ASSESSMENT OF INFORMAL BUSINESSES IN UGANDA

SPEICAL
REPORT
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STATEMENT BY THE MINISTER OF FINANCE, PLANNING AND ECONOMIC DEVELOPMENT

Hon. Matia Kasaija, MP
Minister of Finance Planning and Economic Development

I am glad to present to you this document on the assessment of the informal businesses as a summary of a survey and statements of the intent of various stakeholders in the sectors.

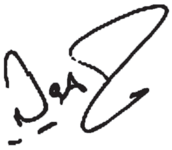
The informal sector also significantly influences subsistence households and is a source of employment for the vulnerable, especially the less educated, the youth and women.

This is where we ask the question(s) whether informality should be a direct target of formalisation; or whether it should be viewed as an indirect benefit of development, improved governance, better regulation, and improved public services. However, informal businesses are not uniform, and there is variability in their extent of informality, the scale of activity, sector of operation, gender of owner age of business, among other characteristics. This suggests that more differentiated definitions will support targeted interventions vital to cater for the varying need of businesses.

This document presents the next step in answering these questions. This document provides contextual interventions to manage the variability in the informal sector and accommodate businesses operating between fully formal and fully informal, thus showing some but not all dimensions of informality. This document also provides information on informality's political, legal, social, economic and cultural drivers.

In addition, this document also unveils the reasons why Interventions to incentivise business formalisation in Uganda over the past decades have shown mixed results and brought limited knowledge on how to address informality systematically. Despite the low membership of business associations, this document proposes business associations such as PSFU, KACITA, UMA, USSIA as a springboard on which government can leverage to formalise the informal sector business in Uganda.

I also note that this document proposes a road map for the conduct of other studies aimed at exhaustively understanding the informal sector. This document also envisages a walk away from ad hoc policy making to a more structured approach which may culminate into an overarching policy and strategy to enhance predictability and certainty in our policy direction. However, implementing such strategic actions does not happen in a vacuum. The business registration, tax administration and business development services have a key role to play, and it is here that we anticipate the most significant gains to be made. We will continue to support local governments, Uganda Registration Service Bureau (URSB), Uganda Revenue Authority (URA) and Enterprise Uganda (EU) to register businesses, collect taxes, and provide business development services efficiently. Therefore, we urge everyone to play their part in ensuring the proposal's success in this document.



Hon. Matia Kasaija, MP
Minister of Finance Planning and Economic Development

Ramathan Ggoobi
Permanent Secretary/Secretary to the Treasury

FOREWORD FROM THE PERMANENT SECRETARY/SECRETARY TO THE TREASURY

It is my honour and privilege to welcome the words of the Honourable Minister of Finance and acknowledge the guidance he has provided in developing this document. He has provided the leadership that has encouraged the investment that we needed and the consequent rapid growth in our economy, from which we all benefit today.

In this document, we take another important step towards creating a stronger, more independent, and better-equipped Uganda to set its own course through history and into the future. Similar to our peers, we have recognised the value that can come from understanding the informal sector for the development of the businesses sector that recognises that the informal sector is a source of livelihood and employment to the vulnerable, especially the less educated, the youth and women; while remaining fair to those who are legally and fiscally compliant.

Therefore, we have made it our duty to publish and share with the people of Uganda the document that details our survey results and statements of the intent of various stakeholders in the informal sector. This document will guide the government in implementing some of the advanced proposals and research going forward.

This document strengthens our resolve not to yoke our businesses with unnecessary administrative burdens. At the same time, we recognise that a small group of businesses bear a tax burden that should be shared with others. Many more businesses that benefit from the infrastructure and services provided by the government need to play their part and contribute as taxpayers so that we can all share in a better future. In this case, each business should pay a fair share of tax commensurate to its ability. Equally, to reduce informality, interventions vital to catering for the varying needs of businesses should be targeted regarding the extent of informality, the scale of activity, sector of operation, gender of owner, age of business, among other characteristics.

Given that most businesses are registered with local governments, we will make efforts to review the benefits that accrue from recognising and digitalising this simplified, intermediate, and temporary legal status for informal businesses to better align with business needs and government goals. We recognise the role of local governments in achieving this strategic goal. A review of unifying the registration forms for all agencies to avoid multiple registration points will be made. In the medium term, Uganda should boast a centralised, digitalised, unique identification system to enhance legal and fiscal formalisation.

This document provides a roadmap for the next steps concerning the implementation of the intervention and further research required to contextualise informality in Uganda. I recognise that we cannot take all the steps in our journey at once, some must follow on from the earlier steps, and that change needs to be thought through, discussed, planned and implemented in ways that are acceptable and over a period that is realistic. I acknowledge the invaluable contribution from all stakeholders, including the Secretariat for PSD/DPI Programmes, EPRC researchers, various organisations that shared their data, and the editorial team. I pledge on behalf of the government will continue to implement the report recommendations while continuing the engagement with stakeholders.

Ramathan Ggoobi
Permanent Secretary/Secretary to the Treasury

Anthony Kintu Mwanje
Coordinator Private Sector Development/Development Planning Implementation Secretariat at MoFPED

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This report would not have been possible without the leadership of the PS/ST, Undersecretary/Accounting Officer MFPED and the Head of the Private Sector Development Unit MFPED who solicited the funds and entered an MoU with the EPRC. Further, the report benefited from the leadership of Dr. Sarah Ssewanyanna and Dr. Ibrahim Kasirye, who led the EPRC research team that comprised of: Mr. Corti Paul Lakuma, Dr. Brian Sserunjogi, Mr. Ambrose Ogwang, Dr. Madina Guloba, Ms. Rehema Kahunde, Mr. Nathan Sunday and Mr. Maya Denis Makika. We also thank the EPRC communication team that facilitated the various policy engagement events. The team is comprised of: Ms. Elizabeth Birabwa Aliro and Mr. Alon Mwesigwa.

We also recognize the relent effort of the Quality Assurance Committee members that ensured that the report meets the research and communication quality and standards expected by stakeholders. The Quality Assurance Committee was chaired by Joseph Enyimu (MFPED), deputized by Francis Kisirinya (PSFU), and the other members of the committee were Dr. Peter Ngategize (PSDU/MFPED), Winnie Lawoko Olwe (UIA), Tina Kaidu (URA), Protazio Sande (IRA), Milton Muwoya (KCCA), Sophie Nampewo (CSBAG), Dr. Martin Francis Kyeyune (UMA), Anthony Kintu Mwanje (PSD/DPI Secretariat), Benjamin Mukiibi (URBRA), Mubiru Richard (PSDU/MFPED), Ndorere Cleopas (MTIC), Namanya Anthony (MoLG), Robert Muwanga (PSD/DPI Secretariat), Gorret Kajumba (PSD/DPI Secretariat) Nichodemus Nayebare (MFPED) and Sheila Lwamafa Nuwamanya (MFPED).

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Anthony Kintu Mwanje
Head, Secretariat for PSD/DPI Programmes - MFPED

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EXECUTIVE SUMMARY

Background

In the quest to encourage business formalisation in Uganda, several interventions have been implemented by the Government of Uganda. These are programmes and activities geared towards voluntary and involuntary registration and digitisation of records; the improvement of the external business environment through the development of enabling infrastructure and encouragement of the formation and mass enrolment to grass-root business associations; and strengthening of existing apex business associations such as PSFU, USSIA, UTODA, KACITA and UMA amongst others.

Despite these efforts, the interventions have shown mixed results and produced limited knowledge on systematically addressing informality. Adding to the challenge is determining whether informality should be a direct target or is instead something indirectly impacted through development, improved governance, better regulation and improved public services.

Methods

Based on a review of relevant literature on informality and analysis of a quantitative survey of 1,303 randomly sampled businesses and qualitative survey of stakeholders in the government, private sector, business assocaiations and development partners this study addressed the following broad objectives:

Objectives

a) Profiled the informal businesses in Uganda: nature, composition, and extent of informality and the main reasons for operating informally;
b) Identified the political, economic, socio-cultural, technological, environmental, legal, and regulatory gaps and incentives responsible for the persistent informality in Uganda; and
c) Assessed attempts and the effectiveness of the current and previous interventions aimed at promoting formal business operations and the reasons for their success and/or failure.

Key findings

(i) Most businesses (72 percent) in Uganda operate between fully formal and fully informal, thus showing some but not all dimensions of informality. We refer to this form of business informality as *either legal or fiscal informality*; Conversely, businesses that are fully informal, herein referred to *as both legal and fiscal informality,* are 28 percent of the total population of informal businesses.
(ii) The majority of business (70 percent) with *either legal or fiscal informality* are registered with local governments; and less by URSB (8 percent) and URA (1 percent);
(iii) Informal businesses are dominated by females, the youth and middle-aged, and less educated persons when compared to their male, the old and the more educated counterparts;
(iv) There is a high mortality rate for informal businesses. Close to 64 percent of informal businesses are 6 years or younger; only 36 percent are older than 6 years. Specifically, a high mortality rate is prevalent among businesses, which exhibit forms of *both fiscal and legal informality*;

(v) There is little value addition among informal businesses. Approximately 57 percent of the informal businesses are engaged in retail trade. However, businesses that have either fiscal or legal informality are marginally less likely to participate in the trading sector and have a significant representation in the industrial sector (11.5 percent);

(vi) While informality creates legal and fiscal distortions, informal businesses contribute 29 percent to GDP. There is also an untapped potential revenue of UGX 407 billion by businesses with turnover above UGX 150 million and whose extent of informality is either fiscal or legal;

(vii) There is little linkage between informal and formal businesses, only 12 percent of the informal businesses supply formal ones with inputs;

(viii) Informality persists mainly as a consequence of Uganda's turbulent political history, the structure of Uganda's economy that yields few jobs, and past economic reforms, which reduced the size of the public sector. There is also a lack of political will and accountability on the side of the government;

(ix) The persistence of informality is partly a consequence of a lack of information on registration fees paid by non-registered businesses, the recurrent and fixed cost of compliance and the number of days it takes to register. Other drivers of informality is the siloed nature of government agencies with regard to sharing of information,even where information is shared, Uganda lack a uniform identification system for registered businesses therefore it is hard to compare information across different agencies. This is coupled with agencies being at different levels of automation, with the majority still operating manual registers e.g local authorities, with the exception of KCCA;

(x) Interventions to incentivise business formalisation in Uganda over the past decades have shown mixed results and brought limited knowledge on how to address informality systematically. Past reforms such as TREP were limited in geographical coverage, understaffing and competing for agency priorities and responsibilities;

(xi) There is also little awareness of digitisation initiatives such as e-tax, Electronic Fiscal Receipting and Invoicing solution (EFRIS), Digital Tracking solution, the Voluntary Disclosure, among others; infrastructural deficits such as poor internet and power connectivity across the country also have a negative impact on the innovations; and

(xii) Business associations such as KACITA, UMA, USSIA, can be a springboard on which government can leverage to formalise the informal sector business in Uganda. However, only 11 percent of informal businesses belong to a business association. However, the mandate of most business associations has been restricted to advocacy on the cost and the provisioning of rent, licenses, competition between traders and hawkers and street vendors, and places of convenience at business premises.

Recommendations

(i) We propose a contextual definition of informal business, which focuses primarily on the dimensions of legal and fiscal informality. It follows that the term "legal informality" is used to refer to whether the business is registered or not with the Local Government (LG) and or Uganda Registration Bureau (URSB). While "fiscal informality" indicates how informal businesses pay income taxes to Uganda Revenue Authority (URA);

(ii) There is, however, a need to manage the variability found in the informal versus formal dichotomy and accommodate businesses operating between fully formal and fully informal; and thus showing some but not all dimensions of informality. For this purpose, we derive the concept of *either legal or fiscal informality*. Conversely, for those businesse that are fully informal, we refer to them as *both legal and fiscal informality*;

(iii) More differentiated definitions are encouraged to support targeted interventions vital to catering for the varying need of businesses regarding the extent of informality, the scale of activity, sector of operation, and gender of owner age of business, among other characteristics;

(iv) Given that most businesses are registered with local governments, there is need to recognise and digitalise this simplified, intermediate, and temporary legal status for informal businesses to better align with business needs and government goals. Specifically, registration, support to businesses and compliance monitoring should move from central government arena and become more firmly established at local government level;

(v) There is a need to unify the registration forms for all agencies. Precisely, avoiding multiple registration points. In addition, a creation of a centralised digitilised unique system of identification will enhance both legal and fiscal formalisation efforts;

(vi) Formalisation efforts should target older businesses that have *either fiscal or legal informality*. It follows that efforts to improve business productivity, such as business development services and the creation of informal clusters, should target younger businesses that have *both fiscal and legal informality*;

(vii) Businesses with *either fiscal or legal informality* or whose turnover was above UGX 150 million would ideally qualify for corporate taxation and are ripe for formalisation. Their continued untaxed status lends credence to the perception that the government is practising discrimination in taxation;

(viii) Awareness campaigns on legal and fiscal registration requirements is imperative; especially among businesses whose extent of informality is *both fiscal and legal*. There is a need to reduce corruption at tax administration and registration services to eliminate the hidden cost of formalisation. In addition, there is a need for simplifying the processes and procedures of using the digitisation equipment procured by legal and fiscal administrative units and heavily intensifying publicity about their existence;

(ix) Business associations should participate more in awareness programmes and basic business development support services such as business training and other administrative support to build awareness about formalisation initiatives among their members; and

(x) There is a need for a national policy and strategy to segment businesses by the extent of informality and characteristics of the owner and business; and define the boundaries, constraints, actors and put in place initiatives to improve the formal-informal relationships.

ACRONYMS/ABBREVIATIONS

BCI	Business Climate Index
BDS	Business Development Services
COBE	Census of Business Establishment
COVID	Corona Virus Diesease
DLGs	District Local Governments
DPI	Development Planning Implementation
EFRIS	Electronic Fiscal Receipting and Invoicing Solution
EMTR	Effective Marginal Tax Rate
FGDs	Focus Group Discussions
FSME	Federation of Small and Medium Enterprises
GDP	Gross domestic product
ICT	Information Communication Technology
ILO	International Labour Organisation
ISIC	International Standard Industrial Classification
KACITA	Kampala City Traders Association
KCCA	Kampala Capital City Authority
KIIs	Key Informant Interviews
LC	Local Council
LG	Local Government
MDAs	Ministries, Departments and Agencies
MoFPED	Ministry of Finance Planning and Economic Development
MSMEs	Micro Small and Medium Enteprises
NDP 3	Third National Development Plan
NSSF	National Social Security Fund
PEAP	Poverty Eradiction Action Plan
PSD	Private Sector Development
PSDU	Private Sector Development Unit
PSFU	Private Sector Foundation Uganda
PSU	Primary Sampling Unit
SACCOs	Savings and Credit Cooperative Organisations
SMS	Short Message Service
SSU	Secondary Sampling Unit
TIN	Tax Identification Number
TREP	Tax Registration Expansion Programme
UBoS	Uganda Bureau of Statistics
UGX	Uganda Shillings
UMA	Uganda Manufacturers' Association

UNDP	United Nations Development Programme
UPE	Universal Primary Education
URA	Uganda Revenue Authority
URSB	Uganda Registration Services Bureau
USE	Universal Secondary Education
USSD	Unstructured Supplementary Service Data
USSIA	Uganda Small Scale Industries Association
UTODA	Uganda Taxi Operators and Drivers' Association
UWEP	Uganda Women Entrepreneurship Programme
YLP	Youth Livelihood Programme

1. INTRODUCTION

There are many definitions of informal sector; but most of definitions converge on the idea that the informal sector includes businesses, workers, and activities operating outside the legal and regulatory systems (World Bank, 2020). The informal sector accounts for 25 to 40 percent of GDP and often more than 60 percent of employment in emerging and developing economies (*ibid*). While Uganda does not have an operational definition of its informal sector, a variety of past attempts to broadly estimate informality in Uganda have suggested that it is large; holds significant influences on subsistence households; and grows out of the inability of the formal sector to create sufficient and dignified jobs to absorb the vulnerable, especially the less educated, the youth and women, who are mostly unskilled and lack capital or social networks to get ahead (Esaku, 2020 and Fourie, 2018).

Informality is also an outcome of other political and socioeconomic factors. Informality pauses a structural constraint on revenue growth and leads to inequitable distribution of incomes and productive resources as most informal businesses operate beyond the sight of the tax system. The latter impacts fairness among businesses and significantly raises the tax burden faced by compliant businesses as the tax authority strives to meet the country's domestic revenue targets (MoFPED, 2019). The tax burden is further worsened by the fusion of the national and subnational taxes.[1] For example, MoFPED (2019) estimates that the informal sector accounted for about 51 percent of the total GDP in 2017/18. The scale of the informal sector in Uganda and similar emerging and developing economies merits rethinking approaches to formalisation. Notably, it is important to ask whether informality should be a direct target of formalisation; or whether it should be viewed as an indirect benefit of development, improved governance, better regulation, and improved public services (World Bank, 2009).

