



# India's Transition Towards Workforce Formalisation

**For Prelims:** [Formalization](#), [Employee's Provident Fund Organisation](#), [e-Shram Portal](#), [Udyam Portal](#), [Pradhan Mantri Shram Yogi Maan-dhan Yojana](#), [Informal sector](#), [Goods and Services Tax](#)

**For Mains:** Formalization of the Economy in India, Social Security Schemes in India, Social Security and Economic Stability

**Source:** [PIB](#)

## Why in News?

India's economy is undergoing a **transformative shift** toward [formalization](#), redefining job structures, [employment security and social benefits](#) for millions, ensuring a larger segment of the population is covered by **social security systems**, offering greater economic stability and a more secure future.

- This transition, supported by the [Employee's Provident Fund Organisation \(EPFO\)](#), enhances economic stability by integrating more workers into social security systems.

## What is Formalization of the Workforce?

- **Definition:** Workforce formalisation is a **crucial step toward building an equitable and resilient Indian economy**.
  - It not only empowers workers through improved social security and working conditions but also strengthens economic fundamentals such as **productivity, tax compliance, and global competitiveness**.
  - Formalization is when jobs move from the [informal sector](#) (small, unregistered businesses and daily wage workers) into the [formal sector](#) (where employees have contracts, job security, and access to benefits).
- **Features:** Businesses operate under clear legal frameworks, ensuring compliance with laws and regulations.
  - Boosts tax revenues, **expanding the tax base** and ensuring a [fairer distribution of the tax burden](#).
  - Employees **receive social security**, healthcare, and benefits under labour laws, including minimum wage enforcement, retirement benefits, pensions, and insurance.
  - **Formal businesses** have **easier access to financial services** and credit from banks and institutions.
  - Formalization encourages **entrepreneurship**, enhances competitiveness, and promotes overall economic growth.

## What is Significance of Workforce Formalisation for the Indian Economy?

- **Widespread Informal Employment:** Approximately **85% of India's workforce is part of the**

**informal sector**, which is not protected by [formal labour laws](#) or social security systems.

- Formalisation ensures better access to social security, healthcare, and pensions, reducing vulnerability to economic shocks.
- **Accurate Data Collection:** Formalisation allows for better data collection on employment trends, which aids in **effective policy-making and economic planning**.
- **Increased Tax Revenue:** A formal workforce contributes more to the [tax base](#), enabling the government to fund public services and infrastructure projects.
- **Reduce Black Money:** Enhances transparency, making [money laundering and illegal activities harder to conduct](#).
- **Digital Inclusion:** Formalisation encourages the adoption of digital tools and technologies, improving efficiency and transparency in the workforce.
- **Attracts Investment:** A formal workforce offers businesses a better operating environment and encourages investment, both domestic and international.

## What is EPFO and its Role in India's Workforce Formalization?

- **About:** The EPFO is one of the **world's largest social security organizations**, providing a wide range of social security benefits to millions of workers across India.
  - It was established under the **Employees' Provident Funds & Miscellaneous Provisions Act of 1952**.
  - EPFO manages over **29.88 crore accounts (EPFO's Annual Report 2022-23)**, underscoring its extensive reach and the magnitude of financial transactions it handles.
  - The EPFO is under the administrative control of the **Ministry of Labour & Employment, Government of India**.
- **Benefits of EPFO:** Ensures long-term financial security through retirement funds, insurance under [Employees' Deposit Linked Insurance \(EDLI\) Scheme, 1976](#), monthly pensions via [Employees' Pension Scheme \(EPS\), 1995](#), and partial withdrawals under EPF (1952) for emergencies, education, or home purchases.
  - The [Employees' Provident Fund \(EPF\) Scheme, 1952](#) allows partial withdrawals for emergencies, education, or home purchases, making it a versatile financial tool.
- **Role of EPFO in Increased Formalization:** From 2017 to 2024, over **6.91 crore members joined EPFO**, with a record 1.38 crore new members registering in the fiscal year 2022-23.
  - In July 2024 alone, **nearly 20 lakh new members were added**, indicating a steady increase in monthly registrations.
  - Many members chose to transfer their funds when changing jobs, ensuring continued access to social security benefits.
  - A significant portion of **new EPFO members are youth**, many of whom are first-time job seekers. Additionally, **more female workers are registering with EPFO**, reflecting a positive trend toward a more inclusive workforce.
  - The rise in EPFO registrations highlights the **growth of formal jobs in India**, with more employees gaining access to essential benefits such as job security, retirement savings, and insurance.

