



RSA

Action and Research Centre

**Boosting
the living
standards of the
self-employed**

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The RSA in
partnership with



About the RSA

The RSA (Royal Society for the encouragement of Arts, Manufactures and Commerce) believes that everyone should have the freedom and power to turn their ideas into reality – something we call the Power to Create. Through our research and 27,000-strong Fellowship, we seek to realise a society where creative power is distributed, where concentrations of power are confronted, and where creative values are nurtured. The RSA's Action and Research Centre combines practical experimentation with rigorous research to achieve these goals.

About JRF

JRF works for social change in the UK by researching the root causes of social problems and developing solutions. Together with the Joseph Rowntree Housing Trust, they use their evidence and practical experience to influence policy, practice and public debate.

Executive summary

In search of meaningful self-employment

Self-employment is the economic trend on everyone's mind. Barely a week passes without another news article or opinion piece either lauding or lamenting it – and for good reason. The number of people in self-employment has grown by 39 percent since 2000, with the result that a record one in seven of the labour force now say they work for themselves. Over half of all the jobs created since 2008 are owed to self-employed positions. Moreover, while there is still widespread disagreement about the causes of the boom, most commentators believe that high levels of self-employment are likely to be a permanent feature of our economic landscape. Indeed, self-employment has been increasing nearly every year since the turn of the century – long before the financial crisis of 2008 sent our economy into recession.

Both main political parties have responded positively to this shift and set out a number of proposals to support the small business community. Among the measures introduced by this government are the Start Up Loans scheme, the abolition or amendment of 3,000 regulations, and the introduction of multiple tax breaks. Labour have sought to match these initiatives with several of their own pledges, including a promise to create a network of regional banks to improve lending to small firms. While each of these moves should be welcomed, they are overwhelmingly centred on supporting businesses as entities in themselves, rather than the *individuals* that sit behind these businesses. Put another way, they have sought to help firms become profitable as opposed to making self-employed lives liveable. In a clear sign that the self-employed currently feel overlooked by the state, just 14 percent of those surveyed in our 2014 RSA/Populus poll said that the government adequately supports people like them, and only 11 percent that the welfare system is fair to the self-employed.

Against this backdrop, the RSA and JRF embarked on a project to better understand how the **livelihoods** of the self-employed could be improved. Our previous research had shown that the majority of people who work for themselves enjoy greater satisfaction at work and in their lives overall, albeit with notable exceptions to the rule. According to the Understanding Society Survey, around 84 percent of the self-employed community are satisfied with their job, compared with 76 percent of all employees (a quarter of the self-employed are 'completely' satisfied). Therefore our starting point for this research was not to find ways of 'saving' people from self-employment – although there are a significant minority that would prefer to be in a conventional job – but rather to help more workers take part in *meaningful* self-employment, which at its best enables people to flourish as creative individuals. Indeed, self-employment is in theory one of the best vehicles through which people can become the 'authors of their own lives', if only they are able to manage its perils and pitfalls.

One fundamental issue facing the self-employed is that the burden of dealing with risks largely falls to them alone. For example,

Just 14 percent of those surveyed in our 2014 RSA/Populus poll said that the government adequately supports people like them

a self-employed builder has no recourse to Statutory Sick Pay should they have an injury on site. Likewise, a self-employed cleaner would have no access to Statutory Maternity Pay were they to become pregnant. In general, the income of the self-employed is more likely to be volatile, with highs and lows that mirror the state of the market. This is a starkly different scenario to that facing most people in wage work, who tend to be shielded by their employer from the tremors of unforeseen events.¹ Yet to focus only on income fluctuations would be to ignore the large number of self-employed people who experience persistently low levels of income year-in, year-out. While our research reveals considerable contention regarding the financial health of the self-employed, the Family Resources Survey clearly shows that the median earnings of people who work for themselves full-time are 25 percent lower than their counterparts in wage work.

Any efforts to improve the living standards of the self-employed must therefore make it a priority to address income volatility, as well as to raise people's earnings potential more broadly. In this report, we argue for a three-pronged approach: managing, spreading, and minimising risks. The first two refer to efforts that would help the self-employed deal with the fallout of unexpected events, for example a sudden dip in the market that dries up their customer base. The third relates to efforts that would enable the self-employed to increase their general earnings, for example through up-skilling or expanding their social networks. For each approach, we outline several recommendations to guide the work of policy makers, financial institutions, public sector organisations and others. In doing so we pay particular attention to the needs of self-employed people at the low end of the income spectrum. While self-employment is an inherently precarious form of work regardless of who takes part, it is the poorest that are most vulnerable to its hazards.