Although the informal sector consists of informal businesses, workers and activities (an inherent interdependence); for ease of scope, this study focuses on informal businesses. While some overlap exists between informal businesses and informal workers (self-employed individuals in developing economies may be both), this study views informality through the business lens. This is to build a working definition for the government, the private sector,the civil society, development partners and other stakeholders that will enable research and reform efforts to nudge informal businesses toward adopting formalisation. Once formalised, this will also enable support for them as envisaged in the Private Sector Development (PSD) and Development Planning Implementation (DPI) result framework of the NDP 3. Specifically, the PSD and DPI result framework aims to deepen informality reduction and a streamlining of taxation at national and local government levels to strengthen budgeting and resource mobilisation.

In the quest to encourage business formalisation in Uganda, several interventions have been implemented by the Government of Uganda. First, the government has established programmes and activities geared toward voluntary and involuntary registration and digitisation of records, such as the Taxpayer Register Expansion Programme (TREP), a simplified tax system through the presumptive tax regime, initiated the National Identification Register, and the National Internet Backbone Infrastructure. Second, improving the external business environment through the development of enabling infrastructure, which encourages fiscal legitimacy and voluntary registration, is pertinent. These infrastructure projects include market facilities for street vendors, expansion of electricity generation, increase in the national and feeder road network, and creation of one-stop business centres. Third, the government is encouraging the formation and mass enrolment of grass-root business associations; and strengthening existing apex business associations such as Private Sector Foundation Uganda (PSFU), Uganda Small Scale Industries Association (USSIA), Uganda taxo Operators and Drivers Association (UTODA), Kampala City Traders Association (KACITA) and Uganda manufacturers Association (UMA), amongst others. Business Associations have been shown to facilitate

1 Also, under informality, jobs and business activities are not registered or protected by the State. They don't enjoy any social or economic benefits, and often have no titled or registered assets. This means they are inherently vulnerable, highly mobile, and insecure. As a consequence, these unregulated entities find it difficult to enter contractual obligations and access credit from financial institutions and donot pay taxes.

the capacity to self-regulate, especially concerning encouraging voluntary business registration and tax compliance; standardising output; accessing the export market; and enhancing synergies and the bargaining power of business enterprises.

Despite these efforts, the interventions have shown mixed results with respect to increasing business formalisation; and have produced limited knowledge on systematically addressing informality. Adding to the challenge is determining whether informality should be a direct target or is instead something indirectly impacted through development, improved governance, better regulation and improved public services. This calls for the development and testing of new approaches to informality based on a deepened understanding of the needs of informal businesses. Past pro-formalisation interventions stand out in the inappropriate segmenting and targeting of businesses (Lakuma *et al.,* 2019). More differentiated approaches may be needed. For example, regulatory simplification of business registration alone may not be attractive enough for the smallest subsistence/household businesses where the costs of formalisation much outweigh the benefits. An intermediate legal status to support the formalisation of the status quo could potentially be a beneficial first step. Larger, more dynamic and growth-oriented informal businesses might be better targeted through strategic public support—that addresses specific obstacles limiting their pursuit of formalisation, rather than indirect universalistic support based on deregulation. This can include targeting those firms most likely to formalise and/or with the lowest opportunity cost to formalise.

The rethinking of approaches to formalisation is even more relevant in the current context of the COVID-19 pandemic. Many formal businesses, hit hard by the pandemic's economic effects, are likely to be forced to pursue income sources through unregistered economic activities, increasing the scale of the informal sector despite its deficiencies as a safety net. Furthermore, both formal Micro Small and Medium Enterprises (MSMEs) that fall into informality and already informal businesses have limited access to government support, increasing their instability and risk of closure. COVID-related growth in the informal sector accentuates the need for appropriate and strategic policy responses.

Based on a review of relevant literature on informality and efforts to promote formalisation and analysis of a quantitative and qualitative survey, this study addresses the following broad objectives: a) profiles the informal businesses in Uganda: nature, composition, and extent of informality and the main reasons for operating informally; b) identifies the political, economic, socio-cultural, technological, environmental, legal, and regulatory gaps and incentives responsible for the persistent informality in Uganda; c) assesses attempts and their effectiveness of the current and previous interventions aimed at promoting formal business operations, and the reasons for their success and/or failure.

The rest of the study is as follows: section 2 explains the study's methods. The subsequent sections presents the results and conclusion to the study. Notably, section 3 characterises informal businesses. Section 4 explains the factors that underpin informality. Section 5 explains governments' past interventions and section 6 analyses the impacts of COVID-19. The conclusion and emerging policy messages are in section 7.

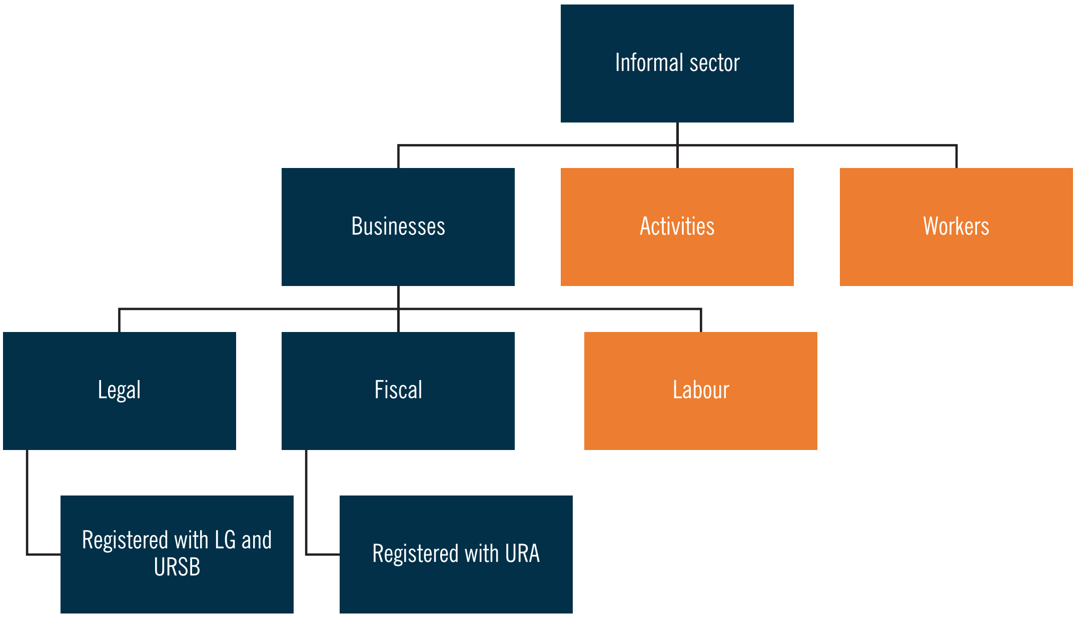
2. METHODOLOGY

This section offers a definition for informality, which facilitates in the scoping of the study. In addition, this section presents the design adopted to collect information from all the relevant sources to find answers to the research questions.

2.1 Definition of informality

This study adopts the conceptualisation by (World Bank, 2020), which defines the informal sector as businesses, workers, and activities operating outside the legal and regulatory systems. Although the informal sector consists of businesses, workers, and activities (an inherent interdependence), this study focuses on informal businesses, as marked in red in Figure 1. The latter two dimesions, workers and activities, were not examined because they would require a household survey, which the project resources in terms of time

Figure 1 Definition of informality



Source: Authors' construction based on World Bank (2020)

and money could not accommodate. Nonetheless, the term "informal business" encompasses three profiles and dimensions of informality: legal, fiscal, and labour. These dimensions are not exclusive, as businesses may be informal across any or all of these dimensions and may cycle in and out of informality. As a result, the term "informal business" can overlay many different business profiles. However, informal businesses exclude non-market production of goods by households, downstream agriculture activities such as weeding and planting, paid and unpaid domestic services, and volunteer services rendered to the community (ILO, 2012).

This study focuses primarily on legal and fiscal informality dimensions, as marked in red in Figure 1. The study de-emphasizes labour informality because the law covers only employers who have five or more employees aged between 16 and 55 years.[2] Most informal businesses tend to fall below the employment threshold of five employees. For this reason, labour informality was excluded because of predicted non-response to question that entail labour informality such as registration and submission of dues to National Social Security Fund (NSSF). In addition, the survey respondents where business owner and/ or manager and not workers. A business owner/manager may only provide generic or exaggerate information on worker welfare.

For this study, the term "legal informality" is used to refer to whether the business is registered or not with the Local Governments (LG), LGs register through keeping record for collection of dues and through issuance of permits and licenses; and or Uganda Registration Services Bureau (URSB).[34] While "fiscal informality" indicates the extent to which informal businesses pay taxes to Uganda Revenue Authority (URA).[5]

2.2 Design of the study

The study employed three methods enumerated below; namely desk reviews, quantitative and qualitative analysis.

2.2.1 Desk review

This involved a review of the extant informal business-related literature, mainly from the World

2 "Labour informality" reflects whether contracts and benefits are made available to employees.

3 See Figure 1
4 LG is interchangeably referred to as Local Authorities
5 Fiscal informality may include businesses that have bank accounts, and maintain book-keeping. However, for simplicity, this aspect is ignored in the construction of the definition of what informal business is.

Table 1 Sample and response rate of informal businesses

Sector	Central	Eastern	Northern	Western	Total from sample	Total from interview
Agriculture	33	0	13	14	60	*31*
Industry	28	0	3	10	41	*82*
Trade	281	18	86	229	614	*669*
Hotels , restaurant e	103	10	38	89	240	*108*
Services exc. Trade and transportation	117	5	28	71	221	*153*
Others services	65	6	15	41	127	*122*
Total from sample	627	39	183	454	**1,303**	
Total from interview	*560*	*31*	*140*	*434*		***1,165***

Source: Informal Business Survey 2021.

Bank, International Labour Organization (ILO) and development agencies such as United Nations Development Program (UNDP). The study also reviewed government policy documents such as the Background to the Budget, Ministerial Policy Statements, and the 2015 Uganda Micro, Small, and Medium Enterprise (MSME) Policy.

2.2.2 Quantitative data collection

Quantitative data collection entailed using a structured questionnaire to collect data from individual informal businesses to answer questions on character, incentives, and past intervention relating to informality.

Sampling procedure and sample size

Prior to the survey, a two-stage stratified sampling procedure was used to pick a sample from the 2018 Census of Business Establishment (COBE) sampling frame of the Uganda Bureau of Statistics (UBoS). The Primary Sampling Unit (PSU) was the region, while the Secondary Sampling Unit (SSU) was the sector. The PSU was picked from Enumeration Areas in the five statistical regions of Kampala, Central, West, North and East. The SSU was picked from the sector stratification conforming to level four of the International Standard Industrial Classification (ISIC).[6]

Using the two-stage stratified sampling method, a sample size of 1,303 informal businesses were selected, taking into account both sampling and non-sampling error (Table 1).[7] The sampling size was determined by a statistical formula that is based on the total business population in each region and sector and the margin of error.[8] Table 1 suggests that the central region and the trade sector had the largest share, 627 and 614 informal businesses respectively. At least 1,165 informal businesses responded to the survey (Table 1), indicating a response rate of 89 percent. A disaggregation suggests that informal businesses in the trade sector overwhelming participated in the survey. This was primarily due to the use of informal businesses in the trade sector to replace non-responding businesses. Informal businesses in the trade sector form a significant majority of businesses in the 2018 COBE sampling frame.

Weighting

To ensure that the results are representative of the entire informal business population in Uganda, sample weights were generated and applied in the analysis. The approach for generating the sample weights is summarized in Appendix A. Table 2 suggests that the weighted sample has a total of 2,238,886 businesses. Up to 1,607,266 businesses had *either Fiscal or Legal*

6 The size stratification was de-emphasized because an overwhelming majority of informal businesses are either micro or small. The 2015 Uganda Micro, Small, and Medium Enterprise (MSME) Policy defines business with less than five workers as micro, those with 5 to 49 workers as small, 50 to 99 as medium and more than 100 as large.

7 The sampling error is inversely proportional to the square root of the sample size, implying the higher the sample size, the small the sampling error. On the other hand, the non-sampling error may actually increase with the sample size.

8 $n=\frac{N}{(1+N*e^2)}$, where n is the sample size, N is the total number of industries, e is the margin of error (the preferred being 5%).

Table 2 Weighted sample of informal businesses by classification

	Total	Percentage
Number of firms	**2,238,886**	**100**
Informality		
Either Fiscal or Legal informality	1,607,266	71.8
Both fiscal and legal informality	631,620	28.2
Industry		
Agriculture	23,816	1.1
Industry	91,557	4.1
Trade	1,237,293	55.3
Hotels , restaurant eating places	432,321	19.3
Services exc. Trade and Transportation	164,019	7.3
Others services	289,881	12.9
Size by employment		
Less than 5 workers	2,078,754	92.8
5-49 workers	160,132	7.2
Size by turnover		
Not exceeding 10 million	1,371,351	61.3
>10 million to 30 million	538,815	24.1
>30 million to 50 million	149,250	6.7
>50 million to 80 million	64,078	2.9
>80 million to 150 million	38,500	1.7
Excess of 150 million	43,960	2.0
Sex		
Female	1,229,584	54.9
Male	1,009,302	45.1

Source: Informal Business Survey 2021.

informality, while 631,620 businesses had *both fiscal and legal informality*. Sector-wise, the *trade sector* has the highest representation with 1,237,293 businesses. Most (2,078,754) informal businesses have less than five workers. Most (1,371,351) informal businesses are exempt from taxation for they fall below the schedule of *Not exceeding 10 million* in turnover. Lastly, most (1,229,584) businesses are female-owned.

2.2.3 Qualitative data collection

Institutional and policy issues affecting informal businesses could not be adequately captured quantitatively, yet those issues are critical for enhancing the compliance and productivity of informal businesses. To address this, the survey employed a qualitative approach, which was executed using Key Informant Interviews (KIIs). More specifically, KIIs were used to solicit information concerning the role played by different institutions in business development, policy and institutional impediments to informal compliance, plans and reforms to foster regulatory compliance of informal businesses. A total of 13 KIIs were conducted. These were drawn from Ministries, Departments and Agencies (MDAs), District Local Government, development partners, civil society organisations, grass-root, and apex business associations. In addition, Focus Groups Discussion (FGDs) were used to collect data from community Self-Help Groups, cooperatives/aggregators, and Savings and Credit Cooperatives Organisations (SACCOs) among others. The key informants and focus groups list is provided in Appendix B: Table A1. Most importantly, the staff of the Development Planning Implementation (DPI) secretariat and Private Sector Development Units (PSDU) of the Ministry of Finance Planning and Economic Development (MoFPED), were involved in the design and data collection.

2.3 Analysis

The data collected were analysed using descriptive statistics with sufficient level of rigour. The quantitative data was triangulated with qualitative information to fill the gaps that could not be quantified.

3. CHARACTERISATION OF INFORMALITY

This section characterises informal businesses by the extent of informality; business and owner characteristics; and use of records, technology and source of inputs. The section also examines the actual and potential contribution of informal businesses to the economy, taxation, employment, and linkages with the formal sector regarding the supply and use of inputs. The section ends with an analysis of the growth and development potential of informal businesses regarding their ability to transcend their size and sector at establishment.

3.1 Extent of informality

Informal business as a concept has been elusive not only as a category given its many possible associations but also as a traceable entity given its mobility and lack of visibility. However, the use of the term "*informal business*" has been matched with efforts to develop more precise definitions that lend themselves to statistical estimation. Based on the World Bank (2020) methodology, this section develops guidelines for harmonising and improving informal business measurement in Uganda and elsewhere. In addition, this section describes the remaining challenges for measurement and data collection.

For this study, the term "*informal business*" encompasses two profiles and dimensions of informality: legal and fiscal. In this study, and as earlier mentioned, "legal informality" refers to whether the business is registered with a LG (these are Kampala Capital City Authourity (KCCA), District Local Governmenets (DLGs), Municipals and Divisions) and Uganda Registration Services Bureau (URSB) and has a trading license; and "fiscal informality" indicates the extent to which informal businesses pay taxes to URA.

Panel A of Figure 2 examines the individual variables used to measure the extent of legal and fiscal informality. In this regard, Figure 2 suggests 30.1 percent of informal businesses are not registered with local authorities (interchangeably used to mean LGs), 92 percent are not registered with URSB, 99 percent are not registered with URA and 26 percent do not have a trading license. A KII suggest that *"Local authorities have an easy process of registration i.e. the municipal council has a team that conducts field visits in various business communities; the process is as simple as collecting the contact details of the business such as the name of the owner, phone contacts, email address, where the owner stays, the type of business and its location. Picking this information marks the end of registration with local authorities".*

In this case, while URSB Act Cap 210 mandates the Bureau to register all business entities in Uganda which are required by law to be registered, that has not not been the case. Instead most business have pursued less legalistic forms of registration with local authorities and trading licenses. This is likely because LGs are relatively closer and accessible to businesses and enjoy some extent of legitimacy when compared to URSB. URSB is also perceived to be expensive and detached from the people. This calls for recognition of these simplified, intermediate and temporary legal status provided by LGs as a form of legal compliance. However, most registers at LGs, except KCCA are manually managed and do not have a unique identifying number that can be used to trace compliance. Nevertheless, some LGs have made steps towards digitilising their business records. A KII suggest that *"the central division of Fort portal municipal council, for example, has a business register which is computerised (stored in an excel sheet). All the above information is captured and stored for reference purposes in case of non-compliance"* (KIIs, Thursday, October 14th, 2021).

