their own cultural, political, economic, and social systems within the limits
definitely has merit as it allows for varied approaches, a more uniform approach is desirable. Because most formal economies are interconnected and interdependent, regardless of geographic location, this Note argues that a uniform means of facilitating both the extension of banking services to informal sector participants and the entry into the formal sector of the same may yield more benefits to all parties of interest, from individuals to local and national governments.

This Note proceeds, in Part II, by describing the informal economy and the motivations of those active in that economy. Part III examines potential barriers to formalization. Part IV explores some alternative financial structures that have developed at the individual State level to encourage economic development toward formalization. Part V.A explains why formalization is a worthy end to pursue, both from the perspective of the individuals working informally and from the perspective of governments seeking to regulate their internal economic, social, and legal workings. Part V.B then argues that a supranational structure would be best able to facilitate the transitioning of particular informal participants into the global, interconnected, and interdependent formal markets by standardizing the formalization process itself. Finally, Part V.C recommends some particulars to guide the development of such a supranational body, specifically drawing on the experience of microcredit presented in Part IV. Encouraging formalization is necessary to alleviate many of the problems presented in developing nations with regard to human rights and economic development, generally. The following sections explore the reasons for and arguments against the entrenched informality in many markets around the world.

II. THE INFORMAL ECONOMY

Participation in the informal economy comes with tradeoffs, some benefits for some costs. An informal market participant will participate in that market where the costs of formalizing outweigh the benefits. In other words, an informal market participant will not formalize unless he sees enough value in that prospect to justify the costs in terms of money, time, and opportunities lost. Before getting to this cost-benefit analysis that every informal, and formal, market participant should engage in, however, Part II.A examines just what is prescribed by international law. See, e.g., G.A. Res. 2625 (XXV), Declaration of Principles of International Law Concerning Friendly Relations and Co-operations Among States in Accordance with the Charter of the United Nations, U.N. Doc. A/RES/2625, at 6 (Oct. 24, 1970), www.un-documents.net/a25r2625.htm ("Every State has an inalienable right to choose its political, economic, social and cultural systems, without interference in any form by another State."). States, therefore, are legally able to pursue very different courses regarding any policy that does not violate international law. Id. Varied approaches by States at the international level thus fall in line with Justice Brandeis's conception of "states as laboratories." See Liebmann, 285 U.S. at 311.
meant by “informal economy.” Part II.B then explores the motivations of those who choose to operate informally and the motivations of those who operate formally who, nonetheless, choose to keep the informal market operating.

A. What Is the Informal Economy?

One way to define the informal economy is to contrast it with the formal economy: the formal economy consists of all sectors of the economy that are taxed, regulated, or have formal oversight. The informal economy, then, encompasses everything else. Depending upon the context and time, however, reference to the “informal economy” has any of several meanings. It is a relatively new concept that, in a popular sense in the United States and in most developed States, is largely perceived in one of two ways: as the black market, including economic activity related to drugs, prostitution, and other illegal activities, or as a grayer market, where day laborers exist off the books and waitresses underreport cash tips.

For less developed countries, the concept has a longer history and a less easily summarized subject matter. The idea of an informal economy was first introduced by Keith Hart when studying urban labor markets in Ghana in the 1970s. Hart based his distinction between “formal and informal income

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17 See R. Duane Ireland, 2012 Program Theme: The Informal Economy, ACAD. MGMT., aom.org/meetings/annualmeeting/past-meetings/theme2012.aspx?terms=r (last visited Feb. 21, 2016) (defining the formal economy as being “comprised of commercial activities that a governing body taxes and monitors for society’s benefit and whose outputs are included in a country’s gross domestic product”).

18 Hernando de Soto, The Other Path: The Invisible Revolution in the Third World xi-xii (June Abbott trans., 1989) [hereinafter de Soto, THE OTHER PATH] (“The ‘informal economy’ is usually thought of as a problem: clandestine, unregistered, illegal companies and industries that pay no taxes, that compete unfairly with companies and industries that obey the law and pay their taxes promptly.”).

19 See Richard A. Epstein, The Moral and Practical Dilemmas of an Underground Economy, 103 YALE L.J. 2157, 2157 (1994) (“All sorts of activities, some desirable and some unsavory, are part of the underground economy. The physician who takes cash for a Saturday office visit is working off the books; so is the waiter who reports some but not all tips as income; so too is the maid who pays no taxes on her wages. But the underground economy is far more vast than these examples suggest, for it embraces much more than the unreported, unrecorded, or informal economy. It includes industries that rely on illegal aliens and businesses that are completely outlawed, such as the trade in narcotic drugs.” (footnote omitted)).

opportunities” on wage income and self-employment because only some types of enterprises, those which are wage based, “are amenable to enumeration by surveys, and—as such—constitute the ‘modern sector’ of the urban economy. The remainder . . . are . . . classified as ‘the low-productivity urban sector,’” which had previously been discounted as negligibly contributing to income growth. To Hart, the study of the economies of developing countries “ha[d] been impeded by the unthinking transfer of western categories to the economic and social structures of African cities.” Hart found that, when denied success by the formal opportunity structure—because of inflation, inadequate wages, or a surplus of labor, for example—people sought informal means of increasing their incomes by “emulating the role of the small-scale entrepreneur.” Hart’s conception of the informal economy thus argued for the study of this segment of the population in determining the productivity of economies because, as Hart concluded after identifying its lack of attention, the “‘reserve army of underemployed and unemployed’ in towns may or may not be the economic disaster it is often thought to be.”

Once introduced to the world, Hart’s characterization of the informal sector was redefined and institutionalized within the International Labour Office (“ILO”) bureaucracy as synonymous with poverty, eventually becoming known as the “excluded” sector in less developed economies in the ILO, World
Bank, and other studies over the next 15 years. That characterization, though, has been consistently challenged by Hart and others who view the informal sector as “people taking back in their own hands some of the economic power that centralized agents sought to deny them.” Thus it is within States where some segments of the population tend to be denied access to the means to generate or retain economic power that informal economies develop most often and become institutionalized components of the formal market itself. The next section explores the motivations of those who operate informally to so operate and the motivations of those who operate formally to keep the informal market operating.