It should also be noted that our proposals at this stage are only indicative, having yet to be fully unpacked or costed. We envisage doing this at a later date through more extensive consultation with expert stakeholders, government representatives and the self-employed themselves. A key task will be to prioritise areas that are most in need of resolution, given the limited and shrinking resources of the state. Box 1 suggests areas of priority for supporting the low-income self-employed in particular. A final point to note is that a number of our recommendations will be as relevant and useful to employees as they are to the self-employed, and therefore we should be cautious of creating new policies, processes or initiatives that are only open to people who work for themselves.

Managing risks

By **managing risks** we mean helping the self-employed to deal with the fallout of unexpected events by taking *individual* action. At present, many appear inadequately prepared to personally respond to income shocks, whether it is the result of sickness or late payments. People with savings, for example, are much better placed to weather a crisis

1. The obvious exception are the 622,000 employees that are estimated to be on zero-hour contracts. For more information see www.ons.gov.uk/ons/dcp171766_373757.pdf

We recommend establishing a 'Right to Request' scheme in the housing market, such that every self-employed worker would be eligible to ask for more flexible terms from their provider

than those without, yet at any one time more than a fifth of households with a self-employed worker have zero savings or are in financial debt. Our first proposal therefore is to introduce innovative automated savings schemes for the self-employed on low-incomes, which would allow them (should they wish) to channel a percentage of their earnings into a savings account. One option would be for the Department for Work and Pensions (DWP) to embed this within the new Universal Credit welfare programme. Another idea would be for banks to create a 'Save When Paid' system for their self-employed clients, enabling them to take a stipend off every invoice payment and immediately transfer this into savings.

As well as having a savings cushion, the ability of people to respond to income dips also depends on whether they can reduce outgoings at short notice, in particular their mortgage repayments or rental costs. To facilitate this, we recommend establishing a 'Right to Request' scheme in the housing market, such that every self-employed worker would be eligible to ask for more flexible terms from their provider. In practice, this could mean asking to switch to an interest-only mortgage or to freeze rent payments entirely. Providers would then be obliged to consider every proposal and state in clear terms the reasons behind their decision, thus ensuring that every homeowner and renter benefits from a clear and transparent appraisal of their situation. More broadly, we call for new financial products that would enable the self-employed to improve their income forecasting, so as to encourage them to prepare for the future. The aim would be to help the self-employed understand, for example, how much they would lose were they to fall ill without insurance and have to rely on basic state benefits.

We also consider how the self-employed might prepare for their retirement. Our analysis shows that people who work for themselves are half as likely as employees to contribute to a private pension, and typically have a pension pot that is half the size at the point of retirement. It also appears that many start saving at a relatively late age, with fewer than 15 percent of self-employed 25–34 year-olds currently contributing to a private pension. This begs the question of whether the self-employed should be auto-enrolled on a workplace pension scheme, just as employees are. Putting the administrative challenges to one side, our view is that it would be unwise to do so, mainly because of the aforementioned issue of volatile incomes but also because of the clear preference among some to have more flexible access to their savings. A more appropriate option would instead be to present a 'compulsory question' to the self-employed when they complete their tax return or Universal Credit application. In practice, this would mean them having to declare – yes or no – whether they want to save into a workplace pension scheme like that provided by Nest, and/or a government backed ISA.

Spreading risks

While these measures are designed to help the self-employed manage risks individually, a second approach we explore is how the self-employed might **spread risks** collectively. By this we mean working with others to cope with the after effects of income shocks. Perhaps the best way of pooling risks is through the welfare system, given its comprehensive and progressive approach. At present, however, the self-employed lack access

Our recommendation is to make a clear-cut alteration to the tax system, such that the self-employed community as a whole pay higher NICs, but where the greatest burden is placed on the highest earners

to many benefits such as Statutory Maternity Pay and Statutory Sick Pay (although they have recently secured entitlements to the Maternity Allowance and the new Single-tier State Pension). The optimal scenario would be for the government to provide them with more social security protections. Yet the fundamental stumbling block – both in terms of fairness and finance – is that the self-employed pay lower rates of National Insurance contributions (NICs) than their counterparts in wage work. Indeed, many believe that the self-employed already receive more support than their contributions merit.

The question is how this welfare dilemma can be overcome. One option would be to follow the lead of some European countries and allow the self-employed to ‘top-up’ their protection through extra voluntary payments. However, this has the fundamental drawback of excluding the poorest business owners, to say nothing of the foresight it requires. Our recommendation is therefore to make a clear-cut alteration to the tax system, such that the self-employed community as a whole pay higher NICs, but where the greatest burden is placed on the highest earners. By abolishing Class 2 NICs (as was recently promised by George Osborne), increasing the rate of Class 4 NICs, and raising the threshold at which this tax kicks in, we estimate that the government could raise an extra £280m a year, while making a progressive distributional impact overall. Around 38 percent of self-employed workers (with incomes from self-employment between £5,965 and approximately £20,000 per year) would gain from the reforms, with those earning more than £20,000 (around 34 percent of self-employed people) losing and the remaining 27 percent earning too little to be affected by the reform.