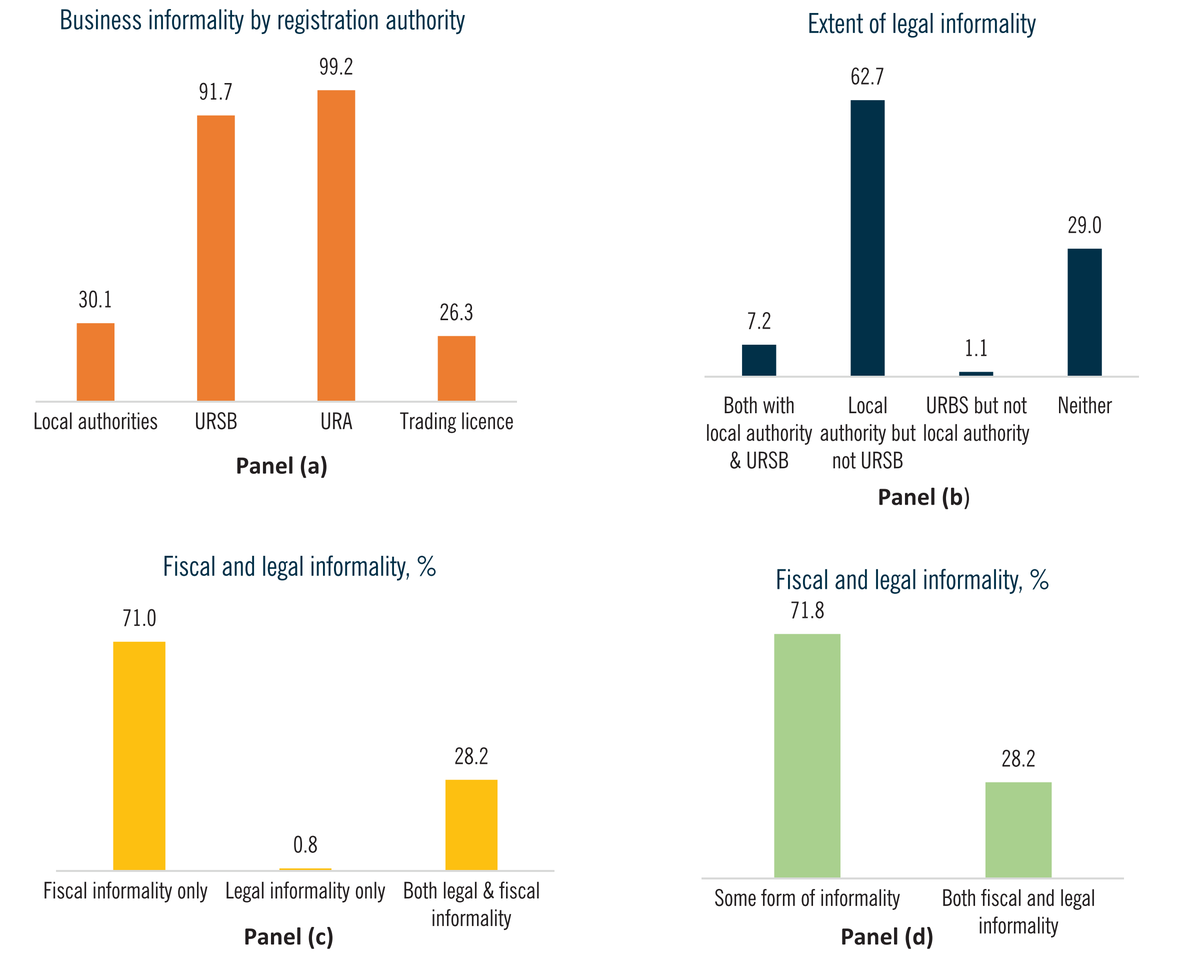
In addition, a KII suggested that *businesses, especially the small ones, are not interested in registering their businesses with URA due to high taxes charged by URA relative to the dues charged by local authorities. Most small businesses believe that registration with URA is for the big businesses. There is a lack of sensitisation about the need to register with URA and URSB. (KIIs, Thursday, October 14th, 2021).*

In Panel B of Figure 2, the trading license is dropped due to its skewed statitiscal distribution, which would present a bias. The omission of licences does not affect our results since an overwhelmimg majority of license holders also pay market dues and acquire permits. As a result, Panel B suggests that only seven percent of informal businesses are registered with both local authorities and URSB. At the same time, 63 percent are registered with local authorities but not URSB. Conversely, only one percent of informal businesses are registered with URSB and not local authorities. As earlier mentioned, local authorities form a stronger platform for formalisation than URSB; this could be used as a vehicle for business registration because they are closer and trusted by the people. There are perceptions that registration with URSB involves many unnecessary administrative steps and often require multiple interfaces with government officials, which could potentially encourage corruption and rent-seeking behaviour. For example, a KII suggested that *"Some people just pay to one enforcement officer and (they) run their businesses uninterrupted", (KIIs, Thursday, October 14th, 2021).* This perception is further exacerbated by the general lack of information about registration requirements and procedures. The lack of coordination between government agencies and insufficient Information Communication Technology (ICT) solutions to integrate and streamline administrative processes hinders the efficient regulation of business.

Panel C of Figure 2 combines the two profiles and dimensions of business informality: legal and fiscal. Panel C suggest that 71 percent of informal business are legally compliant; only 0.8 percent are fiscally compliant, and 28 percent are not compliant both fiscally and legally. The actual presumptive tax payers are 16,245 (Waiswa *et al.,* 2021). This is close to 0.8 percent (17,911 informal businesses) estimated by this study. The presumptive tax schedule is the pro-rated income tax imposed on registered businesses. However, it should be noted that presumptive taxpayers are inconsistent taxpayers they pay in one year and there is no guarantee that they pay in next years. The exact number of presumptive taxpayers is therefore difficult to tell. Part of the problem is because no one is registered as a presumptive taxpayer. It is only when they make payments that we can tell who are presumptive.

Panel D of Figure 2 derives the two variables that this study uses to measure business informality: *either legal*

Figure 2 **Extent of business informality**



Source: Informal Business Survey 2021.

or fiscal informality; *or both legal and fiscal informality*. The former helps to manage the variability found in the informal versus formal dichotomy and represents businesses operating between fully formal and fully informal; thus showing some but not all dimensions of informality. Panel D suggest that such businesses are 72 percent of the sample. The latter represents those fully informal businesses and such businesses are 28 percent of the sample.

3.2 Business owner and individual business characteristics

The business owner and individual business characteristics (e.g., education, gender, age, source of funding, record-keeping, technology use and source of inputs etc.), as factors of informality, are shown to be influential in increasing the rates of formalisation. However, characteristics appear to encompass only a part of the story, as many other comparable businesses do not formalise (World Bank, 2020). Nevertheless, the disaggregation of businesses and business owners by their characteristics is important in revealing the differences in the extent of informality and how businesses and business owners perceive the different factors of formality. For targeted policy intervention, this section examines business and business owners' characteristics by the extent of informality (*either fiscal or legal* informality; or *both fiscal and legal* informality).

3.2.1 Business owner characteristics

It is worth noting that persons involved in informal activities differ widely in terms of income level, age, gender, education level, among other indicators. Indeed, Table 3 reveals that females are more likely to participate in an informal activity relative to males. Overall, Table 3 suggest that women own 56 percent of informal businesses in Uganda. The dominance of women is sustained even after disaggregating the extent of informality: *either fiscal or legal* informality*;* or *both fiscal and legal* informality. The findings corroborate others, which found a higher proportion of women in informal employment than men, especially in low-income countries (Hussmanns, 2018).[9] This questions the structuring of government interventions such as the *Uganda Women Entrepreneurship Programme (UWEP)* and the *Presidential Initiative of Skilling the Girl Child* aimed at empowering women, particularly by reducing informality among women.

The findings also reveal that middle-aged (31-54 years) and young (18-30 years) people are more likely to own informal businesses compared to the elderly (55 years plus). According to UBoS (2019), the *2018/19 National Labour Force Survey* suggest that the youth and middle-aged people dominate the informal activities outside agriculture.[10] Indeed, Table 3 shows that 62 percent and 33 percent of owners of informal businesses are middle-aged and youth, respectively. On the one hand, middle-aged people have accumulated some savings, which they use to start up informal businesses. On the other hand, the high rate of youth unemployment (13 percent as of 2018/19) has made the youth embrace informal businesses out of necessity.[11] This questions the effectiveness of targeted interventions such as the *Youth Livelihood Programme (YLP)*, forcing many young people to venture into informal activities as a source of livelihood.

Furthermore, Table 3 shows that 34 percent and 41 percent of the overall informal business owners are primary and secondary school dropouts, respectively. Further disaggregation by the extent of informality suggests that there are no differences between businesses that are *either fiscally or legally informai*; and those that are *both fiscally and legally informal* regarding the level of education of business owners. Both are invariably primary and secondary school dropouts. This further suggests that informality could be an outcome of the effectiveness of *Universal Primary Education (UPE)* and *Universal Secondary Education (USE)*. It is likely that low levels of education contribute to the increasing number of young people joining the informal sector. A KII suggest that, *"low levels of education also lead to a language barrier in reading information about formalisation. This suggest that there is a missing market for translation of businesses*

9 https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_626831.pdf

10 https://www.ubos.org/wp-content/uploads/publications/05_20212018-19_ALFS_Report_FINAL.pdf

11 https://www.ubos.org/wp-content/uploads/publications/05_20212018-19_ALFS_Report_FINAL.pdf

information into local languages," (KIIs, Tuesday, October 19th, 2021).

This evidence is consistent with both the international and local literature, which associates informality with low levels of education. For instance, Yusuff (2011) and Meghir *et al.,* (2015) suggest that the lack of proper education has been responsible for locking people outside the formal economy and thus increasing the informal economy's size in developing countries economies. In Uganda, a bulk of businesses such as eating kiosks, fish selling, and shoe shining, among others, require no specialised skill to operate and are mainly run by school dropouts and those with no formal level of education (Mugoda *et al.,* 2020). Table 3 suggests that 32 percent of informal business owners were previously in self-employment. This could be related to the previously mentioned low levels of education that have made people seek self-employment out of necessity.

3.2.2 Business characteristics

Table 4 profiles the nature of informal businesses in Uganda. Particularly, the study focuses on the business' age, the industry of operation, business location, how the business was acquired, the source of start-up capital, and the reasons for starting or joining an informal business. Regarding business age, Table 4 suggests that 64 percent of informal businesses are 6 years or younger; only 36 percent are older than 6 years. The literature negatively associates business' age with informality, which may explain the persistence of informal businesses (Dabla-Norris *et al.,* 2008). This evidence points to the many challenges, including lack of credit, faced by Micro Small and Medium Enterprises (MSMEs) in Uganda, which leads to a high mortality rate (Lakuma *et al.,* 2019). A disaggregation suggests that a majority of businesses designated to have *either fiscal or legal* informality are marginally more likely to be 6 years or older when compared to their counterparts

Table 3 Business owner characteristics by the extent of informality

Characteristic	Either fiscal or legal	Both fiscal and legal	All
Sex			
Male	42.1	49.4	44.1
Female	57.9	50.6	55.9
Age group, years			
<30	32.7	32.2	32.5
31-54	60.9	64.7	62.0
>=55	6.4	3.2	5.5
Highest Education Level			
At least primary	33.0	36.8	34.0
Secondary	39.1	44.3	40.5
Certificate level	11.2	7.5	10.2
Diploma and above	16.4	10.7	14.9
Not stated	0.3	0.8	0.4
Occupation prior to starting the business			
Employed in the same type of business or activity	11.2	13.8	11.9
Employed in a causal job (e.g. maid etc.)	16.0	19.4	16.9
Employed in a formal job	18.1	17.4	17.9
Self-employed	31.9	31.6	31.8
Unemployed	8.1	7.1	7.8
Others (e.g. housewife, student etc.)	14.8	10.7	13.7
Total	100.0	100.0	100.0

Source: Informal Business Survey 2021.

meant to be *both fiscal and legal* informal. This finding has two implications: the first is that formalisation efforts should target older businesses with *either fiscal or legal* informality. It follows that efforts to improve business productivity should target younger businesses that are *both fiscal and legal* informal. The second is that the degree of informality lowers with an increase in the years of existence of a business. Therefore, interventions to ensure a longer life span of businesses would be a step towards encouraging business formalisation.

Regarding the industry of operation, the majority (57 percent) of the informal businesses are engaged in retail trade (Table 4). Engagement in retail trade suggests four things: First; most informal businesses are not involved in value addition and innovation and are mainly involved in breaking the bulk from other sectors through wholesaling and retailing of goods and services. Second, and as suggested by (Mugoda *et al.,* 2020), is that women dominate the trading sector, which is consistent with assertions mentioned earlier that women own most informal businesses. Third, is the seemingly limited scope for using informal businesses to drive Uganda's industrialisation agenda. Finally, informal businesses are missing out on the benefits derived from formalisation. Benefits realised by formalised businesses may include: higher profits and greater value-added (Medvedev and Oviedo Silva, 2015); financially intangible benefits such as the desire to comply with registration regulations (Gatti *et al.,* 2014); security and protection; building trust with customers; and receiving good publicity (de Mel and Woodruff, 2013).

However, a disaggregation suggests that businesses that have *either fiscal or legal informality* are marginally less likely to participate in the trading sector (45.8 percent) and have a significant representation in the industrial sector (11.5 percent); while businesses that have *both fiscal and legal* informality are more likely to participate in the trading sector (60.9 percent) and have less representation in the industrial sector (6.5 percent). The disaggregation unravels the potential of businesses that have *either fiscal or legal* informality to be used as a vessel of value addition and sectoral value chain linkages to formal businesses. These network effects could help them take the next step toward formalisation.

Regarding the area of operation, informal businesses are mainly located in urban areas (71 percent) as opposed to peri-urban areas (29 percent) (Table 4). The choice of location is informed by the need to be closer to their sources of inputs and their customers who reside in their neighbourhoods. This is relevant in the context of the government's initiative to create more cities. Perhaps, informality is a direct consequence of urbanisation as it creates the need to develop survival strategies (Altrock, 2012).

At least 90 percent of informal businesses are self-founded instead of acquiring an existing business through purchase or inheritance (Table 4). This fact links closely to strands of earlier mentioned evidence, which suggest that the main source of start-up capital for informal businesses is own/personal savings; and that it takes some experience and an extended time, in regard to life-cycle, to accumulate sufficient personal savings for opening up a self –founded business.[12] Conversely, it also points to the earlier mentioned deficit in financial inclusion faced by young and small businesses. Indeed, a majority of informal businesses are less than 6 years old.

In addition, Table 4 suggests that 85 percent of informal businesses were started up using internal financing. The inaccessibility of external finance is primarily due to high interest rates and the lack of documentation (such as business plans, and business records) required (Lakuma *et al.,* 2019). A KII suggest that "*the advantage with registering a company is that you access loans (external finance) easily. Even money leaders prefer to give money to businesses which are registered" (KIIs, Tuesday, October 19th, 2021).* Nevertheless, the disaggregation shows no differences between businesses whose form of informality is *either fiscal or legal*; and those whose form of informality is both *fiscal and legal;* this suggests that reducing the financial costs of informal businesses should be offered

12 The evidence that self-founded businesses are partially as a result of a history of accumulation of resources through own/personal savings reinforces the former argument; While the fact that a majority of informal business owner were previously self-employed, and that informal business are owned by the middle-aged person reinforces the latter argument.

indiscriminately regardless of the extent of informality.

As earlier mentioned, many businesses are founded to help generate survival economic activity at critical times and increasing flexibility for businesses otherwise constrained by regulation (Ulyssea, 2018). It is thus not surprising, from Table 4 that 55 percent of businesses cite the opportunity to start and develop a profitable business as the main reason for creating and joining informal businesses. It is possible that in the search for easy sources of income, urban dwellers leverage the existing demand for daily consumables in the neighbourhood by starting up small retail shops. This idea accompanies the growing recognition and acceptance that some amount of informality will persist regardless of governance and development and that its existence may be a good thing.

3.3 Record keeping, technology use and sources of inputs

Quality record keeping is critical for any kind of enterprise. Records serve as a means of assessing business performance, setting standards, and making corrective measures to make up for past losses. Equally, technology helps businesses improve

Table 4 Business profile, %

	Either fiscal or legal	Both fiscal and legal	All
Years of existence			
<4 years	33.3	49.5	37.9
4-6 years	30.3	16.9	26.5
>6 years	36.4	33.6	35.6
Industry			
Agriculture	2.9	1.6	2.6
Industry	11.5	6.5	7.8
Trade	45.8	60.9	56.9
Hotels, restaurant eating places	7.9	13.0	9.3
Services exc. trade	11.5	11.9	11.6
Other services	10.3	16.2	11.9
Location of business			
Other Urban	31.7	21.3	28.9
Urban	68.3	78.7	71.1
How business was acquired			
Founded	90.6	92.5	91.1
Purchased	3.5	4.3	3.7
Family and others	5.9	3.2	5.1
Main source of funding to set up enterprise			
Own/hh savings	85.0	85.3	85.1
Loan/credit	8.4	7.3	8.1
Others	6.6	7.3	6.8
What was the main reasons for starting or joining this business?			
Convenience of location and/or hours of operation	10.2	14.2	11.3
The opportunity to start and develop a profitable business	57.6	47.4	54.8
To have a secondary source of income	20.2	13.8	18.5
Unable to find another source of income	6.6	18.2	9.8
Others specify	5.4	6.3	5.7
Total	100	100	100

Source: Informal Business Survey 2021.

their processes. For example, information technology enables companies to saturate the economic market with their message. Meanwhile, the source of inputs influences the quality and quantity of production. This section, therefore, discusses these 3 aspects of a business.