B. Where (and Why) Are Informal Economies?

A concise answer to this question is that informal economies develop where the benefits promised by informality outweigh the costs to those individuals engaging in economic activity informally. Every nation, regardless of wealth or level of development, has an informal economy. Those in the developing world are much more prominent than those in most developed countries. For example, in Third World and post-Communist States transitioning to market economies, 80% of some populations may exist as

26 Keith Hart, The Idea of Economy: Six Modern Dissenters, in BEYOND THE MARKETPLACE: RETHINKING ECONOMY AND SOCIETY 137, 158 (Roger Friedland & A. F. Robertson eds., 1990). Another school characterizes the informal economy as being comprised of “income earning activities unregulated by the state in contexts where similar activities are so regulated.” Portes, supra note 20, at 148 (citing Manuel Castells & Alejandro Portes, World Underneath: The Origins, Dynamics, and Effects of the Informal Economy, in THE INFORMAL ECONOMY: STUDIES IN ADVANCED AND LESS DEVELOPED COUNTRIES 11 (Alejandro Portes et al. eds., 1989)); see also Edgar L. Feige, Defining and Estimating Underground and Informal Economies: The New Institutional Economics Approach, 18 WORLD DEV. 989 (1990). That characterization suggests unified interdependent systems involving many points of intersection between the formal and informal economies. Portes, supra note 20, at 149. This school sees the informal economy as complementary to the formal economy, enhancing the profitability of the formal sector by reducing the cost of inputs and increasing the “yield” of wages earned in the formal economy with the provision of cheaper-than-otherwise-possible goods and services. Id. at 150, 162.
28 Tomal & Johnson, supra note 8, at 71.
“informals”\(^{30}\) and, in some States, the informal economy accounts for over 50% of GDP.\(^{31}\)

According to the ILO, it is a fact that “the larger part of the world’s working population earns its livelihood under the vulnerable and insecure conditions of the informal economy.”\(^ {32}\) Not including employment in agriculture, which would significantly increase the following percentages, approximately 65% of employment in developing Asia, 51% in Latin America, 48% in North Africa, and 72% in Sub-Saharan Africa exists in the informal economy.\(^ {33}\) Informal economies typically include small-scale business activities in traditional sectors.\(^ {34}\) According to the ILO, most jobs created today, in many parts of the world, are informal, including both self-employment and informal wage work.\(^ {35}\)

Although the particular contours of informal sectors vary by country, many develop where “the system is administered in a corrupt, incoherent, exorbitantly expensive, discriminatory or elitist manner” because the laws do not adequately protect all of the members.\(^ {36}\) That “incoherence” derives from the notion that “the law must reflect the heterogeneous social realities of its people.”\(^ {37}\)

Where the local circumstances in a developing nation do not match those notions, “the result is a system of governance that drives people into informality based on its incoherence.”\(^ {38}\) Informal economies thus may develop where Western nations influence and encourage development based on notions developed in the context of social realities that are markedly different from those present in the developing country. For example, in Hernando de Soto’s study of Peru, he found that in order to legally register a shop, an entrepreneur would have to spend 289 days, working six hours a day, at a cost equal to 36 times the Peruvian monthly minimum wage—those registration requirements

\(^{30}\) Id. (citing DE SOTO, THE MYSTERY OF CAPITAL, supra note 24, at 15–16).

\(^{31}\) Id. at 128–29. In 2000, de Soto reported that underground markets accounted for 50% of GDP in Russia and Ukraine and 62% of GDP in Georgia; that “85% of all new jobs in Latin America and the Caribbean have been created in the informal sector”; and that only 10% of the workforce in Zambia was legally employed. DE SOTO, THE MYSTERY OF CAPITAL, supra note 24, at 69.


\(^{33}\) Id. at 7.

\(^{34}\) Id. at 1.

\(^{35}\) Id.

\(^{36}\) Miller, supra note 29, at 129.

\(^{37}\) Id. at 130.

\(^{38}\) Id.
bore no relationship to the economic realities of the vast majority of Peruvians. Informal economies may also develop where the incoherence results from a lack of trust in a corrupt regime and, therefore, a lack of trust in the laws it produces. In post-Soviet States not long after partition, for example, those citizens who did not trust the institutions that were largely still run by the very same bureaucrats that had run the prior regime participated in some aspects of the informal economy.

Informal economies develop and thrive all over the globe. Although informal markets develop in every nation, regardless of GDP or other economic measures, informal markets develop most substantially in States that do not adequately provide for their populations. In short, no matter the peculiar circumstances of any given case, an informal economy will develop where the benefits promised by informality outweigh the costs to an individual engaging in an economic activity informally.

1. The Benefits of Operating Informally

In weighing the benefits against the costs of formally or informally operating, both economic and noneconomic factors are judged. Economic motivations relate to "unemployment and an inflexible formal labor market[,] the declining real price of capital[,] and the high cost of formal production." Non-economic motivations relate to "a greater flexibility and greater

39 See Susan J. Winterberg, Still on the Other Path? The Impacts of Business Formalization in Peru and Their Lessons for SME Development Policy 4 (2005), https://www.academia.edu/1384164/. Still_on_the_Other_Path_The_Impacts_of_Business_Formalization_in_Pe...


41 See Wallace & Latcheva, supra note 40, at 84.

42 Tomal & Johnson, supra note 8, at 71.

43 See generally Miller, supra note 29, at 128.

44 See Fallah, supra note 27, at 12.


46 See id. at 278.
satisfaction in work[,] a complete use of [one’s] professional qualifications[,] and the increased leisure time.”

The most easily identified benefits of operating informally are those economic factors exposed when contrasting the various costs necessarily paid by formal market participants. The taxes and withholdings, registration and licensure fees, and any spending for compliance, specifically, that must be paid by formal market participants are not paid by those operating informally. Several studies have put numbers to the cost of formality: for example, studies of Peru, Costa Rica, and Argentina found the cost of operating fully within the law, as compared to the cost of operating informally, to be between $590 and $1,231 per month, $3,600 per year, and $1,000 to start a business, respectively.

Additionally, the time formal market participants spend toward accounting for or paying any of those costs, as well as the time spent registering the business or its employees and complying with regulations, is not spent by those operating informally. In Ecuador, for example, the basic process for registering a business can take 141 days. The average for all Latin American States for the basic registration of a business is 97.2 working days, requiring 13.5 procedures to register. The benefit to those who do not engage in such onerous registration lies in the opportunity costs they save by not standing in line, essentially, for days on end. To state this differently, those who do go through such registration processes lose the value of all the opportunities they have lost while registering.