## What are the Challenges in Workforce Formalisation in India?

- **Cost of Formalisation:** Many [MSMEs \(Micro, Small, and Medium Enterprises\)](#) and small businesses find workforce formalisation costly and cumbersome, as nearly **80-90% of India's workforce operates informally**. Small businesses **prefer informality to avoid compliance burdens**.
  - Simplifying compliance and reducing financial barriers will be crucial in overcoming this challenge.
- **Seasonal Workforce:** Migrant and seasonal workers in agriculture, construction, and low-wage jobs **often lack formal contracts** due to frequent relocations, lack of documentation **hinder their formalisation**.
- **Resistance to Change:** Workers in the informal sector are **reluctant to formalise due to a preference for flexibility** and lack of awareness about the benefits.
- **Digital Divide:** Limited access to digital tools in rural areas hinders formal employment despite [Aadhaar](#) and [Unified Payments Interface \(UPI\)](#) advancements.

- **Skill Gaps:** Informal workers often lack the **necessary skills required** for formal jobs, and there is a **shortage of accessible skill development programs** for these workers.
- **Gender Inequality:** [Women face disproportionate barriers to formal employment](#), including socio-cultural constraints, lack of **childcare services**, and gender bias in the workplace.

## India's Initiatives Related to Formalisation of Workforce

- [e-Shram Portal](#)
- [Udyam Portal](#)
- [Pradhan Mantri Shram Yogi Maan-dhan Yojana](#)
- **Labour Reforms:** The [labour codes](#), such as the [Social Security Code, 2020](#), [Industrial Relations Code, 2020](#), and [Occupational Safety, Health and Working Conditions Code, 2020](#), aim to simplify archaic labour laws, improve working conditions, and make it easier for businesses to hire formally.
- **GST and Digital Payment Systems:** [Goods and Services Tax \(GST, 2017\)](#) and [Digitalisation](#) are helping reduce informality by encouraging businesses to operate **transparently and contribute to the tax system**.
  - Increased financial transparency via digital payment systems and streamlined indirect taxation are formalising businesses.

## Way Forward

- **Incentivise Formalisation:** Policies should focus on reducing the cost of formalisation, providing incentives for businesses to transition to the formal sector.
- **Improve Financial Inclusion:** Expanding access to banking services through the [Pradhan Mantri Jan Dhan Yojana \(PMJDY\)](#) and promoting digital payment systems will help integrate more businesses into the formal economy.
- **Education and Skill Development:** Improving access to quality education and vocational training under the Skill India Mission will equip workers with the skills needed for formal jobs.
- **Promote MSMEs:** Strengthening MSMEs **through funds and functionaries** and making them more competitive on a global scale will boost formalisation and create more jobs.
- **Targeted Schemes:** Implement schemes specifically designed to formalise **tribal workers**. Ensure tribal workers are covered under social security schemes like [Pradhan Mantri Jeevan Jyoti Bima Yojana](#) and [Pradhan Mantri Suraksha Bima Yojana](#).

## Conclusion

The formalization journey strengthens India's workforce by providing job security and a safety net, crucial in uncertain times like the Covid-19 pandemic. This rise in EPFO registrations underscores India's progress toward a more organised economy, ensuring a secure and brighter future for millions.

### **Drishti Mains Question:**

Discuss the importance of formalising the Indian economy. How does this transition benefit workers and the country's economic stability?

## UPSC Civil Services Examination, Previous Year Question (PYQ)

### **Mains**

**Q.** How globalization has led to the reduction of employment in the formal sector of the Indian economy? Is increased informalization detrimental to the development of the country? **(2016)**