3.3.1 Record keeping

Record-keeping is the recording of business financial transactions, including sales, purchases income, receipt, and payment by an individual or organisation. In essence, bookkeeping may be defined as the art of recording business transactions in books regularly and systematically. While it is expected that informal businesses do not keep records (Böröcz, 2000), it is surprising that Table 5 suggests that a majority (64 percent) of such businesses do practice bookkeeping. Similarly, more than one-half of informal businesses indicated that they do keep records on debtors (82 percent), purchases (78 percent), stock (62 percent) and creditors (50 percent). The knowledge and skills could inform this choice in record keeping.

The findings suggest a high incentive amongst informal businesses to keep particular records even though they are not sufficient in estimating profits, which is the variable used to calculate the amount of tax owed. Nonetheless, information on creditors, stock, purchases and debtors are useful in estimating tax deductions. Additionally, the unavailability of records on turnover could explain the earlier alluded low access to external credit by informal businesses. A disaggregation shows no difference between businesses whose informality is *fiscal or legal* and those who are *both fiscal and legal.* Therefore, Business Development Service (BDS) interventions should target both types of businesses indiscriminately.

Table 5 Record keeping, technology use and sources of inputs

	Either fiscal or legal	Both fiscal and legal	All
Do you keep records?			
No	31.5	49.0	36.4
Yes	68.6	51.0	63.6
Type of record kept			
Records of creditors	48.8	55.3	50.2
Stock record	60.6	65.3	61.7
Record of purchase	78.7	73.5	77.5
Records of debtors	80.6	87.0	82.0
Business access to technologies			
Computer (laptop or desktop)	6.1	5.0	5.8
Tablet	3.0	1.5	1.9
Internet connectivity	42.2	28.2	38.2
Smartphone	48.8	35.4	45.0
Technological knowhow			
Computer (laptop or desktop)	14.0	21.9	16.2
Tablet	12.2	19.4	14.2
Internet connectivity	45.7	39.4	43.9
Smartphone	49.9	46.0	48.8
Sources of inputs			
Locally within town	68.7	71.1	69.3
Other districts	25.4	11.7	21.5
Locally from rural areas	5.8	16.5	8.8
Other sources	0.2	0.7	0.3

Source: Informal Business Survey 2021.

3.3.2 Technology use

There is growing consensus that the spread of digital technologies will enable informal businesses to keep records, access wider markets, and allow for innovations that could eventually raise the productivity of low-performing sectors. Table 5 suggests that more than 40 percent of informal businesses have access to a smartphone and 30 percent of the same businesses are likely to access internet connectivity. This significant uptake of technology provides a glimmer of hope. Studies have found that informal businesses with access to technologies such as mobile money are likely to be more productive (Islam, 2016). The uptake of tablets and the internet may reduce informality, for it enables informal businesses to acquire information regarding registration from various government websites.

However, the gains from advances in access to technology may be further away than expected. Many of the innovations in the technology sector require an infrastructure that uses computers and tablets. Table 5 suggests low use of computers (6 percent) and tablets (2 percent). This could be attributed to not only the cost but also technological know-how. Indeed, Table 5 suggests that only 16 and 14 percent of informal businesses have the knowledge and skill to operate a computer or a tablet. The findings are not different from those of Mugoda *et al.,* (2020), who found informality to be more pronounced in economies with low technological know-how.

In this regard, two policy issues emerge from the disaggregation of business access to technology: First; there are no differences between *either fiscal or legal* and *both fiscal and legal* informality in relation to low use of infrastructure (computers and tablets); Second; businesses whose informality is *either fiscal or legal* tend to use more internet connectivity and smartphones than their counterparts whose informality is *both fiscal and legal.* The former calls for BDS interventions to target both types of businesses indiscriminately. While the latter suggests that businesses that are *either fiscal or legal* informal are ripe for formalisation. Meanwhile, a disaggregation of technological know-how indicates no differences between businesses whose informality is *either fiscal or legal* and those whose informality is *both fiscal and legal*. This calls for an indiscriminate approach in providing BDS that targets technological know-how.

3.3.3 Source of inputs

It is worth noting that access to inputs plays a big role in the survival of MSMEs. Table 5 shows that almost 70 percent of informal businesses source their inputs/ supplies within their local towns as opposed to more distant places such as other districts (22 percent) and rural areas (9 percent). This could be due to the need to reduce transport costs incurred by sourcing inputs/ supplies from other districts, rural areas and other countries. This could partly explain the earlier findings that over 70 percent of informal businesses are located in urban areas where they can easily access suppliers. A disaggregation reveals that businesses whose informality is *either fiscal or legal* are marginally less likely (69 percent) to source inputs locally; and more likely (25 percent) to source inputs in other districts when compared to their counterparts whose informality is *both fiscal and legal.* Businesses whose informality is *both fiscal and legal* seek inputs mostly locally (71 percent) compared to other districts (12 percent). This suggests that BDS services geared towards access to inputs should target business whose informality is *both fiscal and legal.*

3.4 Contribution of informal business to the economy

Informal businesses provide income through wages. They also offer linkages for sourcing input and supply of formal firms. Informal businesses are also a source of productivity spillover to formal and vice versa. For instance, informal firms have been found to be efficient users of space and a source of quick decision-making, unlike their formal counterparts (Amonoo, 2020). This section, therefore, discusses the contributions of informal businesses to Uganda's economy. Notably, the section focuses on contribution to overall GDP, linkages, potential tax revenue and employment.

3.4.1 Contribution to GDP by informal businesses

While informality creates legal and fiscal distortions, informal businesses contribute immensely to GDP through sales (World Bank, 2020). Thus, informal businesses are seen to play a complementary role in generating incomes that provide the poor segments of the population with a means of survival and welfare improvement.

In this regard, Table 6 uses the income approach/sales revenue to estimate informal businesses' contribution to GDP as of December 2020.[13] As of December 31, 2020, informal businesses generated income amounting to UGX 41,280 billion shillings, an equivalent of 28.7 percent of the aggregate GDP. Disaggregation by gender suggests that UGX 29,160 billion shillings, which is 70.6 percent of the revenue by informal businesses, is generated by women, which is consistent with the earlier assertion that suggests that women dominate informal businesses.

A disaggregation by industry reveals that the trade sector contributes UGX 27,480 billion, which is the largest amount by any single sector and this is 66.6 percent of the total informal business contribution. Hotels, restaurants and eating places come second with a contribution of UGX 5,376 billion, which is 13 percent of the total informal business GDP. This is unsurprising given the earlier evidence suggesting that most informal businesses are in the trading and the hotel, restaurant eating places industry.

An examination by turnover suggests that large business that falls under the corporate income tax schedule contribute up to UGX 11 trillion, which is 29 percent of informal business GDP and 8 percent of Uganda's GDP. The second-largest turnover is from the business that has a turnover greater than UGX 10 million and not exceeding UGX 30 million.

13 The total monthly sales reported by an informal businesses in a typical month that is neither busiest nor slowest is converted to annual.

Table 6 Contribution to GDP by informal businesses

Sales	Either fiscal or legal informality	Both fiscal and legal informality	All
Total	32,400	8,910	41,280
Sex			
Male	23,500	5,710	12,120
Female	8,940	3,210	29,160
Industry			
Agriculture	1,750	316	2,064
Industry	604	1,840	2,448
Trade	23,000	4,510	27,480
Hotels , restaurant eating places	4,440	929	5,376
Services exc. Trade and Transportation	1,660	491	2,148
Others services	988	823	1,812
Size by turnover			
Not exceeding 10 million	4,080	1,900	5,970
>10 million to 30 million	7,360	1,990	9,350
>30 million to 50 million	5,020	721	5,740
>50 million to 80 million	2,610	1,400	4,010
>80 million to 150 million	3,160	1,330	4,490
Excess of 150 million	10,200	1,580	11,800
Size			
Less than 5 workers	28,900	6,650	35,520
5-49 workers	3,510	2,260	5,772
Informal business GDP (Total sales)	32,400	8,910	41,280
Informal business GDP to Uganda's GDP (%)	22.5	6.2	28.7

Source: Informal Business Survey 2021.

Memorandum item: Uganda's GDP in 2020 is UGX 143,904 billion

In terms of firm size, the micro businesses contributed UGX 35,520 billion, which is 86 percent of the total informal sector to GDP. This is consistent with the earlier evidence that suggests that most informal businesses are micro. A disaggregation by the extent of informality suggests that businesses whose informality is *either fiscal or legal dominate* all aspects of informal businesses' contribution to GDP. This suggests relatively more productivity among businesses whose informality is *either fiscal or legal.* This calls for the formalisation of such business and support to businesses whose informality is *both fiscal and legal*.

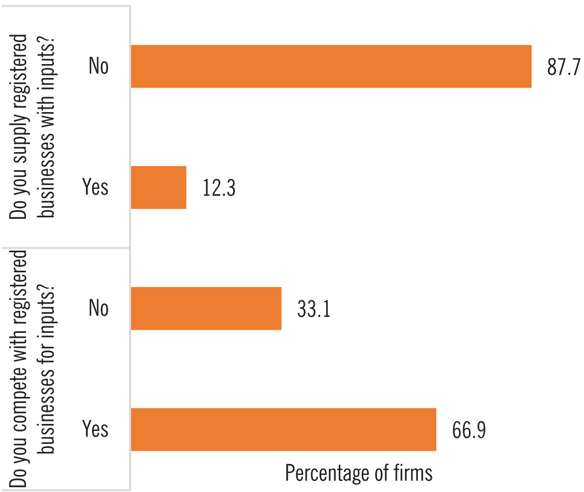
3.4.2 Linkages between informal and formal businesses.

The integration of informal and formal businesses in a location within a cluster benefits informal businesses through participation in supplying as a subcontractor and direct sales linkages that they may not have had access to otherwise (Mukim, 2013). In addition, a strong positive relationship between the productivity of the businesses in a cluster has been found, suggesting significant productivity spillovers for informal businesses (Chhair and Newman, 2014). Informal clusters can also be used for communication with the government regarding proposed policy reforms, air grievances, and take other measures to promote and protect businesses within the cluster (UNIDO, 2004). Informal businesses are also a subordinate complement to formal businesses (Portes and Haller, 2005). By operating without regulation, the informal economy provides the formal economy with low-cost inputs and flexibility.

Clusters have been shown to work in Kenya, Nigeria, Cambodia and India, where buyer linkages within clusters are especially strong between small formal businesses and their informal counterparts (*ibid*). There is a significantly faster growth rate for firms with an interim partnership arrangement with their supply chain members than those without (Wynarczyk and Watson, 2005). Yet, informal and formal business cooperation in Uganda are often limited. Figure 3 suggests that a small percentage (12 percent) of the informal businesses supply formal one with inputs. The missing linkage could result from most informal firms being micro-enterprises dealing in final activities such as wholesale and retail trade, and hotel, restaurant eating places. As earlier mentioned, there is a scope for value addition among informal businesses in Uganda. In this case, businesses in the agriculture and industry sector that have the potential to supply inputs constitute the minority. This missing link in input supplies could also explain informal businesses' slow growth and transition. Earlier evidence suggests that up to 91 percent of informal enterprises remained micro.

However, there is also a risk of negative impact of integrating formal businesses with informal ones, as small informal businesses can become a source of negative competition to formal businesses reducing the net outcomes for the cluster (Chhair and Newman, 2014). Figure 3 suggests that a majority, 66.9 percent, of informal businesses compete for inputs with formal businesses. While competition is necessary for growth and improvement in quality, informal businesses do not incur the regulatory cost, which gives them an unfair advantage over formal firms. This unfair business environment could lead some formal firms to choose to operate informally. This is consistent with the view that businesses will voluntarily choose to be informal after assessing the costs and benefits of formalisation and finding that those costs outweigh the benefits (Maloney, 2004). Equally, some argue that businesses

Figure 3 Linkage with formal businesses.



Source: Informal Business Survey 2021.

often exclude self from the formal economy if the costs (including formalisation costs) outweigh the benefits (De Soto, 1989).

3.4.3 Potential contribution to revenue by informal business

While most informal businesses are small by size and turnover, some large businesses, such as better-off urban professionals (such as doctors, lawyers and architects), often operate informally. For example, less than a third of Uganda's top 60 lawyers paid personal income tax between 2011 and 2014 (ActionAid, 2018). Thus, informal businesses partly consist of thriving enterprises intentionally dodging taxes. This lends credence to the argument that businesses with *either Fiscal or Legal informality* are making a good income and should be taxed by increasing incentives to formalise and charging penalties for failure. This is a matter of ensuring the formalisation of firms that have some form of formality rather than taxing all informal businesses, including those that have some form of *both fiscal and legal informality*.[14]

Table 7 estimates the potential revenue generated by businesses with *either Fiscal or Legal informality.* According to the presumptive and income tax schedule, those businesses are differentiated by turnover. For firms with an income greater than UGX 150 million and fall under the corporate tax schedule, an Effective Marginal Tax Rate (EMTR) of 4 percent was used to calculate the income tax. The EMTR is the impact taxation has on returns on investments. The EMTR value for Uganda is estimated to be at 4 percent (Lakuma, 2019). In addition, businesses were also differentiated by record-keeping to enable the application of the appropriate presumptive tax rates as specified by the 1997 Income Tax Act (amended). Uganda charges a specific tax value for businesses with no records and a tax rate (ad valorem) for businesses with records (Appendix C: Table A2).

Table 7 suggests that 1,088,883 (69 percent) of the informal businesses with *either Fiscal or Legal informality* kept records. It follows that 494,480 (31 percent) of those businesses do not have records. In addition, 928,159 businesses, which have *either Fiscal or Legal informality,* regardless of record-keeping, have their annual turnover not exceeding 10 million shillings and are thus exempted from paying presumptive tax. The high number of businesses not exceeding UGX 10 million turnover annually could be attributed to the micro-size of the business that employ less than five workers. Notably, there is a positive relationship between business size and cash, i.e., larger businesses tend to have more cash flows compared to their smaller counterparts (Rochim and Ghoniyah, 2017).

As at 31st December 2020, businesses with *either Fiscal or Legal informality* and whose turnover was above UGX 10 million but below UGX 30 million had the potential to generate tax revenue worth UGX 18 billion. A more considerable percentage (52 percent) of the potential tax revenue was from firms with records in this category. Similar businesses whose turnover was above UGX 30 million but below UGX 50 million, had the potential to generate tax revenue worth UGX 20 billion. However, for this category, most of the revenue (55.3 percent) emanates from businesses without records. The most interesting is the potential revenue of UGX 407 billion being raised by businesses with turnover above UGX 150 million. This explains up to 86 percent of businesses' total potential tax revenue by *either fiscal or legal informality*. Businesses in this category would ideally qualify for corporate taxation and are ripe for formalisation. Their continued untaxed status lends credence to the perception that "*government is practising discrimination in taxation. There is a need for uniformity in taxation for all people under a similar sector and size*" *(KIIs, Thursday, October 14th, 2021).*

In a nutshell, there is up to UGX 474 billion in potential tax held up by businesses with *either fiscal or legal informality*. This amount could be higher if businesses with *both legal and fiscal informality* are included in Appendix C: Table A3. However, it would not be practical for the revenue authority to chase the whole spectrum of informal firms. This calls for segmentation and concentrating efforts among businesses that have some form of registration and are traceable. These would be businesses, whose informality status is categorized as *either fiscal or legal*.

14 An estimation of tax revenue derived from taxing all businesses is included in Appendix C: Table A3

Table 7 Potential contribution to revenue by partially informal businesses

Threshold (UGX)	Total number of businesses	Businesses with records	Businesses without records	Potential Tax Revenue for those with records (UGX million)	Potential Tax Revenue for those without records (UGX Million)	potential Total Tax revenue (UGX Million)
Not exceeding 10 million	928,159	609,486	318,673	-	-	-
>10 million to 30 million	413,710	307,105	106,606	9,570	8,528	18,098
>30 million to 50 million	130,188	72,257	57,931	9,350	11,586	20,936
>50 million to 80 million	43,280	37,719	5,561	9,000	2,224	11,224
>80 million to 150 million	27,757	27,080	677	16,100	609	16,709
Excess of 150 million	40,268	35,236	5,032	312,000	95,100	407,100
Total	1,583,363	1,088,883	494,480	356,020	118,048	474,068

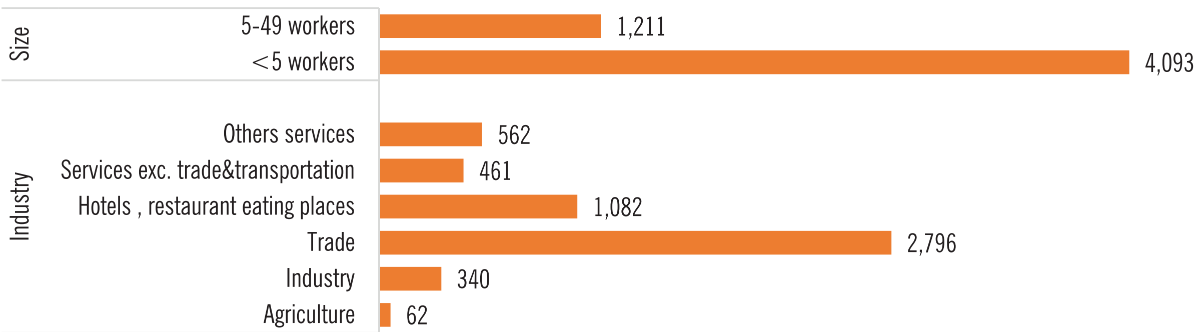
Source: Informal Business Survey, 2021.