Another major benefit to those operating informally arises because informally operated businesses are, by definition, not subject to regulations

47 See id.
48 See Martha Alter Chen, Rethinking the Informal Economy: Linkages with the Formal Economy and the Formal Regulatory Environment 4 (U.N. Dep’t Econ. & Soc. Affairs (DESA), Working Paper No. 46, 2007); see also Fallah, supra note 27, at 6 (“Registering a business often entails completing several requirements related to screening, health and safety, environment, and tax registration.... The burden of registration also includes the time it takes from start to finish.”).
50 See id. at 9, tbl. 2.
51 Id. at 8 (citations omitted).
52 Id. at 9, tbl. 2. These numbers are for only the basic registration requirements: If a business needs special permitting, is subject to an excise tax, or operates in foreign trade, for example, “then the number of procedures and amount of time [required to] register [a business] increase significantly.” Id. at 8.
53 Id. at 4.
54 Id.
formally operated businesses become subject to through registration and compliance. Therefore, the owners of informally operated businesses often employ informal wage-earners who are willing to be paid in cash, perhaps even at a cheaper rate, unreported to the government and therefore not subject to any taxation or withholding.\(^{55}\) This gives the owners of informally operated businesses two advantages. First, the cost of labor to the owner will be lower than the cost of labor would be in a formally regulated business, increasing his profits. Second, because the cost of labor is less for the owner of an informally operated business, the product or service of the business can be offered at a discount from the price a formally operated business would have to charge for the same product or service.\(^{56}\) Because of this discount, the owner of the informally operated business may garner a larger share of the market than he would otherwise receive, increasing his profits.

One potential benefit of operating informally that is not necessarily economic arises when an individual decides not to pay into the tax base because of “a lack of any trust in the way taxes are spent.”\(^{57}\) Where the government loses the trust of its population, “a step into the twilight economy will be taken much more easily.”\(^{58}\) If an individual’s values are such that this negative action would be a benefit to himself, operating informally will come that much more easily.\(^{59}\)

Scholars have identified several predominant reasons informal market participants have mentioned for their participation in the informal economy, including the evasion of taxes and legislation related to labor conditions, quality regulations, and production limits.\(^{60}\) An increase in any of these transaction costs of participation in the formal economy would make it “relatively more appealing to switch to the informal sector.”\(^{61}\) Depending on the ease of access to the formal economy, the benefits of operating informally can be significant, especially for those whose earnings do not go far above maintaining the family’s subsistence.\(^{62}\) Any benefits from informally operating, of course, will be weighed against the costs of operating informally.

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57 See Gërshani, *supra* note 45, at 278–79.

58 See id.

59 See id.

60 See id. at 279.

61 See id.

2. The Costs of Operating Informally

Starting from the individual informal operator’s perspective, several costs are apparent. First, access to banking and credit services is limited for those operating informally, “usually due to insufficient collateral.” The starkest example of a cost created by the lack of access to banking services is the constant fear of having one’s money stolen for a lack of a safe place to deposit the money. Also, the mortgages banks give are rarely available to informal market participants. Commercial banks most often require proof of formal income in order to qualify for a mortgage. Informal market participants, by definition, often have no formal income to report. Therefore, the mortgage as a savings and investment vehicle is not readily available to informal market participants, limiting their ability to be financially secure, especially in times of economic downturn. This lack of access limits the informal operator’s ability to grow her business as well as her ability to withstand economic downturns.

The ability to grow a business is not only limited by access to credit, though. Informal market participants must limit the size of their informal operation for fear of detection of the informal business by government bodies. For example, an entrepreneur employing 50 people runs the risk of detection because those 50 people likely will have to misreport or hide their earnings to protect the entrepreneur and the business employing them. If even one is

See Fallah, supra note 27, at 4. While it is true that access to these services is still limited by operating informally, NGOs and some State organizations have responded to this concern, specifically, by offering microcredit and other services where the NGOs or State organizations operate. See, e.g., VANGUARD, supra note 15, ¶ 11.


See id.

See id. (“Given current practice, where commercial banks require proof of formal income as a condition for accessing home loans, it turns out that lack of ready access to these instruments mitigates the attractiveness of formal employment; i.e., being able to own a house that not only serves to provide a consumer good (a roof over our head), but is also an insurance vehicle that can be accessed as well in times of economic misfortune.”).

See id. at 12 (“[L]ack of access to credit limits firms’ growth as well as their capacity to survive economic downturns.”).

Fallah, supra note 27, at 4.
audited (or, perhaps more likely, examined) by an authority or someone with a duty to report suspicious financial activity to an authority, the entrepreneur will likely be detected and may be shut down by the authorities.

Another example arises from situations where the informal business is generating good profits. Those profits, at some point, will likely have to be reported and formalized or the entrepreneur runs the risk of detection and fines or other punitive measures. Where the benefits of operating informally are still outweighed by the costs of entry into or the costs of compliance with the formal economy, despite earning good profits, the entrepreneur has incentive to produce less, employ less, and earn less solely to avoid detection. Further, this fear of detection also limits informal market participants' ability to get government support, like training or subsidy programs. This, of course, would apply to the owners of the informal businesses, but also to the employees earning informal, but real, wages, who would be deterred from seeking such government support as might help them enter the formal market. Fear of detection thus affects all informal market participants, though those who own informal operations obviously have more incentive to hide the operation as they profit from those operations more than those they employ.

Another potential cost in some parts of the world is the cost of any bribes that need to be made in order to be allowed to continue to operate. For example, a study published in 2000 reported that in some post-Soviet States, bribing government officials was still the norm, in other post-Soviet States, it was simply not uncommon. In Russia and the Ukraine, 90% of managers reported that it was normal to pay bribes to government officials; in Slovakia, 40% of managers said they paid bribes; and in Poland and Romania, still 20% of managers paid bribes. Those figures were distinguished by the study as bribes paid specifically to government officials from bribes those firms paid for "protection" to the mafia or other criminal gangs.

Informal market participants also face, in many cases, substandard labor conditions due to employment in an unregulated business. Sweatshops

71 Id.
73 Id.
74 Id. These latter bribes for "protection" would presumably still have to be paid even where operating informally, unless the operations were so well hidden that not even the criminal elements were aware of the economic activity ripe for exploitation.
75 James Heintz & Robert Pollin, Informalization, Economic Growth and the Challenge of Creating Viable Labor Standards in Developing Countries 2 (Political Econ. Research Inst., Working Paper No. 60, 2003), http://scholarworks.umass.edu/cgi/viewcontent.cgi?article=1048 &context=peri_workingpapers ("In many cases, the process of informalization is directly linked to these concerns over human rights violations, downward pressures on poverty-level wages, or a general erosion of working conditions. Sweatshops and factories using child labor often must
and businesses employing children, for example, must generally operate informally as the practices of such businesses are generally outlawed by domestic laws and violate international laws concerning human rights, worker's rights, children's rights, and labor standards. Other areas where the presence of informal markets effects societal concerns are in the areas of health, safety, and environmental protection. In 2007, the ILO described the following ways that workers in the informal economy faced “severe decent work deficits” and “precarious and vulnerable” conditions:

[W]ork in the informal economy is often characterized by... unsafe and unhealthy working conditions, low level of skills and productivity, low or irregular incomes, long working hours and lack of access to information, markets, finance, training and technology; workers in the informal economy are not recognized, registered, regulated or protected under labour legislation and social protection; workers... in the informal

operate informally since government regulations frequently prohibit many of the most common abuses.


Informalization will also place downward pressure on wages and working conditions in formal jobs as well. Thus, the process of informalization proceeds in part through a vicious cycle: a relatively high proportion of informal jobs makes it increasingly difficult for workers to bargain for decent wages, working conditions and social protections, so that what had once been formal jobs become increasingly informalized over time.

There are numerous parallels between the process of informalization and more general concerns over worsening employment conditions and the growing prevalence of labor abuses. For example, anti-sweatshop activism in the countries of the global North in recent years reflects a heightened awareness over questions of international labor standards as they pertain to manufacturing and industrial protection. Similarly the question of child labor has assumed a greater urgency in international organizations such as the ILO and UNICEF.

Id.

Id.

Fallah, supra note 27, at 1.
economy are generally characterized by poverty leading to powerlessness, exclusion and vulnerability; most workers . . . in the informal economy do not enjoy secure property rights, which does deprive them of access to capital and credit; [workers in the informal economy] have difficulty accessing the legal and judicial system to enforce contracts and have limited or no access to public infrastructure and benefits; [and] women, young persons, migrants and all the workers are especially vulnerable to the most serious decent work deficits in the informal economy.80

The most prominently argued aspect of the informal economy that affects both informal and formal market participants stems from the non-payment of taxes for money earned informally.81 It is often argued that when informal market participants shirk their duty to pay taxes to the government, they are in fact “weaken[ing] government’s ability to provide public services and [are therefore] hamper[ing] economic development.”82 Although informal market participants receive the benefit of not having to pay the tax in the first place, these participants also have to face the cost of receiving less public services and having to contend with slower economic development in the community.83 Further, the taxes evaded by those in the informal economy may be collected, or may be perceived to be collected, instead from those already paying taxes in the formal economy.84 The perception or reality of this over-taxation of formal market participants may disincentivize those participants from both operating in the formal market and paying their own taxes.85 Finally, the presence of a large informal sector also tends to lower the overall productivity of a society because of the resulting lack of economies of scale.86 Because informal market participants need to avoid detection in order to keep operating, their businesses tend to be smaller than they would otherwise grow to be.87 Because of this artificial limitation on size, these firms do not have the purchasing power necessary to buy in bulk or dedicate labor to its most efficient use across the firm, advantages formal firms that grow sufficiently in the right markets do have.88 This limitation creates costs for both formal and

80 BACKGROUND DOCUMENT, supra note 32, at 3.
82 Fallah, supra note 27, at 1.
83 See id.
84 See, e.g., id. at 4.
85 See, e.g., id.
86 See id.
87 See id.
88 See id.
informal consumers and hinders economic development, generally. The factors that affect whether businesses operate in the formal or informal economy operate in the aggregate: that is, “What matters is how these factors combine together.”

Informal economies thus exist wherever these costs are outweighed by the benefits discussed above. That the benefit of operating informally more often outweighs the costs in developing countries than in developed countries seems to be a simple fact at present; that the costs remain also seems to be a fact. Because many of those costs relate to human rights abuses and ineffective economic development, development scholarship often cites formalization as a primary means to alleviate poverty and create the conditions necessary for economic progress.

Policy discussions calling for formalization often cite these costs to the individual and the larger costs to society as motivation for those calls. The formal economy, it is argued, provides the regulation and oversight necessary to correct human rights abuses, the access to credit and other banking services necessary to secure or expand businesses, and the fair allocation and collection of taxes necessary to provide the services that only a government can practicably deliver. Calls for formalization, however, often go unanswered; the next part explores the barriers to formalization that often explain why.

89 See id. Because the larger an informal business grows, the more likely it is that the government will detect the business and, perhaps, shut down the business, informal sector businesses tend not to grow such that the business would benefit from increasing economies of scale. Id.


91 Scholarship in this field frequently cites the ongoing costs of operating informally, especially in developing States, in terms of human rights, governance, and economic costs at the societal level. See BACKGROUND DOCUMENT, supra note 32, at 3.


93 See Fallah, supra note 27, at 6–8 (categorizing the policies attempting to formalize informal economies in terms of “reducing barriers to formalization, simplifying the tax system, enhancing enforcement, and building trust with the public”).

III. BARRIERS TO FORMALIZATION

Barriers to formalization generally fall into several categories: regulatory barriers, administrative barriers, fees and financial requirements, corruption in public administration, socio-cultural attitudes, lack of key business services, and criminality. The barriers that frustrate formalization the most are the regulatory barriers, administrative barriers, and fees and financial requirements, along with corruption in some States. These areas most significantly converge to form the barriers of taxation, business registration/licensing, and labor law.

Problematic regulatory barriers are those that "comprise inappropriate requirements and stem from a government policy-making environment" that does not encourage entrepreneurship. Those wishing to formalize in developing countries are especially prone to regulatory barriers because of the history of colonialism and neocolonialism:

In general, many developing countries are emerging from a history of heavy-handed regulation, with approvals required for even the smallest activity, and authority overly centralized and inflexible. This means they are hampered by the legacy of a heavily regulated economy and a command and control approach to administration and enforcement. Years of poor quality law-making has created a tangle of complex and inconsistent laws that present a daunting regulatory hurdle to the would-be formal enterprise. As such, the regulatory systems of these countries are not well developed to support a flourishing market economy that will create growth and formal jobs.

This unique history has only frustrated the formalization process in developing countries where formal financial services are lacking to start. This history has led to the extensive and onerous registration requirements that many scholars cite as a factor in the decision whether to participate in the formal economy or the informal economy.

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95 EMERGING BEST PRACTICE, supra note 11, at 11 (citing a SIDA fact-finding study, World Bank Doing Business reports, FIAS Investment Climate Surveys, and the SBP compliance cost survey of the informal sector).
96 Id.
97 Id.
98 Id. at 12.
99 Id.
100 Id.
101 See, e.g., WINTERBERG, supra note 39, at 4.
Administrative barriers are the bureaucratic requirements that flow from regulations, their implementation and enforcement. Even where a regulation is efficiently designed to accommodate entrepreneurship, its administration may prove to be a hassle, dissuading those wishing to formalize from doing so. Some barriers have to do with efficiency, some with the capacity of the administering agency, and some with the abuse of power by administrators.