3.4.4 Employment by informal businesses

Informal businesses are a source of employment, primarily where the formal businesses cannot provide those jobs at the speed required. Figure 4 suggests that informal businesses employed 5.3 million workers. However, further disaggregation of employment by firm size indicates that over 77 percent of employment is mainly by informal micro-enterprises. Indeed, micro businesses account for 70 percent of the total number of businesses, while small businesses account for 20 percent (UBoS, 2011). This evidence calls for support for micro- businesses before seeking formalisation. Interventions could include reducing business constraints by reducing registration costs and processes, improving credit access and cost, reducing tax rates, and improving the business environment by increasing the quality of services such as electricity and water. Such incentives would hasten business size transition and hence formalisation (Suri, 2019).

Considering the industrial distribution of employment by informal businesses, Figure 4 suggests that more than 2.7 million people (53 percent) are employed in the trade sector, followed by 1 million people (20 percent) in the hotel, restaurant eating places and 562,000 people (10.6 percent) in other services respectively. These findings are similar to those of UBoS (2011). The observed large contribution by the trade sector could be explained by the large entrepreneurial spirit of Ugandans, emanating out of a lack of any other opportunity to generate income (Angus, 2018). Moreover, the extensive employment contribution of the trade sector could be a result of the location of informal businesses in urban areas with high population density requiring retail and wholesale services to provide for their needs for fast-moving consumer goods. The trading sector could also be a relatively

Figure 4 Employment ('000 persons) by size and industry as at December 2020



Source: Informal Business Survey 2021.

more straightforward sector to join for the jobless. The trading sector tends to have low entry costs and the highest concentration of informality. Indeed, sectors with the highest concentration of informality tend to generate the highest number of informal sector jobs. These findings call for policy targeting the trade sector for business development and the social protection of informal workers.

Table 8 suggests that females dominate informal business employment both currently and at the start of business. The disaggregation indicates that businesses with either fiscal or legal formality employ twice more workers than those who are *both fiscally and legally* informal. A comparison of Table 8 row dimensions indicates that own account workers (self-employed workers) explain more than one-half of informal business workers, regardless of gender or informality. This dominance can be attributed to the earlier mentioned low education, significant participation of middle-aged persons and the increased use of internal financing, which are all consistent with own account workers.

3.5 Transition of informal businesses

Transition is a measure of growth by either changing scale/ size or changing sector, from low technology activity such as trading to value addition. This section, therefore, examines these two aspects of business growth.

3.5.1 Transition by scale

Businesses transition by scale also referred to as business growth, refers to the changes in the size of a business, measured by the change in the number of employees and industry. Table 9 follows (Tan and Fock, 2001) and tracks the scale transition of informal businesses using percentage change in the number of employees on the date of the survey from those on the date of establishment. Table 9 shows that over 90 percent of informal businesses have not transitioned and have remained micro (employing less than 4 workers), and only 4 percent have transitioned to small (employing 5 to 49 workers). Worth noting is that transition can be bidirectional. Table 5 suggests that business growth can regress. Indeed, about 2 percent of businesses reduced in size from small to micro.

The low transition and the reduction in business size speak to the earlier identified challenges that informal businesses face, both at start-up and during their operations. These challenges are low access to credit, lack of records, and low technological access and use. In addition, the low scale transition could have been heightened by the impact of COVID-19 and its containment measures on businesses, such as the lockdowns, which resulted in massive layoffs of

Table 8 Employment status ('000 persons) by the extent of business informality

	All			Either fiscal or legal			Both fiscal and legal	
Employment status	**Males**	**Females**		**Males**	**Females**		**Males**	**Females**
Employment at start								
Own account workers	1,150	1,484		808	1,096		342	388
Paid family worker	137	214		89	150		48	64
Paid hired	556	621		416	483		140	138
Unpaid	176	186		120	82		56	104
Total	**2,019**	**2,504**		**1,433**	**1,811**		**586**	**693**
Current employment								
Own account workers	1,132	1,492		839	1,052		294	440
Paid family worker	171	151		129	116		41	34
Paid hired	813	741		531	519		282	221
Unpaid	413	392		274	264		139	128
Total	**2,529**	**2,775**		**1,773**	**1,952**		**756**	**823**

Source: Informal Business Survey 2021.

workers as employers were unable to pay salaries.[15] The reduction in business size and the low transition also explains the increased mortality rate of business. It was earlier noted that most informal businesses do not reach their sixth birthday.

Table 9 Transition by scale

Transition by scale	Percentage of businesses
Remains Micro	91.3
Micro to Small	3.7
Small to Micro	1.6
Remains Small	3.5

Source: Informal Business Survey 2021.

3.5.2 Transition by sector

Table 10 also tracked transition by sector by comparing the sector to which the businesses belonged at the establishment with the current sector of operation. Table 10 reveals a less than 0.5 percentage point change in informal businesses transition from one industry to another. This means that informal businesses tend to remain in their sector of operation at the establishment. As earlier mentioned, most businesses are involved in trading activities. This suggests that there is limited value addition and innovation amongst informal businesses, which is not consistent with Uganda's industrialisation agenda.

Table 10 Industrial transition

	Before	Currently	Percentage point Change
Agriculture	1.1	1.0	-0.1
Industry	4.1	4.1	0.0
Trade	55.3	55.4	0.1
Hotels , restaurant eating places	19.3	18.9	-0.4
Services exc. Trade and Transportation	7.3	7.6	0.3
Others services	13.0	13.0	0.0

Source: Informal Business Survey 2021.

15 This will be discussed later.

4. FACTORS UNDERPINNING INFORMALITY.

This section documents political, economic, socio-cultural, technological, environmental and legal incentives responsible for the persistent informality of Uganda businesses. The section also examines the perceived benefits and costs of remaining informal.

4.1 Political dynamics underpinning informality

In general legal and fiscal informality in Uganda originally emanate out of Uganda's turbulent political history, starting with the collapse of the economy in the 1970s. According to (Muwonge *et al.,* 2007), previous political turmoil contributed to the development of poor business culture and petty business culture, which persists to date. Besides past political instability, the structure of Uganda's economy has remained reliant on subsistence agriculture and correspondingly less on high productivity manufacturing (AfDB, 2010). And while the contribution of the services sector to GDP has overtaken the agriculture and manufacturing sectors in recent years, it has only produced low productive jobs that are informal in nature. Past economic reforms have also fuelled informality over the years. In this regard, the lack of a clear policy to address the cost of the structural adjustment programme in the 1990s, meant that retrenched public servants with insufficient information and limited awareness of alternative business advice and opportunities opted for the informal businesses.

Despite the above, there is a scope for policy emphasis made in Uganda's Vision 2040 on the informal economy. It is not clearly visible in national and local planning processes and there is limited institutional engagement at the national level to understand and later address it. A KII suggests that:

There is a lack of political will from the top to the lowest administrative units to encourage businesses to register with URA since registration implies tax payment, which in turn affects business' (voters') profits. In addition, political leaders shielding some would-be tax payers against tax payment. There is also *lack of accountability on the side of government for tax payers' money. Indeed, the response of tax payers to tax payment was higher in places where government had provided services (KIIs, Monday, February 14th, 2022).*

Furthermore, the differences in the economy (due to diversity in demographic, socio-economic, size and type of activities), reduce cohesion and limit representation in urban politics and planning priorities. More recently, the growth of both legal and fiscal informality is attributed to increased state political interference and competition (Goodfellow and Titeca, 2012). In this respect, continued central government interference has rendered formal institutions of cities' governments increasingly dysfunctional in Uganda. Categorically, the study reveals that as below;

"Increased political competition has created an environment where informal groups seeking to protect their livelihoods can tactically leverage a political intervention in their favour, helping them evade the policies and regulations of the City Council. Meanwhile, politicians have used these interventions to build support in a city—that was largely lost to the opposition. These processes have progressively undermined already weak formal institutions for urban governance".

While this is the case, the study argues that these short term political favours and exemptions to informal businesses facilitate the survival of informal livelihoods in situations where state policies and regulations are threatening them.[16]

In addition, limited representation of the informal sector in Uganda's urban politics has partly contributed to its persistence (Anonymous, 2017). Uganda's political economy is dominated by a small elitist policy-community which dominates policy-making. As such, the resources and skills of the informal economy are rarely valued. Moreover, the political class exploits the informal businesses for political capital. Furthermore, while the informal sector is an important vote bank, the informal business's limited representation in urban politics keeps it nearly voiceless (Tanaka, 2010).

4.2 Social and Cultural dynamics incentivising informality

Socially, many important facets of traditional culture among Uganda's diverse communities have fuelled the persistence of informality. Furthermore, many years of civil war and ethnic tensions have given rise to a culture of conflict and distrust in sections of the society (AfDB, 2010). As a result, business owners resist full entry into the modern monetary economy. In other words, the reliance on informal institutions for business transactions in Uganda remains high.

Moreover, fiscal informality has also been escalated by reduced tax morale and fiscal legitimacy, based on the wide public perception that public services are financed through borrowing from foreign countries and a prevailing sense that due to wide corruption and mismanagement over the years, the government has not been delivering value for money with the resources collected from the public. Similar sentiments were put forward in FGDs as below;

To encourage business formalisation, Government needs to intensify support programmes such as cheap loans, market intelligence and information, put money in our SACCOs and provide business training that facilitates business enterprises (FGD, Monday, October 11th, 2021).

The government needs to scale up service provisions such as garbage collection, power distribution, build roads and hospitals to encourage the informal businesses to register (FGD, Monday, October 11th, 2021).

Provision of social services, e.g. collecting garbage to account for the dues collected by local authorities. This boosts people's willingness to pay. Also, the municipal council offers bursaries to needy students and provides help to the elderly (FGD, Monday, October 11th, 2021).

In addition, the Government's perceived favouritism for foreign business firms is based on the wide belief

16 Extended normally in the run-up to national general elections

that tax exemptions and holidays are only granted to foreign-owned businesses and that there are no tax incentives for domestic business firms, the majority of which operate on a small scale.

Lack of social safety nets, social support and access to contributory social security schemes for workers in the informal sector fuels informality. Uganda's social security coverage remains low; out of the 17.2 million total labour force, 15.6 million (91 percent) are employed in the formal and informal sectors and eligible for pension. However, the pension coverage is about 1.9 million (including public service, national social security fund, and a few occupational schemes); which is about 11.4 percent of the estimated total labour and about 12.6 percent of the estimated active labour force in Uganda (EPRC, 2018). Given this limited coverage, most business firms, especially women, enter at the lower end with small market stalls or operating from home. This is characteristic of women business owners who are already constrained by cultural and labour market discriminations.

Besides lack of safety nets, unemployment and population growth have persistently remained high. Uganda's unemployment rate was 8.8 percent in 2019/20 and was synonymous with women (8.4%) and rural (9.1%) areas (UBoS, 2021). Besides general high unemployment, youth unemployment (13 percent) remains higher than the national average. It is usually some of these youth that moves into the informal sector.

Poverty remains a key driver for informality among Ugandan households. While poverty has declined from 56.4 percent in the pre-PEAP period (1990-1997) to 21.4 percent in 2016/17, the share of households living in transient poverty had risen to 46.3 percent (EPRC, 2020). Spatially, urban poverty is increasing, contributing to 10 percent of the poor population in Uganda. Poor people who migrate to urban areas often fail to secure decent and productive employment – escalating informality in urban areas. Besides poverty, informality has also been catalysed by internal and external risks in the agriculture sector, causing households to move out and into the sector. The reversal in income poverty from 39 percent in 1999/00 to 50 percent in 2002/3; among crop farmers was based on recurrent drought and other vagaries of weather (Appleton and Ssewanyana, 2004). This trend reveals that curtailing informality requires making key investments to build resilience in the agriculture sector. This is because households that move out of the agriculture sector into non-agricultural sectors end up in self-employment in the informal sector on account of the failure of the wage employment sector to absorb excess labour from the agriculture sector (*ibid*).

Besides poverty, the business culture of most business firms in Uganda is instead a survivalist than a long term with business growth and expansion prospects. These business growth prospects could impact the business owner's characteristics to pursue formalisation. As earlier mentioned, 55 percent of non-registered business owners started their businesses out of an opportunity to start a profitable business. These findings are close to a study that suggested that although 66 percent of businesses wanted to expand their businesses, as high as 59 percent of these, planned to expand only within Uganda, only 16 percent planned to expand within the East African region; while only 3 had plans of expanding to the rest of Africa (EPRC, 2017a).

4.3 Business environment incentives underpinning informality

Besides political and social incentives, informality in Uganda is also incentivised by the pre-existing constraints in the business environment. A review of the EPRC quarterly business climate index (BCI) reports undertaken between 2012 to-date, reveals that, over the past 9 years, Uganda's business environment remains constrained by high electricity costs and outages, unfavourable tax policy, high cost of credit, increasing competition from substandard products as well as corruption and bribery.

Relatedly, businesses remain constrained with regard to obtaining land, with as high as 36 percent not possessing any land. Previous efforts to register businesses have also been uncoordinated and required business owners to visit multiple registration centres, resulting in losses of valuable work time and money. Regarding the high cost of credit, evidence suggests that only 14 percent of business firms have ever listed on the stock market to raise working capital (EPRC, 2019). The remaining 86 percent have never used this channel to raise capital, primarily due to a lack of knowledge of how the stock market works.

Moreover, business firms in Uganda have generally not embraced business development services. For instance, up to 36 percent of businesses do not use insurance products due to perceived restrictive costs and lack of awareness about its importance (EPRC, 2015). By size and sector classification, insurance products were a preserve for large firms operating in the services sector. In the same view, most business firms remain informal due to a lack of awareness of the need to have audited books of accounts and or the need to keep financial records. In addition, as high as 72 percent of businesses did not have audited books and or do not keep financial records (EPRC, 2016). Further to the above, while 71.2 percent of businesses had subscribed to business associations, these potential formalisation platforms had not been fully leveraged by Government to boost the formalisation of the informal sector (EPRC, 2016). Yet, 62.2 percent of business firms reported that they joined business associations due to their ability to advocate for a better business environment.

4.4 Legal and regulatory incentives

Uganda currently lacks a clear national policy on the informal sector (Muwonge *et al.,* 2007). Due to a lack of this framework, there exists limited information dissemination on the legal and regulatory practices, including registration procedures for the informal sector businesses. Without a clear regulatory framework, defining the boundaries, constraints, actors, and initiatives to improve the formal-informal relationships has not been possible.

Besides the lack of a regulatory and institutional framework to address informality, an ad hoc business regulatory environment has resulted in informality. Indeed UNCDF (2018) reported that introducing an excise duty on mobile money transactions comprising receipts, payments, and withdrawals at a rate of 1 percent of the transaction value in 2018 reversed gains made in formalising the agriculture, education, and rural finance and energy sectors. The introduction of this tax increased the business operating costs for 71 percent of the businesses (EPRC , 2017). A KII also suggested that the legal provisions such as "*confidentiality of financial details of eligible taxpayers, e.g. bank details", have shielded several potential taxpayers"* (KIIs, Monday, February 14th, 2022).

4.5 Benefits of remaining informal in Uganda

This section discusses both the in-kind and monetary benefits of remaining informal. Flexibility and autonomy, especially for self-employed individuals, may constitute the former. In contrast, higher profits constitute the latter.