Barriers presented by the fees and financial requirements of formalization "are caused by regressive fees which penalize smaller firms, overly complex tax regulations, and poor administration." Total costs of registering can certainly be a problem, as well as the costs of taxation and continuing compliance, but so too can minimum capital requirements for businesses wishing to obtain a limited liability status be a barrier for those wishing to formalize.

Many of the opportunity costs saved by operating informally, are, in fact, barriers to the formalization of informal market businesses and capital. That is, because of the onerous requirements to legally register a business in Peru, for example, informal market participants forego the time and money required to complete that registration and, thus, benefit by putting those resources to some more productive use. The time and money required to register a business in a given State, then, are barriers to the formalization of a business. Where the government bureaucracy in Peru was so oppressively endless, Hernando de Soto called his book on the phenomenon of the informal economy, The Other Path, because the poor were effectively locked out from the formal, legal path by the prohibitively high costs of compliance with the law and endless streams of red tape. In fact, in order to legally register a simple garment shop, an entrepreneur had to spend an average of 289 days working six hours a day at a cost equal to 36 times the Peruvian monthly minimum wage.

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102 EMERGING BEST PRACTICE, supra note 11, at 13.
103 Id.
104 Id.
105 Id. at 14.
106 Id.
107 These opportunity costs are discussed supra Part II.B.2.
109 See generally Leora Klapper, Luc Laeven & Raghuram Rajan, Entry Regulation as a Barrier to Entrepreneurship, 82 J. Fin. Econ. 591 (2006) (evaluating the empirical effects of regulatory barriers on the creation of new limited liability firms, the size of the new entrants, and the growth of those firms already participating in the formal market).
110 WINTERBERG, supra note 39, at 1.
111 Id. at 4.
Of course, registration and licensure fees are only the first costs incurred; once a business becomes formalized, it incurs many more costs to remain formal, including the costs involved with paying taxes and complying with labor laws, health and safety laws, and any other government regulations that pertain to the particular business. Each cost represents a barrier to formalization.

IV. ALTERNATIVE ROUTES TO ECONOMIC PROGRESS: MICROFINANCE AND COMMUNITY-BASED BANKS

One of the tools that has proven most effective in providing some financial services, and thus enabling some economic progress, to those otherwise shut out from formal financial service firms is microfinancing. This part examines the development and uses of microfinancing and similar locally-focused alternatives to traditional brick-and-mortar banks.

A typical transaction in microfinancing is one where a farmer seeks a small sum from a lender for crop production or livestock rearing or, more and more today, where an individual seeks a small sum so that individual can purchase the capital necessary to start an income-generating business. In either case, by paying off that loan, the individual becomes eligible to apply for another small loan in order to continue in or grow her business. For example,

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112 Id. at 2.
113 A useful and concise definition for "microfinance," a term which may carry several loaded meanings, for the purposes of this Note is provided below:

"Microfinance" is often described as financial services for poor and low-income clients. In practice, the term is often used more narrowly referring to services delivered by self-described "microfinance institutions" (MFIs) who usually use techniques developed over the last three decades to make and manage tiny uncollateralized loans. These techniques include group lending and liability, pre-loan savings requirements that test clients' willingness and ability to make regular payments, graduated loan sizes, and most importantly an implicit guarantee of quick access to future loans if present loans are repaid promptly.


In the Emergency Relief and Development Overseas’s Wezesha project in the Eastern Democratic Republic of Congo, for example, accountability and support throughout the lending payment process are assured by the procedures followed:

Once approved, each member receives a home and business visit and goes through a week-long pre-loan training process. After this, they receive their loans starting at $50 USD. They repay the loan... on a weekly basis...
two $200 loans to Costa Rican entrepreneurs enabled one to buy equipment to run a bakery out of her home and the other to buy materials to make garments from home.\textsuperscript{116} That small injection of capital was just what those entrepreneurs needed to create and sustain successful businesses and earn more than they would from wage-paying jobs doing the same types of work.\textsuperscript{117}

Microfinance focuses primarily on "alleviating poverty through providing services to the poor."\textsuperscript{118} As such, it "has grown to become an immensely popular strategy for reducing poverty."\textsuperscript{119} In fact, it is "one of the principal employment creating policies of today's development industry."\textsuperscript{120}

Because of this focus on alleviating poverty, most microfinance institutions are non-profit organizations dependent on government aid to function.\textsuperscript{121} An ongoing debate exists over whether microfinance should be self-sustaining and charging higher interest rates, diversifying services, and becoming more efficient,\textsuperscript{122} or whether microfinance "should reach deeper into the ranks of the poor."\textsuperscript{123} Also because of that focus, financial services provided by microfinancing institutions have historically prioritized the extension of small amounts of credit—microcredit—a practice that continues today.\textsuperscript{124} Microcredit lenders extend credit to borrowers that traditional banks view as too costly, too risky,\textsuperscript{125} or as simply not worth the investment.\textsuperscript{126} Some

\textit{Id.}

\textsuperscript{116} Lomax, \textit{supra} note 5.
\textsuperscript{117} \textit{Id.}
\textsuperscript{118} Barr, \textit{supra} note 6, at 278.
\textsuperscript{120} \textit{Id.}
\textsuperscript{121} See Barr, \textit{supra} note 6, at 278 & n.59. One study found that about 40\% of microfinance institutions were self-sustaining and not dependent on government dollars. That study, however, very likely tracked the better performing institutions. Therefore, although it may not be "that the industry as a whole is moving towards financial self-sustainability," it is arguable "that a significant part of the best institutions are doing so." \textit{Id.}
\textsuperscript{122} \textit{Id.} at 279 (citing, for example, Jonathan Morduch, \textit{The Microfinance Promise}, 37 J. ECON. LIT. 1569 (1999)).
\textsuperscript{123} \textit{Id.} (citing, for example, \textit{MICROCREDIT SUMMIT}, http://www.microcreditsummit.org/ (last visited Mar. 31, 2016)).
\textsuperscript{124} \textit{Id.} at 278.
\textsuperscript{125} \textit{Id.} at 279.
\textsuperscript{126} See \textit{id.} at 283 ("[T]he transaction costs in lending small amounts to lots of poor borrowers are high."); Patrick Honohan, \textit{Banking System Failures in Developing and Transition Countries: Diagnosis and Prediction} 30–31 (Bank for Int'l Settlements, Working Paper No. 39, 1997), http://www.bis.org/publ/work39.pdf (discussing that in developing countries, commercial and
microfinance institutions, though, offer a broad range of services like insurance, transactional services, and savings accounts, though on a small scale. 127

Whether providing microcredit, strictly, or providing a broader range of services, microcredit institutions use a variety of risk reduction strategies available only in the unique environments in which such institutions function. 128 For example, there have been instances where social pressures, including shaming, were used to increase pay-back rates on loans. 129 A variety of substitutes for traditional collateral and legal enforcement measures have been found in particular circumstances and those substitutes have often been successful. 130 Of course, the unique environments in which microfinance institutions operate also introduces and exacerbates some problems. 131 For example, two such problems are that the default rates on microloans are often quite high and that these institutions’ decision-making and accounting processes are not very transparent. 132

Some of these microfinance institutions, especially those that offer financial services in addition to the extension of small amounts of credit, are known as credit unions. 133 Credit unions are not-for-profit financial cooperatives, founded to correct the failure of the market to provide access to financial services for individuals of modest means. 134 Because financial services systems are not well developed or broadly accessible in many developing countries, credit unions arise to provide the lacking services, offering communities financial services while capturing the savings of the communities for their own economic growth. 135

"such banks have tended to confine themselves substantially to servicing the activities of foreign enterprises... and the trade finance requirements of the largest domestic enterprises").

127 Barr, supra note 6, at 278.
129 Barr, supra note 6, at 279.
130 Id.
131 Id. at 280.
132 Id.
135 Id.
Because of the many successes of some microfinance institutions, however, the microfinance industry has greatly expanded and continues to expand in both scale and the number of services offered, particularly in developing countries. With such expansion, the need for regulation and supervision increases to ensure the "security of the people's deposits and the soundness of the financial market." The next part thus begins from the understanding that the microfinance industry is growing to the point where regulation is necessary to protect the formal market, itself, from the many negative effects resulting from the economic growth of, and subsequent attempts to formalize by, previously informal players.

V. EASING THE TRANSITION

For reasons ranging from pure revenue generation to simply bettering the lives of those far away, calls for formalization have been heard since Hart and de Soto brought the informal masses into the conversation. This part argues that, because most formal economies are interconnected and interdependent, regardless of geographic location, a uniform means of facilitating both the extension of banking services to informal sector participants and the entry into the formal sector of the same may yield more benefits to all parties of interest, from individuals to local and national governments. To do that, this part examines the reasons for formalization, in light of the costs, benefits, and barriers discussed above, and then proposes that a supranational structure would best facilitate the transition from the informal economy into the formal economy. Part V.A first explains why formalization is a worthy end to pursue, both from the perspective of the individuals working off-book (that is, informally) and from the perspective of governments seeking to regulate their internal economic, social, and legal workings. Part V.B then argues that a supranational structure would be best able to facilitate the transitioning of particular informal participants into the global, interconnected, and interdependent formal markets by standardizing the formalization process itself. Finally, Part V.C recommends some particulars to guide the development of such a supranational body, specifically drawing on the experience of microcredit presented in Part IV.

136 See Mathurin Founanou & Zaka Ratsimalahelo, Incentives, Supervision and Regulation of Microfinance Institutions in the Developing Countries ¶ 3 (Munich Personal RePEc Archive, Paper No. 41428, 2012), http://mpra.ub.uni-muenchen.de/41428/.

137 See id.
A. Why Formalize?

Microcredit, at present, is one of the best proven means by which individuals can truly better their own economic circumstances. But it is not enough. As it is real people that are affected, the most persuasive evidence is perhaps anecdotal: in India, where the microcredit movement really began—a movement that won its sponsors a Nobel Peace Prize—several people have had to sell blood and even organs to repay loans they took from microlending companies. That is to say nothing of the fact that there is little empirical evidence that “microcredit borrowers, on average, commonly, directly, and quickly escape poverty, as many assume.” Thus, since the best thing we have got is not good enough, scholars and advocates for change call for something else—they call for formalization of the informal economies in which so many work for too little in substandard conditions.

The calls for formalization of informal economies propose everything from lessening regulation of the formal system to the level of the informal, to various schemes proposing the coexistence of the two systems, to intensifying regulation of the informal system to the level of the formal—thereby subsuming the informal into the formal. The experience of developed nations is part of the impetus for these calls as the formalization process “has very much been an integral part of the general economic development of industrialized countries.” Often, the call comes from the top-down where a government seeks reform, and seeks more tax dollars, among other goals.
Other, more altruistic calls come more from the bottom-up where development scholars and organizations like the ILO seek to improve the lives of the working poor across the globe. No matter the motivation, many of the same reasons for formalization are cited.

The case is generally made, for example, that governments will generate more tax revenue in the long term, creating the potential for a more prosperous society, if formalization is undertaken. Governments have always taken action to affect the size of the informal sector in order to counter the societal costs described in Part II.B.2. Burkina Faso, for example, created a special minimal tax for those who had never previously paid taxes, to try and shift them from the informal sector to the formal sector. Nigeria, too, has created a special council charged with developing small, informally operated businesses in order to grow its economy in the long term.

The case is also generally made that the lives of those involved in the informal economy will improve through formalization. As "work is central to people's well being," improving work conditions is often cited as a driving motivation for formalization. Recently, the ILO has focused on advancing a concept termed "Decent Work." The concept was developed by government representatives, employers, and workers, and recognizes that work is "a source of personal dignity, family stability, peace in the community, democracies that..."

See BACKGROUND DOCUMENT, supra note 32, at 1-3 ("In the context of the global decent work deficits, breaking out of informality is increasingly seen as the principal development challenge across regions. The issue is central to realizing decent work as a global goal and for all workers, for achieving the Millennium Development Goals (MDGs) and for promoting a fair globalization."). Because the question of formalization involves the motivations of individuals as well as governments, most arguments will cite incentives for all interested parties to formalization. See, e.g., Fallah, supra note 27, at 4-5.


Id.

Id.

See VANGUARD, supra note 15, ¶ 11.


deliver for people, and economic growth that expands opportunities for productive jobs and enterprise development.\textsuperscript{155} The decent work agenda includes job creation and training, guaranteeing rights at work, extending social protection, and promoting independent workers' and employers' organizations to advance the social dialogue.\textsuperscript{156} Because problems that arise in the informal economy "cut[] across all four pillars" of the decent work agenda, formalization of the informal economy has been a central focus for the ILO.\textsuperscript{157}

While the decent work agenda is pursued primarily by the ILO, other international organizations and States aiming to reform in similar ways pursue the same goals as those set out by the ILO.\textsuperscript{158} For example, in Ghana, Kenya, and South Africa, specific policy initiatives have been introduced to take action on employment and poverty reduction with reference to informal activities.\textsuperscript{159} Likewise, other regional meetings in Latin America and Asia have also addressed the problem of formalizing the informal economy in terms of poverty reduction.\textsuperscript{160}

The individual's perspective must never be forgotten, of course, as self-interest will drive any workable plan for formalization.\textsuperscript{161} Many argue that formalization will bring significant benefits to informally operating entrepreneurs, from access to capital to grow a business to better benefits for their employees and society in general.\textsuperscript{162} One argument is that businesses in the formal economy receive protections under the law, enabling businesses to promote themselves without fear of State reprisal, to enter into long-term and enforceable contracts, and to gain access to government support programs.\textsuperscript{163} A second argument is that the government's policies will better reflect the entrepreneur's needs and those of society, thanks to more comprehensive information about the private sector.\textsuperscript{164}

Many reasons thus exist to attempt to formalize informal economies. The existence of informal economies will likely never entirely cease, despite even the most successful attempts at formalization, as evidenced by the existence of informal economies in even the most developed countries with the

\textsuperscript{155} Id.