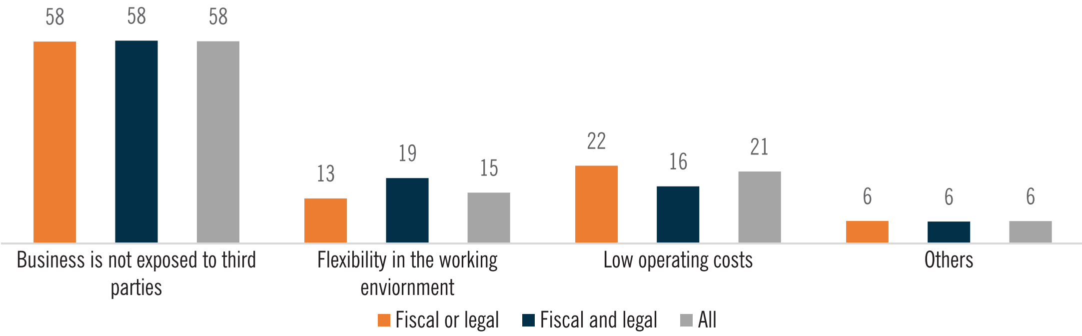
4.5.1 In-kind benefits of business remaining informal in Uganda

According to (OECD, 2007), regulatory, administrative, fees, and financial requirements are the major hindrances to small business formalisation in developing countries. Based on the findings, we expound on each of these to understand what could be the key hindrance in the case of small businesses in Uganda. Figure 5 suggests that more than half of all businesses that remain informal in some way benefit from being outside of the regulatory and administrative reach of local authorities. A KII suggests that "*when you register, you are exposed to high taxes, and in the process, you lose customers to competitors because you have to put your prices higher to meet the tax. When a business has a "small capital", it prefers to stay hiding than being exposed and forced to pay taxes," (KIIs, Tuesday, October 19th, 2021).*

Another KII suggest, *"What is the use of formalising if cannot do business with the government? We are told that the government has many opportunities for emerging businesses" (KIIs, Thursday, October 21st, 2021).*

On the administrative side, the government must be mindful of how regulations are enforced to incentivise the formalisation of businesses. To achieve business formalisation, enforcement procedures should not involve excessive paperwork but should reduce

Figure 5 Main benefits that businesses gain from not being registered, %



Source: Informal Business Survey 2021.

bureaucratic red tape, abuse of authority and corruption. A KII suggests that

"*formalization requirements are very many, including your level of education. Just imagine your level of education to start any business*" (KIIs, Tuesday, October 19th, 2021).

These findings concur with OECD (2007), which demonstrated that on the regulatory side, the government need to be sensitive, particularly to small businesses, with regards to additional reporting, inspection and other compliance procedures before pushing for formalisation agenda.

In this case, the first step in reducing administrative and regulatory barriers to small business formalisation would entail raising awareness of public servants on the needs of the private sector, with a view of creating a more service-oriented model that respects self-employed informal businesses as opposed to the culture that views public servants as an arm of control and enforcement. A KII suggests that too much government breeds corruption:

"corruption is mainly from government officials who doubles as our competitors…For their businesses are not registered" (KIIs, Tuesday, October 19th, 2021).

There are other benefits of remaining informal. Figure 5 suggests that businesses that practice both legal and fiscal informality tend to have a flexible working environment and lower operating costs than those with *legal or fiscal informality*.

This evidence points to the need for regulatory simplification. Business registration alone may not be attractive enough for businesses that practice both *legal and fiscal informality* if the costs of formalisation outweigh the benefits. An intermediate legal status to support formalising businesses that practice both legal and fiscal informality could be a beneficial first step. Larger, more dynamic and growth-oriented informal businesses might be better targeted through strategic public support addressing the specific obstacles limiting their pursuit of formalisation rather than through indirect universal support based on deregulation. This can include targeting businesses that do not benefit from informality, which is businesses that practice *either legal or fiscal informality*.

4.5.2 Monetary benefits for business informality

Besides the benefit of being out of reach of regulatory and administrative reach, as already discussed in the previous section, informal businesses also have

Figure 6 Do informal businesses charge lower prices than formal ones

Source: Informal Business Survey 2021.

economic incentives to remain informal. In this regard, Figure 6 reveals that 35 percent offer lower prices than registered firms. This finding is partly attributed to the earlier mentioned lower operating costs that informal businesses face compared to their registered counterparts. The evidence further reveals that informal firms charge higher prices to a limited extent than their formal counterparts. Despite these benefits, sensitisation is necessary to raise awareness among informal businesses on the lost benefits of being formal.

A KII calls for

"Sensitisation of the business communities about business registration through radio programs, conducting meetings/workshops with tax payers and public speakers on cars should move around communities, announcing the need to register businesses" (KIIs, Tuesday, October 19th, 2021).

4.6 Business perceptions about the formalisation process

To establish which short to medium interventions should be undertaken to encourage formalisation, the study enlisted perceptions from informal businesses. The following indicators were investigated namely; cost of business registration; annual payments by already registered businesses; registration compliance costs for already registered; duration of business registration; and distance to registration points.

4.6.1 Perceptions of business registration fees

A business's decision to formalise depends on the costs and benefits of formality (Suresh, et al., 2011). As such, the formalisation decision is comparable to any other investment decision the firm takes. In this regard, each business compares its perceived costs of being formal, including initial fixed cost registration and recurrent costs (e.g. tax payments), with its perceived benefits of being formal (e.g., access to banks and courts). Against this backdrop, to establish whether costs of business registration, tax amount and compliance fees for registration were prohibitive and prevent businesses from registering, non-registered businesses in Uganda were asked how much they think it would cost them to register businesses, the taxes they would pay and the related compliance registration costs to different government agencies.

The evidence presented in Table 11 reveals that overall (Panel C), non-registered businesses perceive that registration fees are most costly at URA, followed by URSB and least expensive at the local authorities. Specifically, non-registered businesses perceive the registration fees to be an average of UGX 150,000 with a maximum of up to UGX 2.3 Million at URA; UGX 100,000 at URSB; and UGX 35,000 at local authorities, with a maximum of UGX 1 Million for both URSB and local authorities respectively.

However, a disaggregation by the extent of informality suggests that businesses that have *both fiscal and legal informality* (Panel B) perceived a higher cost for registration at URA and URSB than their counterparts with *either fiscal or legal informality* (Panel A). Despite these perceptions, obtaining a tax identification number (TIN) from URA is free. In contrast, the actual registration cost at URBS does not exceed UGX 24,000 for registration of sole proprietorship and UGX 60,000 for registration of limited companies. [17] [18] The findings reveal the two crucial gaps for policy action— limited awareness of registration processes and procedures as well as hidden additional registration costs incurred by informal businesses. Indeed an FGD revealed that ;

Businesses fear URA due to corruption; as such, sensitisation about URA's image needs to be undertaken. For example, when business people were going to obtain TINs, URA used to tell people that the computer network was off. However, the network would work when people paid UGX 30,000 (FGDs, Thursday, October 14th, 2021).

Specifically, the perception of a higher registration cost at URSB among businesses with *both fiscal and legal informality* businesses demonstrates two things: first is that there is a need for intensification of registration awareness campaigns at the local level where most of these businesses are located. Second, the high

17 https://web.ura.go.ug/Pages/Home%20page%20services/How%20to%20get%20aTax%20payer%20Identification%20Number%20(TIN).aspx
18 https://ursb.go.ug/fees

Table 11 Business owners' perceptions of registration and tax/fees to legal authorities (UGX)

	Minimum	Maximum	Mean	Median	#business
Panel A: Either fiscal or legal informality					
Register with local authorities	3,000	1,000,000	51,471	40,000	1,226,416
Register with URSB	10,000	1,000,000	157,524	60,000	72,781
Register with URA	1,000	2,300,000	217,318	150,000	252,513
Tax/fees with local authorities	5,000	1,000,000	90,035	50,000	1,308,116
Tax/fees with URA	3,000	10,000,000	355,524	200,000	250,694
Payment obligations with local authorities	1,000	744,000	52,908	10,000	1,043,324
Payment obligations with URA	2,000	500,000	85,203	50,000	235,889
Panel B: Fiscal and legal informality					
Register with local authorities	1,000	500,000	44,125	35,000	278,027
Register with URSB	3,000	500,000	201,715	250,000	23,292
Register with URA	3,000	1,000,000	251,255	200,000	73,477
Tax/fees with local authorities	3,000	1,500,000	65,021	50,000	301,499
Tax/fees with URA	20,000	6,750,000	361,438	200,000	84,769
Payment obligations with local authorities	1,000	500,000	23,431	10,000	255,595
Payment obligations with URA	3,000	400,000	110,303	100,000	78,217
Panel C: All businesses					
Register with local authorities	1,000	1,000,000	50,113	40,000	1,504,443
Register with URSB	3,000	1,000,000	168,238	100,000	96,073
Register with URA	1,000	2,300,000	224,967	150,000	325,990
Tax/fees with local authorities	3,000	1,500,000	85,350	50,000	1,609,615
Tax/fees with URA	3,000	10,000,000	357,019	200,000	335,463
Payment obligations with local authorities	1,000	744,000	47,108	10,000	1,298,919
Payment obligations with URA	2,000	500,000	91,454	50,000	314,106

Source: Informal Business Survey 2021.

perceived registration cost for both groups at URA and URSB is indicative of the numerous additional hidden costs that informal businesses are likely to incur in the registration process. In this regard, the procedures for obtaining a TIN and business name registration at URA and URSB, respectively, involve filling and submitting online forms, passport photos, valid identification documents, and online payment for name search fees. Most informal business owners have low education, and they likely incur extra fees by hiring agents to overcome the administrative and regulatory bureaucracy. This adds ups to the cost of registration and may also breed corruption.

4.6.2 Annual tax payment by already registered business

The mandatory requirement to pay taxes upon business registration by non-registered businesses has been reported as one of the major barriers to business registration in developing countries (Suresh, et al., 2013). According to the World Bank informal sector enterprise surveys, the main reason why informal businesses do not register with authorities is to avoid tax payments (Farazi, 2014). To establish whether tax rates and dues pose a significant barrier to business registration, perceptions were solicited from non-registered businesses about the annual tax rates incurred by their registered counterparts to the different Government agencies.

The findings presented in Table 12 reveal that overall, non-registered businesses perceive that annual tax payments are highest at URA and lowest at local councils. At the URA, non-registered businesses perceive that their registered counterparts pay an annual average of UGX 200,000 in taxes (Table 12, Panel C). A similar perception is held, regardless of the extent of informality (Table 12, Panels A and B). However, according to Uganda's presumptive tax schedule, presumptive tax rates are based on annual sales turnover and whether a business keeps records or not (See Appendix C: Table A2).

As earlier discussed, an informal business with an average annual sales turnover of UGX 14,112,000, practising *both fiscal and legal informality* with business records, would pay a yearly presumptive income tax of only UGX 16,448. On the other hand, businesses that practice *either fiscal or legal informalityl* with records and an annual turnover of UGX 20,160,000 would pay a yearly presumptive income tax of only UGX 40,640. The observed large perceptional differences between actual tax paid by informal businesses point to a gap in awareness campaigns by URA, especially in targeting tax education for small businesses in Uganda.

4.6.3 Compliance costs for already registered businesses

Compliance costs are associated with larger informal sectors, more corruption, and less investment (World Bank, 2020). Compliance depends on efforts at enforcement and the imposition of penalties for evasion by government authorities. To understand whether compliance costs are a major barrier to business formalisation in Uganda, the study sought perceptions from non-registered businesses on how much their registered counterparts incur to comply with the payment obligations with the different registration agencies. Table 12 reveals that non-registered businesses perceive compliance costs are highest at URA and least at the local council level. The observed large perception could be due to proximity. Unlike local councils, URA registration offices tend to be located in mainly urban centres away from the non-registered business. At URA, non-registered businesses perceive that their registered counterparts pay an average of UGX 50,000 with a maximum of UGX 500,000 in compliance costs. The perceived high compliance costs at URA could emanate out of hidden additional costs that come with fulfilling administrative and regulatory requirements. A KII also suggests that" *there is a multiplicity of taxes and dues in Uganda, we never get any explanation why we have to pay for all these taxes and dues" (KIIs, Tuesday, October 19th, 2021)*. Therefore, it is prudent that compliance costs are minimised by encouraging URA to leverage the Local Government registration structure, especially for small businesses.

4.6.4 Perceptions on duration and distance of business registration

In the past, the government has undertaken initiatives to lessen business registration requirements to encourage non-registered businesses to register. In 2013, the TREP programme was started and aimed at easing the registration of informal businesses. Through this programme, the government aimed to reduce and or consolidate the number of steps required to register—through one-stop shops, simplifying administrative processes for licensing and digitising the process and using online facilities. To establish whether the duration of business registration is a limiting factor to business formalisation in Uganda, perceptions of non-registered business with regard to the duration of business registration for similar registered businesses were assessed.

a) Duration of business registration

Table 12 reveals that non-registered businesses perceive that registration duration is the longest at URA and URSB offices. Overall, informal businesses perceived that it takes an average of 3 days to register at both URA and URSB premises. Despite the above perceptions, the actual registration time at the different agencies is as follows, registration at URA for a TIN, whether for an individual or a company, takes one day, while at URSB, business name registration takes 30 minutes; registration of a company whether local or foreign takes 3 working hours upon submission of all required document (URSB,2021).[19] In the same view, municipalities and local councils take a maximum of

19 https://businesslicences.go.ug/index.php/license/id/1005

one day to issue trading licenses upon submitting all requirements and payment of requisite fees.

The observed deviation in duration for URA and URSB is not surprising. Both offices tend to be centrally located, mainly targeting medium to large scale urban-based businesses in major cities and municipalities; as such, they are not readily available and assessable by informal businesses. Nonetheless, a disaggregation by the extent of informality suggests that businesses that practice *both fiscal and legal informality* perceive that it takes an average of 7 days to register at URSB. This highlights the need for sensitisation of this group on the registration modalities. The discrepancy between the actual and perceived duration of registration could indicate the existing administrative barriers to informal business registration. From the supply side, delays can arise from bureaucratic obstruction, ranging from lack of access to services, corruption, system breakdowns, lack of internet services, and excessive paperwork. On the demand side, delays could emanate from low literacy level, ability to use technology and lack of time to complete the process. Specifically, an FGD stated as below;

The government needs to make online registration simple to encourage registration. While many business people have smartphones, there is a need to have a simple USSD code. The wording in the registration system should be short. Business people donot have time (FGDs, Thursday, October 15th, 2021)

Table 12 Number of days to register a business

	Minimum	Maximum	Mean	Median	#observations
Fiscal or legal					
Days					
Register with local authorities	1	180	2.7	1	1,504,752
Register with URSB	1	99	6.7	2	118,791
Register with URA	1	365	6.4	2	214,787
Register with KCCA	1	30	3.3	1	76,315
Fiscal and legal					
Days					
Register with local authorities	1	365	5	1	369,516
Register with URSB	1	120	11.7	7	96,496
Register with URA	1	356	13.7	3	153,397
Register with KCCA	1	356	7.5	2	203,613
All					
Days					
Register with local authorities	1	365	3.1	1	1,874,268
Register with URSB	1	120	8.9	3	215,287
Register with URA	1	365	9.4	3	368,184
Register with KCCA	1	356	6.4	1	279,928

Source: Informal Business Survey 2021.

b) Distance to registration points

The convenience of business registration can be an incentive for formalisation. Table 13 suggests that URA is located furthest from non-registered businesses, regardless of the extent of informality. This is not surprising; given that URA has most of its business registration processes online, URA's last-mile physical presence is low. Overall, non-registered businesses move an average of 15 kilometres to register at URA offices. This is consistent with a KII that suggests that" *distances to URA offices are long……Just imagine from here (Nanywa) to Luwero" (KIIs, Tuesday, October 19th, 2021).*

However, a disaggregation by the extent of informality suggests that businesses that practice *either fiscal or legal informality* move the longest distance (20Km) to URA registration points. On the contrary, businesses that practice *both fiscal and legal informality* showed the longest registration distance to URSB (15Km). These results suggest that registration with URA is much more of a problem for the former group, while registration with URSB is more of a problem for the latter group. This calls for the extension of URA services to businesses that practice *either fiscal or legal informality;* and the extension of URSB services to businesses that practice *both fiscal and legal informality.* Both URA and URSB should collaborate with local authorities to obtain information on both groups.

A KII suggests that *"there is a need for more sensitisations/outreach programs from URSB, mainly to explain their mandate to the business communities of Kakumiro district. The programs should not be selective but rather engage the entire business community. Additionally, there is a need for at least one URA and URSB office in Kakumiro district to make it easy for the business owners to register their businesses with these two entities (KIIs, Tuesday, October 19th, 2021).*

Table 13 Number of days to register and distance to registration points (km)

	Minimum	Maximum	Mean	Median	#observations
Fiscal or legal					
Distance (KM)					
Register with local authorities	0.1	40	2.5	1	1,474,222
Register with URSB	0.5	99	13.9	3	170,961
Register with URA	0.1	80	17.4	20	466,143
Register with KCCA	0.2	15	4	2	67,970
Fiscal and legal					
Distance (KM)					
Register with local authorities	0	25	3.6	1	412,947
Register with URSB	1	28	14.2	15	65,738
Register with URA	0.5	42	14.8	10	196,797
Register with KCCA	0.2	500	6.4	1.5	185,212
Register with local authorities					
All					
Distance (KM)					
Register with local authorities	0	40	2.7	1	1,887,169
Register with URSB	0.5	99	14	6	236,699
Register with URA	0.1	80	16.6	15	662,940
Register with KCCA	0.2	500	5.8	1.6	253,182

Source: Informal Business Survey 2021.

5. GOVERNMENT INTERVENTIONS TO SUPPORT THE FORMALISATION OF BUSINESS OPERATIONS

This section examines the effectiveness of past government interventions to encourage formalisation. These interventions include but are not limited to infrastructure to improve the business environment and the acquisition of technology.