\textsuperscript{156} Id.

\textsuperscript{157} BACKGROUND DOCUMENT, supra note 32, at 7.

\textsuperscript{158} See id. at 5–8.

\textsuperscript{159} See id. at 5.

\textsuperscript{160} See id. at 5–8.

\textsuperscript{161} See discussion supra Part II.B.2; see also Fallah, supra note 27, at 12 (The basic calculation for a given individual thinking of formalizing a business is, essentially, "a profit maximization decision").

\textsuperscript{162} See Jansson & Chalmers, supra note 49, at 1; see also discussion supra Part II.B.1.

\textsuperscript{163} Jansson & Chalmers, supra note 49, at 1.

\textsuperscript{164} Id.
EASING THE TRANSITION

highest quality of governance and services. Nevertheless, formalization should be available to those informal market participants who do choose to formalize. The availability of the opportunity to formalize, however, is limited by regulatory and administrative barriers, discussed in Part III. The next section proposes that a means of getting around many of those barriers and of tipping the cost-benefit analysis toward engagement in the formal market lies in the development of a supranational body that would provide a uniform transition experience for informal market participants to formalize.

B. A Supranational Body Would Be Best Able to Facilitate Transition into the Global Formal Economy

As of 2005, some 30 States were either currently implementing or planning to implement formalization programs based on Hernando de Soto’s Peruvian model of streamlining business registration requirements and focusing on individual property rights. Other States, like Nigeria, are formulating their own creative responses to the problems presented by the informal economies that exist domestically. Although these local approaches should create solutions that best fit the particular problems in each State, they are not designed to provide the best means for transitioning the informal businesses and capital created at the local level into the formal structures common among developed States at the global level. In a world where the global economy is a reality, where geographically distinct markets are interconnected and interdependent, there should be a more uniform approach to formalization than that which exists today.

The very real problems of those involved in the informal economy are best addressed at the local level, by organizations or initiatives focused on

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165 For a discussion of the motivations of informal market participation in even the most developed countries, see Gërxtani, supra note 45, at 276–79.

166 See supra Part V.A for some humanitarian and economic reasons that the opportunity to enter the formal market should be extended to all.

167 WINTERBERG, supra note 39, at 1.

168 See generally VANGUARD, supra note 15 (describing the Nigerian government specifically developing a bank to handle the needs of the many micro- and small-business entrepreneurs in the State).

169 See supra note 16 for a discussion of how the “states as laboratories” approach will yield responses best fit to the particular conditions of the respective states serving as laboratories.

170 See, e.g., Paul Hirst, The Global Economy-Myths and Realities, 73 INT’L AFF. 409, 409 (1997) (“It is widely accepted by academics, journalists and politicians of all shades of opinion and in many countries that we now face the challenge of a truly globalized economy.”).

alleviating poverty and improving conditions. The transition into the formal economy, however, would be best addressed by a body above the local and even national levels. A supranational approach could set uniform minimum standards to which individual States or NGOs involved with advancement or reform of informal economies could look for guidance. These standards should be made available to every bank or financial services firm, no matter how informal, showing the businesses and their constituents what is, in fact, expected before one can interact with the institutions that comprise the global formal economy.

Such standards could limit the extent to which many of the barriers to formalization frustrate the process, currently. Uniformity of standards for firms wishing to transition would provide the necessary information for the firm to plan a move from informal practices to the formal practices mandated for entrance into the global economy. For example, firm A may be operating informally because it is in a State with little or no meaningful governance, a corrupt State. Firm B may be operating informally because the domestic registration requirements are too burdensome and regulations lax, making it unnecessary to properly register and enter whatever formal market is operating in the State. If firms A and B can access information about the agreed upon standards for a firm's entry—agreed upon by developed, formal economy participants in the global community—into the formal firms of the global economy, then firms A and B can circumvent domestic issues and bank wherever they choose, if they can prove to those institutions that they meet the standards provided.

Of course, this would seem to require that firms A and B meet the standards, themselves, before they would be granted access to formal economies. More realistically, however, firms A and B would operate with informal financial services firms or as part of community-based banks in their respective States before acquiring (and saving) the means to engage in formal economies. It is this intermediate level of governance that can best be leveraged by a supranational body setting rules and monitoring outcomes.

Uniformity of regulations and reporting practices for intermediate administrators of formalizing firms at the local or national levels would provide firms and governments in formal economies a systematic means of measuring almost endlessly diverse markets and firms. For example, community bank C and small, relatively informal microlending firm D each have 20 clients. Community bank C operates in a region of a State where over 90% of people work in agriculture. Microlending firm D, on the other hand, operates in the capital city of a State heavily dependent on manufacturing. Community bank C's clients are paid seasonally and use the bank primarily for savings accumulation. Microlending firm D's clients are paid weekly and use the firm to borrow small amounts of capital for their side businesses, collateralizing

172 See supra Part III for a discussion of those barriers to formalization.
their weekly earnings. Uniform regulations and reporting practices for the administrators of community bank $C$ and microlending firm $D$ would provide the supranational body, and then the formal firms and institutions, a means by which to compare the seemingly disparate business models and clientele of both bank $C$ and firm $D$.

After some time, these reports would provide a pool of information statistically significant enough to identify outliers, providing an effective and efficient means to monitor so many small players across the globe. National and regional trends could be identified by one body charged with oversight. Emerging markets could be identified more quickly by the sheer number of individuals and firms attempting to formalize, giving formal market participants better information about where and in whom to invest. Failing markets could also be more quickly identified and better-targeted assistance programs may be delivered where needed.

This approach does raise the possibility of the exploitation of emerging markets by formal market participants. However, if the supranational body were charged with a mission similar to the overwhelming majority of microlending organizations—that is, to “alleviat[e] poverty through providing services to the poor”—that possibility becomes less threatening. Exploitation becomes even less distinct a possibility if this supranational organization were put under the auspices of an internationally accountable organization, such as an arm of the United Nations. A supranational body such as this could usefully provide consistent encouragement and oversight of the formalization efforts of individual firms, forward-thinking communities, States, and NGOs active in this area. Such oversight should limit the corruption barrier to formalization.