5.1 Current and previous measures to promote formal business operations– the reasons for their success and/or failure.

Uganda's national policy response to support informal business formalisation has involved tax policy reforms and administration and participatory initiatives. This study takes special interest in tax administration, which comprises digitisation, tax education campaigns and taxpayer register programmes.

With regards to taxpayer registration, in 2013, the Tax payer Registration Expansion Programme (TREP) was launched to encourage small businesses to register as taxpayers and receive a Tax Identification Number (TIN). TREP was organised by URA, Kampala Capital City Authority (KCCA), URSB, and other local governments. Despite being in existence for 8 years, Figure 7 suggests that only 5 percent of non-registered businesses are aware of the programme. Various accounts explain the observed trend. It has been highlighted that TREP was limited in geographical coverage (Jouste, et al., 2021) . Remarkably, while the first phase of TREP (TREP I) covered divisions in Kampala city and TREP II covered municipalities in Wakiso district, TREP III did not lead to the coverage of the whole country (*ibid*).

Besides limited scope in geographical coverage, KIIs reported that the implementation of TREP had a number of challenges that continue to limit its effectiveness. First, the programme suffers from understaffing, resulting from delayed recruitment processes by URA and competing agency priorities and responsibilities. Specifically for URA, KIIs revealed that URA officers have additional duties of enforcing presumptive tax payments, which affects their commitment to the one-stop-shop. Specifically, A KII stated as below;

In this city, there is a URSB and a local government officer at the TREP one-stop-shop; however, the URA officer is not available at the TREP desk, yet it is supposed to be a one-stop-shop. URA is understaffed and takes a long to recruit new staff (KIIs, Monday, October 18th, 2021).

Second, implementation of TREP is constrained by low budgets for trade promotion at the Local Government Level. A KII with a district commercial officer revealed as below;

The budget for trade promotion, laws, and registration remains limited. In a financial year, a total of UGX 12 -15 million is sent to the city to promote trade but also to facilitate other departments (cooperatives, tourism and industry). This low budget limits mass sensitisation, awareness and supervision. Trade is poorly funded, yet the department is expected to grow government revenue (KIIs, Monday, October 18th, 2021).

Another KII stated as below;

Marketing of the TREP is lacking in this city. Due lack of funds, for radio airtime, talk shows about TREP happen only once a year (KIIs, Monday, October 18th, 2021).

However, the use of Radio is not the best approach. There is no feedback collected from the tax payers when you use radio programmes, and this is not productive. So more physical engagements are required because feedback from the community is very key. In addition, one-on-one inspections and sensitisation exercises are required. Also, the sending out telephone SMS messages to the business community as reminders about business registration is necessary (KIIs, Monday, October 18th, 2021).

URA and URSB should work closely with the Kakumiro

District Local government regarding their mandate of registering businesses. URA and URSB officials should avoid spot visits only for a few businesses they are interested in (KIIs, Monday, October 18th, 2021).

Third, there is limited facilitation for registration compliance. According to a KII, the LGs receive UGX 1.5 Million for enforcement for a whole city. This facilitation is disbursed quarterly; however, sometimes, it is not remitted. To increase effectiveness, there is a need to improve facilitation for registration compliance.

Fourth, the TREP database is not interlinked among the three agencies that form the one-stop-shop. Currently, if a business registers with one of these agencies, their business registration details are not interconnected with the other agencies. Most informal businesses stop registration with only one agency.

There was also a lack of coordination and harmonisation of mandates of the various agencies involved in the implementation of TREP. A KII suggests that:

Each of the agencies (Local governments, URSB and URA) focused on implementing its mandate during the implementation of TREP. For instance, institutions like KCCA did not bother about acquiring TINs but only concentrated on issuing out trading licenses. Indeed, TREP failed to achieve the intended objectives of avoiding multiple points of contact. That is partly why legal compliance did not necessarily translate into fiscal compliance. That's how local governments end up with millions of registered businesses not necessarily paying taxes. Also, integration of the information by the different entities was difficult as the LG did not have a system in place, yet URA already had a system in place. As such, the biggest part of the TREP budget was spent on system development by the LG (KIIs, Monday, February 14th, 2022).

Government is not having a uniform way of formalising businesses.......Some agencies are asking for a trading license, while others want taxes......... In addition, more than 50 percent of businesses registered are with the (LC) chairman. The LC chairman(s) have robust business registers at the local council level. These registers must be utilised (KIIs, Thursday, October 14th, 2021).

A multi-stakeholder approach to business formalisation is very key. There is a need for different concerned entities, e.g. URSB, URA and local authorities, to work together to enable more businesses to register (KIIs, Thursday, October 14th, 2021).

Besides inadequate national coverage, Jouste *et al.,* (2021) reported that while both TREP and E-tax system enabled presumptive firms to declare their incomes to URA in the first year of operation of the formalisation programmes, many informal firms were not persistent in filing tax returns in the subsequent years. In this regard, the study alluded this inconsistency on low enforcement capacity of tax officials, encouraged by the increased focus of the tax authority on large firms. Overall, the study revealed that to formalise, small businesses must have easier access to government services such as tax registration, filing and paying, as demonstrated through the implementation of TREP.

Considering tax administrative innovations, since 2009, the government, through the Uganda Revenue Authority (URA) introduced the Electronic-tax system and filing of tax returns (E-tax system). The E-Tax system is complemented by the Electronic Fiscal Receipting and Invoicing solution (EFRIS), Digital Tracking solution, and Voluntary Disclosure. These systems were an improvement over the erstwhile Excel-based form, which aimed at increasing transparency and simplifying the filing of tax of mainly presumptive taxpayers—mainly the informal sector. Besides enabling registered businesses to report and or pay taxes, these online platforms also enable small businesses to register as new taxpayers and assign newly registered businesses, a TIN to be used on the platforms. Despite the benefits, awareness of these administrative tax innovations, by non-registered businesses, remains low. Besides limited awareness of these systems to the business community, Ladu and Nakaweesi (2021) reported that application to these systems was limited by the many technical and administrative requirements; poor internet and power connectivity across the country. Therefore, attracting non-registered businesses to enroll and later use these platforms calls for simplifying the processes and procedures as well as heavily intensifying publicity about their existence. A KII suggest that:

There has been slow uptake of EFRIS. Not every business person who is eligible issues receipts using the EFRIS system. In addition, the business community lacks the required logistics, such as the internet, a computer which are necessary when using the EFRIS system. There is also inadequate capacity/ skills among business owners on how to use the EFRIS system (KIIs, Monday, February 14th, 2022).

Besides formalisation interventions at the central Government level, various initiatives have also been undertaken at the Local Government level. According to KII, formalisation interventions at the district level have taken the route of mass sensitisation through radio talk shows, implementation of local ordinances and community engagement through barazas to deliberate about business formalisation.[20] However, KIIs reveal that inadequate implementation budgets have limited effective implementation.

5.2 Challenges faced by initiatives for addressing informality

Despite the previous formalisation efforts, the informal sector accounts for about 51 percent of the total GDP in Uganda (MoFPED, 2019). Indeed, the evidence presented in Table 14, reveals several barriers that non-registered businesses encounter with registration at different government agencies. Indeed, the evidence presented in Table 13 indicates that lack of awareness about the need to register and the registration processes and procedures remain key in incentivising both legal and fiscal informality. Indeed, an FGD in Masaka city main market stated as below;

We do not know how to benefit, and URSB does not effectively explain the importance of registration. They only distributed a leaflet. Business registration is not important for us unless there is a way we are going to be helped. Our businesses are small and registration has to be paid for. Businesses do not understand the process and benefits of registration (FGDs, Wednesday, October 20th, 2021).

20 For Masaka city, there is a policy which state that local business licenses are only a preserve of business that have registered with URSB and obtained a TIN from URA.

Others stated as below;

We fear that business registration is for Government to get taxes. We fear that government will add other taxes on top of the market dues. We need to see the benefits of registration, such as financial inclusion and insurance (FGDs, Wednesday, October 20th, 2021). And also, harsh tax law enforcers discourage people from formalising businesses …….The assessment is so bad…… people from Kampala do assessment……….yet we have our local leaders here who know everyone, and they could have been used in that exercise (FGDs, Wednesday, October 20th, 2021).
People need to be sensitised on the importance of taxes, why we pay them, and their benefits. In assessment, people donot know how to register and where to go and register (FGDs, Wednesday, October 20th, 2021).

We think that it is only big businesses and companies that should get a TIN; these have big sales and capital (FGDs, Wednesday, October 20th, 2021).

We think registered businesses do not have any advantage over us. They have to pay taxes and are under Government's watch. URA puts a lot of monitoring on taxes. Registration means Government will monitor every business transaction (FGDs, Friday, October 22nd, 2021).

Besides awareness, fiscally informal businesses are deterred by the perceived high registration costs at URA and the perception of anticipated high taxes to be paid to URA once the business is registered. In addition, as already discussed, business owners are discouraged from registering at URA due to weak accountability of taxpayers' money and widespread corruption (Table 14).

Moreover, lack of basic access to government support programmes such as those providing finance, business development services, and capacity building act as a disincentive for business formalisation, most especially for fiscal formalisation. Indeed a KII stated as below,

Table 14 Reasons for not registering business with URA and URSB, %

Reason	URA	URSB
High costs involved in business registration	27.8	15.0
High taxes that need to be paid if registered	17.8	
High tax compliance costs after registration	5.7	
Poor accountability of taxpayers	8.8	4.6
Lack of information about the process	29.1	38.7
Limited access to registration	3.3	3.3
Don't know if need to register	30.1	
Other Reasons*	6.6	2.0
No aware of the importance of registering with URSB		55.9

Source: Informal Business Survey 2021.

Informal businesses are sometimes not trained properly on the registration requirements of a particular business. Sometimes they bring requirements for an individual to register companies. This wastes time (FGDs, Friday, October 22nd, 2021).

As earlier highlighted, some of these informality incentives are as a result of constraints in Uganda's business environment.

Other reasons include: High time that would be spent dealing with govern, Bribes registered businesses are expected to pay, Lack of technology, Limited access to government support programs, and The process if cumbersome.

Besides, Table 14 above also suggests that non-registered businesses at URA and URSB are further hindered by limited access to registration service points. A KII from Masaka city revealed that ;

The one-stop-shop under TREP is only centrally located in the city yet the city is very large. There is a need to have a registration camp in the different divisions of the city so that registration services are brought close to businesses (KIIs, Monday, October 18th, 2021).

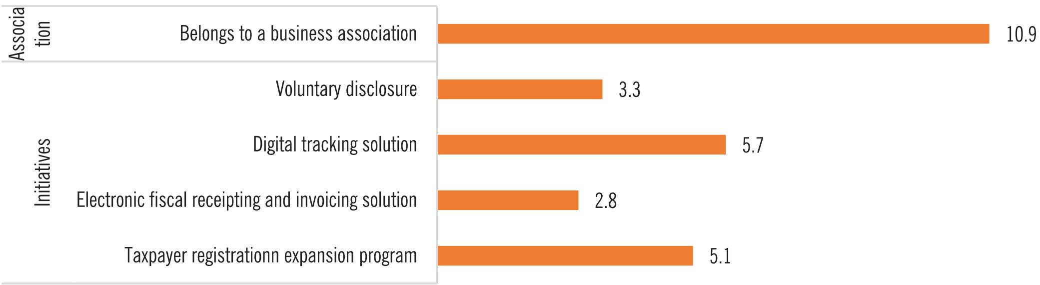
Currently, URSB has a total of 8 branches, 3 of which are located in Kampala, while the rest are regional offices in Masaka, Mbale, Mbarara, Arua and Gulu. Given the limited national geographical coverage of URSB service points, non-registered businesses may find it time-consuming and costly to travel far away from their localities to register. Therefore, instead of being centrally located in a major urban centre, URA and URSB could liaise with lower Local Government business registration centres for businesses. Indeed a key informant interview stated as below;

Past awareness campaigns and business registration training for URA and URSB failed in this area because their mobilisation was poor. These agencies did not target the right participants. To get the right businesses, they could have involved the district commercial officers, heads of local markets, the market committees and the chairman of the business community. The participants gathered came for allowances and lunch (FGDs, Thursday, October 14th, 2021).

5.3 The role of business associations regarding formalising the informal sector

Globally, business associations broadly facilitate capacity building of its members and advocate for an improved business eneivronment. As such, business association such as PSFU, KACITA, and UMA can be a springboard on which government can leverage to formalise the informal sector business in Uganda. There is also another strand of business associations, such as the Federeation of Small, Medium Enterprises (FSME) and Uganda Small Scale Industries Association (USSIA). Informal business associations provide two main functions: first, raise awareness among their members and the authorities concerning the needs and barriers faced by informal businesses (ILO, 2006). They provide policy guidance and influence legislation so that the national environment is more conducive to the development and integration of informal businesses into the formal economy. Second, they provide services that help informal businesses strengthen and enter the formal economy. These services may include

Figure 7 **Awareness of initiatives to encourage business registration and membership to business association, %**



Source: Informal Business Survey 2021.

facilitating the supply of training, access to information, technology and finance, and other business support services.

Despite the above benefits, there is scope for improvement of the role of business associations with regard to increasing awareness about the government's formalisation initiatives in Uganda. Indeed, Figure 7 suggests that of the 11 percent of informal businesses that belong to a business association, only 5 percent are aware of TREP. This Government formalisation initiative has been in existence for the last 8 years. Indeed an FGD suggests that:

Business association leaders have not been informed about encouraging formalisation by any Government agency. Their role stops at fundraising in SACCOs (FGDs, Thursday, October 14th, 2021).
A KII stated;

Business associations are many in this area; however their mandate has been restricted to advocacy on the cost and the provisioning of rent, licenses, competition between traders and hawkers and street vendors, and places of convenience at business premises. In this regard, few associations participate in TREP activities (KIIs, Monday, October 18th, 2021).
Another KII stated;

The business community has not appreciated the value of being a member of a business association. They only join associations/ groups whenever programs such as emyooga come up (KIIs, Monday, October 18th, 2021).

Similarly, we observe low awareness among informal businesses for other fiscal initiatives implemented by URA more recently to reduce tax gaps and leakages (Figure 7). The findings reveal two important policy options; *first,* there is a need for incentivising business associations with basic business development support services such as business training and other administrative support to build awareness about formalisation initiatives among their members. Concerning support to business associations, a key informant from a business association suggest that:

Business associations have inadequate finances for a wide geographical outreach. The government could sponsor radio talk shows and workshops for these associations to promote awareness about registration among the business community (KIIs, Monday, October 18th, 2021).

Another KII stated that the majority of business associations were not registered yet. To encourage members' formalisation, the government could recognise these informal sector associations by facilitating their registration to formal status. In addition, the budget for the Ministry of Trade, Industries and Cooperatives could be increased at Local Government level to increase public and mass sensitisation, especially for the district commercial officers.

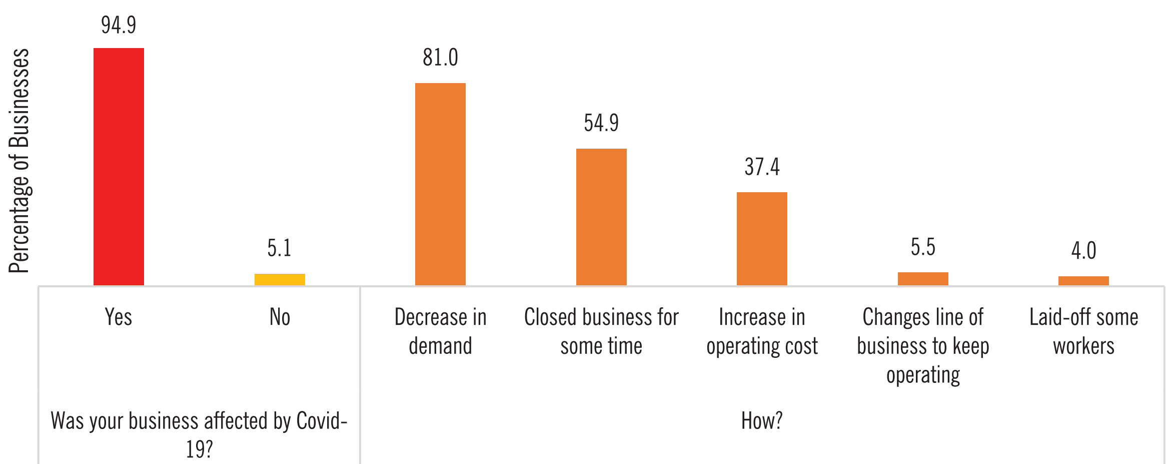
6. EFFECTS OF THE EMERGENCY OF COVID-19 PANDEMIC ON INFORMALITY IN UGANDA

Informal businesses faced high risks during the COVID-19 outbreak. These businesses were the hardest hit by the widespread shutdowns imposed to control the spread of the virus. Indeed, Figure 8 suggests that about 95 percent of the informal businesses were affected by COVID-19 and its lockdown measures. Given their earlier mentioned smaller average size and lower productivity, informal businesses are often less able to weather shocks than formal businesses. As earlier mentioned, informal businesses have less access to finance and are disproportionately owned by women who often find themselves without social protection. In this context, most informal businesses responded to the effect of COVID 19 by reducing aggregate demand for goods and services (81 percent), while 55 percent closed their businesses for some time. In addition, 37.4 per cent of the informal businesses faced increased operating cost, while 5.5 percent changed their line of business to keep operating.