Specifically, the creation of an NGO that specializes in facilitating transition into formal economies would allow those NGOs focused on improving the daily circumstances of those in the informal economy to focus on those particular efforts. It would allow each NGO to put their resources toward the areas in which they have the most expertise, making each more efficient in pursuit of its particular mission.

This would continue, to some extent, the current “states as laboratories” practice where States or NGOs help individuals and firms take the first steps toward meaningful formalization through creative solutions tailored to particular regions or communities. That would allow for the most efficient

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173 In statistics, the probability that the result of a given experiment or study can be attributed purely to chance decreases as the number of discreet data points increases. See *Statistical Significance*, DICTIONARY.COM, http://dictionary.reference.com/browse/statistical+significance (last visited Mar. 31, 2016). A result is “statistically significant” when that probability is very low. *Id.* Thus, the data collected from disparate and geographically diverse businesses and markets would provide a pool from which analysts from formal institutions could draw to determine whether a given individual, business, or market has met or substantially complied with the standards prescribed. See *id*.

174 Barr, *supra* note 6, at 278.
local solutions to immediate problems of those in the informal economy to be effectively managed. It would also, though, provide those wishing to transition into the formal economy with an expert and accountable body acting as a middle-man of sorts to guide them toward formalization into the global economy. This middle-man could make its expertise available to States, NGOs, or even individual people or businesses wishing to transition into and make the most of the global formal economy.

Of course, because of the sheer size of the informal economies of some States, accounting for 50% of GDP and perhaps 80% of some populations, what is proposed here does not seek to eliminate all informal economies around the world. Rather, what is proposed is merely a system in which those who seek formalization can more easily achieve it.

The next section recommends some particulars to guide the development of such a supranational body, specifically drawing on the experience of microfinance and community-based banking presented in Part IV.

C. Existing Microfinance Practices Should Be Leveraged to Facilitate Entry into the Global Formal Economy

As developed in Part IV, the microfinance industry is growing to the point where regulation is necessary to protect the formal market from the negative effects resulting from the formalization process itself. Because of the need for regulation in this area and the utility that microfinance and formal bank alternatives provide to those most in need of the protections that follow from participation in the formal market, this section argues that the proposed supranational organization should work with—and provide oversight of—those institutions and organizations active in providing microfinance services to leverage their expertise and local focus for the benefit of those populations both seek to serve. The proposed supranational organization should, therefore, be guided by the experiences of the institutions of whatever size and function that do the day-to-day work with informal populations. Currently, many of those institutions are microcredit organizations.

As the microfinance industry continues to expand, it is believed by some that microfinance institutions, with proper regulation, “will become self-sustainable and achieve massive outreach.” The supranational body proposed would regulate the industry to help the industry and individual organizations develop toward that end. Further, where the right conditions exist and any such

175 See supra notes 29–30 and accompanying text.
176 See supra Part IV.
177 See Founanou & Ratsimalahelo, supra note 136, ¶ 4.
institutions do become self-sustaining, some believe that these institutions can be easily formalized and integrated into the formal financial sector.\textsuperscript{178} This may be desirable in order to efficiently move a significant number of participants or blocks of capital, served by the institution, into the formal economy. It may also, however, deprive remaining informal market participants of the learned expertise of that organization. In either case, the proposed supranational organization would be in the best position to either facilitate formalization or the development of another microfinancing institution in the area potentially now-deprived of such service.

Further, if the proposed supranational body provided oversight of these institutions, especially in sectors of the economy that are repressed or ill-functioning, there would only be increased opportunities for the poor to “build assets, increase price competition and drive down interest rates, and lay the groundwork for banking sector development should legal institutions take root.”\textsuperscript{179} Some suggest that formal institutions like traditional banks “develop successfully only if a sufficiently large demand for bank loans materializes.”\textsuperscript{180} Therefore, microfinance institutions may be the necessary precursors to formal institutions taking root in an area. Likewise, credit unions as alternatives to formal banks seem to be natural precursors to more formal institutions participating as formalization begins. Thus, encouraging these types of practices to continue, but to be regulated under uniform standards, seems a promising incremental step toward formalization of the discrete communities in which the microfinance and other alternative institutions are active.

The approach argued for in this Note addresses Hart’s conception of the informal sector as “people taking back in their own hands some of the economic power that centralized agents sought to deny them”\textsuperscript{181} because the proposed supranational organization should be guided by a humanitarian mission, similar to the mission of many microcredit organizations, in seeking to achieve positive economic effects. This proposal is made so that the informal market participants, themselves—that is, the people working without industry regulation, safety codes, adequate pay, etc.—may see the benefits of industry regulation, codes, pay, and other regulable aspects that are more likely to result where the economy develops, generally.

VI. CONCLUSION

Because most formal economies are interconnected and interdependent, regardless of geographic location, a uniform means of facilitating both the extension of banking services to informal sector participants and the entry into

\textsuperscript{178} See id.
\textsuperscript{179} Barr, supra note 6, at 285.
\textsuperscript{180} Id. at 286.
\textsuperscript{181} Hart, supra note 26, at 158.
the formal sector of the same may yield more benefits to all parties of interest, from individuals to local and national governments. This Note proposes that a supranational organization accountable to a humanitarian mission statement—something to the effect of “to alleviate poverty by encouraging and facilitating access to formal market institutions by those in developing markets”—would be best positioned to facilitate informal market participants’ transition toward formal markets.

That organization could leverage existing arrangements between microcredit and other community-based banking alternatives and their clienteles. It could leverage its position to provide uniform standards downward to those clienteles to inform them of the particular formal market institution’s requirements for access. It could leverage its position to provide a standardized means by which to judge seemingly disparate businesses upward to the formal market institutions seeking new business.

Informal economies present problems to global economic development because those economies, by definition, are removed from the economies of the most advanced countries, those countries best able to help alleviate the severe conditions largely present in those places where informal economies develop and thrive. Extensive scholarship and simple logic demonstrate that where the benefits to be had by operating informally outweigh the costs of so operating, people struggling to survive day-to-day will almost always choose to operate informally. The proposal, here, is that a supranational body accountable to humanitarian principles would facilitate formalization in a way that best accounts for both humanitarian and economic interests of formal and informal market participants alike. This approach may yield more benefits than would otherwise be achievable to all parties implicated, from individuals to local and national governments. Such an approach, this author hopes, would fill coffers and stomachs all over the world.

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