This is consistent with earlier studies that have suggested that preventive measures adopted by the government of Uganda to curb the spread of COVID-19 resulted in an increase in operating expenses for businesses that continued to stay open (Lakuma *et al.,* 2020). Consequently, the majority of informal businesses especially in the service sector were predicted to have closed within one to three months due to the persistence of the pandemic and its related restrictions. The latter businesses halted operations largely due to their inability to implement preventive health measures such as providing on-site lodging for employees and sanitizers and hand-washing equipment for customers hence their closure (*ibid*).

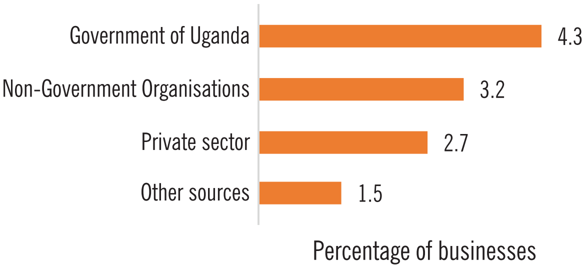
Following the unprecedented consequences of COVID-19 and its containment measures on business operations, several stakeholders such as the government, private sector and some development partners came up with initiatives to support vulnerable groups, including informal businesses. However, less than 5 percent of informal businesses received any form of support from the government of Uganda (Figure 9). This could be attributed to the fact that a large proportion of government support during the crisis has mainly targeted formal business. The inaccessibility of support by informal businesses may partially explain the drivers of Figure 9 where many informal businesses closed their business operations.

Figure 8 Effects of emergency of the COVID-19 pandemic on informal businesses



Source: Informal Business Survey 2021.

Figure 9 Percentage of businesses that received support from sources



Source: Informal Business Survey 2021.

The effects of COVID-19 and the general absence of support for informal businesses could have resulted in the loss of sales and revenue by 65 percent (Figure 10). This finding is consistent with Lakuma *et.al.,* (2020) that revealed that lockdown measures reduced business activity by more than half. As earlier mentioned, the large decline in sales and revenue is partly due to the inability of informal businesses to implement COVID-19 preventative health measures such as the provision of on-site lodging for employees and sanitisers and hand-washing equipment for customers.

7. CONCLUSIONS AND EMERGING ISSUES

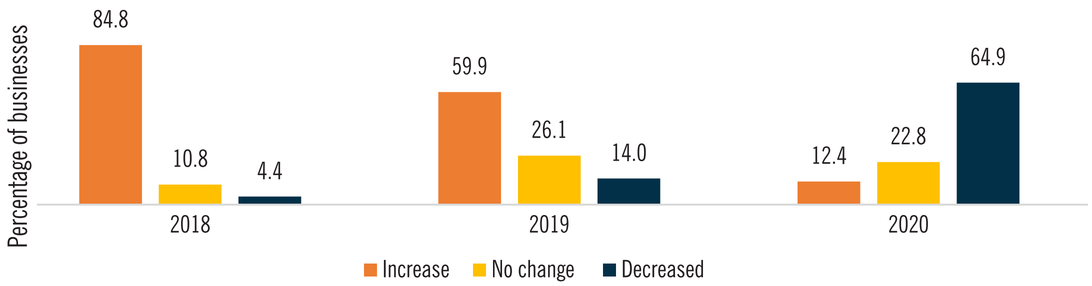
Based on a review of extant literature, a firm-level survey and KII, this study offers a contextual definition of informal business, which focuses primarily on the dimensions of legal and fiscal informality. It follows that the term "legal informality" is used to refer to whether the business is registered or not with the Local Government (LG) and or Uganda Registration Service Bureau (URSB). While "fiscal informality" indicates how informal businesses pay income taxes to Uganda Revenue Authority (URA).

There is, however, a need to manage the variability found in the informal versa formal dichotomy and accommodate businesses operating between fully formal and fully informal; and thus showing some but not all dimensions of informality. For this purpose, the study derives the concept of *either legal or fiscal informality*. The study shows that such businesses are 72 percent of the sample. Conversely, there are those businesses that are fully informal. Those businesses are represented by the category herein referred to as *both legal and fiscal informality,* and such businesses are 28 percent of the sample.

These definitions enable not only research and reform efforts to nudge informal businesses toward adopting formalisation; but also are an appropriate tool for segmentation and targeting of informal businesses. Indeed, more differentiated interventions are vital to catering for the varying need of businesses regarding the extent of informality, the scale of activity, sector of operation, and gender of owner age of business, among other characteristics.

Given that most businesses are registered with local governments, there is need to recognise and digitalise this simplified, intermediate, and temporary legal status for informal businesses to better align with business needs and government goals. Specifically, registration, support to businesses and compliance monitoring should move from central government arena and

Figure 10 Sales and revenue performance (%)



Source: Informal Business Survey 2021.

become more firmly established at local government level. In addition, simplification of administrative procedures and compliance requirements (fiscal and regulatory), especially for businesses that are *both legally and fiscally informal*, would contribute to more streamlined, efficient and effective processes.

It is worth noting that females, the youth and middle-aged, and less educated persons are more likely to participate in an informal activity relative to their male, the old and the more educated counterparts. This questions the effectiveness of programming of government interventions such as the *Uganda Women Entrepreneurship Programme (UWEP)*, and *Presidential Initiative of Skilling the Girl Child*, *Youth Livelihood Programme (YLP);* and calls for integrated approaches in designing livelihood intervention; and creating strong linkages between entrepreneurship with education.

There is a high mortality rate for informal businesses. Specifically, a high mortality rate is prevalent among businesses, which exhibit forms of *both fiscal and legal informality*. This finding has two implications: first; formalisation efforts should target older businesses that have *either fiscal or legal informality*. It follows that efforts to improve business productivity should target younger businesses that are *both fiscally and legally informal*. Second; the degree of informality lowers with an increase in the years of existence of a business. Therefore, interventions to ensure a longer life span of businesses would be a step towards encouraging business formalisation.

Regarding the industry of operation, a majority of the informal businesses are engaged in retail trade. However, a disaggregation suggests that businesses that have *either fiscal or legal informality* are relatively, but marginally, less likely to participate in the trading sector and have a significant representation in the industrial sector. The disaggregation unravels the potential of businesses that have *either fiscal or legal* informality to be used as a vessel of value addition and sectoral value chain linkages to formal businesses. These network effects could help them take the next step toward formalisation.

Informal businesses have a viable yet untapped potential for revenue generation. This potential is mostly by a relatively small group of informal businesses with annual turnover above UGX 150 million and whose extent of informality is *either fiscal or legal*. Businesses in this category would ideally qualify for corporate taxation and are ripe for formalisation. Strong penalties should be put in place for non-compliance by this group. Making tax evasion very costly for this group would be prudent.

While informality creates legal and fiscal distortions, informal businesses contribute immensely to GDP and employment. Therefore, informal businesses should be indirectly impacted through development, improved governance, better regulation and improved public services; rather than a direct target of regulation.

Despite the perceived significant contribution by informal businesses, only a small percentage of informal businesses supply formal ones with inputs. A majority of informal businesses compete for inputs with formal businesses. While competition is necessary for growth and improvement in quality, informal businesses do not incur a regulatory cost, which gives them an unfair advantage over formal firms. This unfair business environment could lead some the formal firms to elect to operate informally.

Inspite of this evidence, informality endures mainly due to Uganda's turbulent political history, the structure of Uganda's economy that yields few jobs, and past economic reforms, which reduced the size of the public sector. There is also a lack of political will and accountability on the government's side. This calls for a national policy and strategy to segment businesses by the extent of informality and characteristics of the owner and business; and define the boundaries, constraints, actors and put in place initiatives to improve the formal-informal relationships.

The persistence of informality is partly a consequence of the lack of information on registration fees paid by non-registered businesses, the recurrent and fixed cost of compliance and the number of days it takes to register. For example, non-registered businesses perceive registration fees which are higher than actual fees. The false perception is prevalent primarily among businesses whose extent of informality is *both fiscal and legal.* The findings reveal the two important gaps for policy action— limited awareness of registration processes and procedures as well as hidden additional registration costs incurred by informal businesses.

Businesses are not willing to formalise partly because they see no value for the taxes they pay. There is no fiscal legitimacy. Therefore a greater focus on quality of service delivery link between revenue collected and services provided is so important. Businesses need to see value for the tax they pay.

Interventions to incentivise business formalisation in Uganda over the past decades have shown mixed results and brought limited knowledge on how to address informality systematically. Past reforms such as TREP were limited in geographical coverage, understaffing and competing agency priorities and responsibilities. Low budgets constrain the implementation of TREP for trade promotion at the LG level. The TREP database is not interlinked among the three agencies that form the one-stop shop. There was also a lack of coordination and harmonisation of mandates of the various agencies involved in the implementation of TREP. This calls for the enhancement of teamwork of the agencies under TREP. There is a need to unify the registration forms for all agencies. Precisely, avoiding multiple registration points. In addition, a creation of a centralised digitilised unique system of identification will enhance both legal and fiscal formalisation efforts.

There is also little awareness of digitisation initiatives such as e-tax, EFRIS, Digital Tracking solution, the Voluntary Disclosure among others, Infrastructural deficits such as poor internet and power connectivity across the country also negative impact on the innovations. Therefore, attracting non-registered businesses to enroll and later use these platforms calls for simplifying the processes and procedures as well as heavily intensifying publicity about their existence. This calls for increased facilitation to tax education.

Business associations such as KACITA, UMA, USSIA, can be a springboard on which government can leverage to formalise the informal sector business in Uganda. However, only 11 percent of informal businesses belong to a business association. This is primarily because business associations are unaware of business formalisation. The mandate of most business associations has been restricted to advocacy on the cost and the provisioning of rent, licenses, competition between traders and hawkers and street vendors, and places of convenience at business premises. The business community has also not appreciated the value of being a member of a business association; business association have inadequate finances for a broad geographical outreach; and a majority of the business association are not registered yet. Additionally, trade associations should be part of the entities involved in business registration.[21] This study also proposes a roadmap in appendix D. This roadmap proposes activities that defines the major steps or milestones needed to address some key findings in this study.

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APPENDIX A: WEIGHTING PROCEDURE

In order for the sample estimates from the survey to be representative of the population, it is necessary to multiply the data by a sampling weight. The basic weight for each sample business is equal to the inverse of its probability of selection, calculated by multiplying the probabilities at each selection stage. A business weight was attached to each sample business record in the data files. Below is the detailed explanation on how the weights were calculated. The weights were calculated based on the probability of selection at each stage. At the sector level, the weights were computed separately for each stratum (size).

Based on the stratified two-stage sample design, the probability of selection for the sample business within a sample region (enumeration area) can be expressed as follows:

$$p_{hi} = \frac{n_h \times M_{hi}}{M_h} \times \frac{m_{hi}}{M'_{hi}},$$

where:

phi = probability of selection for the sample businesses in the ith sample PSU (region) in stratum (sector)

nh = number of sample PSUs selected in stratum h for the survey

Mhi = total number of businesses in the frame for the ith sample PSU in stratum h

Mh = total number of businesses in the sampling frame for stratum h

mhi = number of sample businesses selected in the ith sample PSU in stratum h

M'hi = total number of businesses listed in the ith sample PSU in stratum h

The basic sampling weights, or expansion factors, are calculated as the inverse of these probabilities of selection. Based on the previous expressions for the probabilities, the weights for the sample businesses can be calculated as follows:

$$W_{hi} = \frac{M_h \times M'_{hi}}{n_h \times M_{hi} \times m_{hi}},$$

Where:

Whi = basic weight for the sample business in the ith sample PSU of stratum h

Design weights were adjusted for businesses non-response and for individual non-response to get the sampling weights.

APPENDIX B: LIST OF KII PARTICIPANTS

Table A 1 List of KII participants

No	Name	Designation
1	Simon Ategeka	Licensing Officer, Fort Portal Municipal council
2	George Mutakooha	District Commercial Office of Kakumiro district
3	Tina Kaidu	Assistant Commissioner URA
4	Nicholas Musoke	Research Officer, URA
5	Taban Peter Data	Resident District Commissioner- Adjumani District
6	Mangapi Lawrence	Mayor Adjumani / Head Adjumani SACCO
7	Oyela Concy	VHT/LC1 - KEYI A
8	Geoffrey Mutebi	District Commercial Officer Mbarara District
9	Nahabwe Sharon	Principal Commercial Officer Bushenyi District
10	John Abitekaniza	Deputy Commissioner Business Development and Quality Assurance.
11	Mugerwa Ronald Joseph	Senior Commercial Officer, Masaka City
12	Dorothy Nakachwa	Technical Coordinator,Uganda Small Scale Industries Association (USSIA), Greater Masaka Region
13	Nakayiza Irene	Chairwoman Masaka City Market
14	Nanyinja Irene	Representative of Female Workers/ Deputy Speaker Masaka City Council
15	Mr. Wasswa Sempijja	District Commercial Officer Masaka
16	Kasumba John	Mobiliser, Focus Group Discussion

Source: Informal Business Survey 2021.

APPENDIX C: PRESUMPTIVE SCHEDULE AND POTENTIAL CONTRIBUTION TO REVENUE BY ALL INFORMAL BUSINESSES.

Table A 2 Schedule for the computation of "presumptive" income tax for small businesses

Gross turnover per annum	With records	Without records
Not exceeding UGX 10 million	NIL	NIL
Exceeding UGX 10 million but does not exceed UGX 30 million	0.4% of annual turnover in excess of 10 million	UGX 80,000
Exceeding UGX 30 million but does not exceed UGX 50 million	UGX 80,000 plus 0.5% of annual turnover in excess of UGX 30 million	UGX 200,000
Exceeding UGX 50 million but does not exceed UGX 80 million	UGX 180,000 plus 0.6% of annual turnover in excess of UGX 50 million	UGX 400,000
Exceeding UGX 80 million but does not exceed UGX 150 million	360,000 plus 0.7% of annual turnover in excess of UGX 80 million	UGX 900,000

Source: Income Tax Act.

Table A 3 Potential contribution to revenue by all informal businesses

Threshold (UGX)	Total number of firms	Number records	Numbers without records	Revenue for those with records (UGX million)	Revenue for those without records (UGX Million)	Total potential revenue (UGX Million)
Not exceeding 10 million	1,371,351	806,830	564,521	-	-	-
>10 million to 30 million	538,815	380,608	158,207	11,000	12,657	23,657
>30 million to 50 million	149,250	80,213	69,037	10,300	13,807	24,107
>50 million to 80 million	64,078	58,517	5,561	14,900	2,224	17,124
>80 million to 150 million	38,500	36,972	1,529	22,600	1,376	23,976
Excess of 150 million	43,960	38,928	5,032	376,000	95,100	471,100
Total	2,205,953	1,402,067	803,886	434,800	125,164	559,964

Source: Informal Business Survey 2021.

APPENDIX D: INFORMALITY ROADMAP: THE WAY FORWARD

	Objective	Result	Road map
1	Characterise informality in Uganda	There are 3 Branches of Informality: 1. Business 2. Activity and 3. Workers	The Study focused on one branch of imformality, which is business. There is a need to understand the other segments (actvitity and workers) before embarking on the development of a policy and strategy. Nevertheless, the study on business informality should be disseminated and the policy recomendation implemented.
		Most businesses (70%) are registered with local governments	A policy level conversation on the role of local government as basis for business registration needs to be facilitated.
		Only 1.1 % of businesses are registered with URSB	
		Only 0.8% of businesses are registered with URA	
		Informality is mostly a trading sector phenomena	Current intervention need to be rettolled and repurposed to mainly mainly focus on the trading sector, small businesses, businesses with low turnover and women. This calls for (1) supporting informal clusters; (2) providing support to informal businesses without formalization as a target; and (3) developing simplified, intermediate, and temporary legal statuses for informal businesses to better align with business needs and government goals.
		More than 90 % of busineses are small	
		Most (60 %) businesses have turnover not exceeding 10 million	
		Most (55%) businesses are owned by women	
2	The rethinking of approaches to formalization		

	Objective	Result	Road map
3	Identify the political, economic, socio-cultural, technological, environmental, legal, and regulatory gaps and incentives responsible for the persistent informality in Uganda	Informality persists partly as a consequence of Uganda's turbulent political history	Identify political economy issues that promote informality
		Past economic reforms, which reduced the size of the public sector	
		There is also a lack of political will and accountability on the side of the government	
		The structure of Uganda's economy that yields few jobs	Leverage other sectors other than the service sector to create jobs
4	Assess attempts and their effectiveness of the current and previous interventions aimed at promoting formal business operations, and the reasons for their success and/or failure	Only 11 percent of informal businesses belong to a business association.	Business associations such as KACITA, UMA, USSIA, can be a springboard on which government can leverage to formalise the informal sector business in Uganda.
		The mandate of most business associations has been restricted to advocacy on the cost and the provisioning of rent, licenses, competition between traders and hawkers and street vendors, and places of convenience at business premises.	Enhance the role of business association to incude linkage to policy, business develoment and support to formalisation.

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