The extra revenue generated through this change would go some way towards financing extra welfare coverage, even if it does prove unpopular with some workers in the short-term. However, as well as establishing a new tax and welfare settlement, we also urge the government to review how the self-employed interact with welfare *as it stands*. It is concerning, for example, that only 61 percent take up their Tax Credit entitlements, compared with 85 percent of employees. Another problematic feature of the Tax Credits system relates to overpayments. The amount of Tax Credits self-employed workers are entitled to is determined at the start of every tax year for the following 12 months, but this is only an estimate based on their current circumstances and how much they earned the year previously. While self-employed workers are encouraged to report any unexpected changes in income or family status to HMRC, in practice very few remember to. The result is that those who earn a few thousand pounds more than anticipated often face a large one-off bill by HMRC, which in turn puts them in financial difficulty.

The government hopes that many of these problems will be resolved with the introduction of Universal Credit (UC), which will roll several means-tested benefits into one. The RSA backs the underlying principles of this new welfare programme, and believes that it is right to encourage people to grow their business in pursuit of profit. However, there are clearly several changes that need to be made before we can be confident that UC will have a positive impact. Our major proposal in this regard is that the Start-Up Period – where people are exempted from the Minimum Income Floor – be extended from 12 to

24 months, given that it often takes longer than a year for fledgling business owners to find their footing. The Minimum Income Floor is an ‘assumed level of earnings’ against which UC payments will be pegged, with anyone earning below this amount not receiving any extra credit to make up the difference. Other recommendations are to establish ‘Grace Vouchers’, which the self-employed could cash-in for a temporary exemption from the Minimum Income Floor, and to turn Post Offices into portals through which the self-employed could seek advice and interact with the online UC system. Over 95 percent of the population live within a mile of a Post Office, and subpostmasters already dispense informal advice about existing benefits.

It is unlikely that the government will heed all our proposals regarding the welfare state. But even if it did there is no guarantee that the self-employed would be fully protected from the risks they face. This is because the welfare state was only designed to be a safety net providing basic support, rather than a system that maintains people’s living standards at the level they have been accustomed to. As such, we need to consider whether the self-employed can pool risks in other ways, for example by forming collective agreements among themselves. In this report, we put forward two indicative proposals. The first is to create a collective income protection (IP) insurance scheme, which could support self-employed people in the event of a long-term illness. By bringing the self-employed together under one umbrella, the effect should be to reduce premiums to a more palatable level. Our second recommendation is for the government to work in partnership with business support organisations and pilot a new social enterprise with a ‘cash-pooling’ service, such that business owners would be able to dip into a collective pot of money as they await payments from clients.

Minimising risks

Finally, we consider how the self-employed might be able to **minimise risks** ex ante. In the short-term, this means preventing mishaps from occurring in the first place, for example through implementing more robust health and safety interventions. However, in the long-term it means improving the general earnings potential of the self-employed by boosting their personal capital (mental and physical health), human capital (skills and knowledge) and social capital (relationships). Looking first at personal capital, the evidence suggests that instances of back problems and fatalities at work are higher among the self-employed, possibly because they operate in poorly equipped work environments with no human resources team to oversee their wellbeing. Given that many lack the financial resources to pay for external guidance, we suggest identifying ‘anchor institutions’ in local areas, for example FE colleges or housing associations, which could freely share their knowledge about occupational health. We also recommend that the self-employed be allowed full access to the new Fit for Work service, which is designed to help people return to work as soon as possible after an illness.

With regard to human capital, we look in particular at the extent to which the self-employed are able to access opportunities for personal development. A concern is that they are just half as likely as employees to have participated in training within the last year. One solution, as

advocated by several other organisations, is to allow the self-employed to claim tax relief on more types of training, and in particular that which is sustained year after year. Looking beyond what the state can do, we also propose that the BBC consider establishing a MyBusiness Portal, which would bring together training information from around the web – both generic and sector-specific. The rationale for nominating the BBC is that it has significant resources at its disposal and appeals to people from across the income spectrum. We also consider how employment services could be enhanced, given their role in helping people transition from unemployment into self-employment. In the short-term this means making adjustments to the New Enterprise Allowance (NEA) and Work Programme schemes, while in the long-term it could involve establishing a single self-employment service to help people start, sustain and – importantly – formalise a business.

While it is relatively easy to comprehend how personal and human capital might be developed, the nature of social capital means it is more difficult to nurture. Unlike employees, the self-employed are not able to tap into the social and commercial networks that are often embedded within a traditional workplace. The challenge is particularly acute for people on low incomes, whose networks tend to be less extensive and rewarding than those from more affluent backgrounds. Although professional groups and online networks offer valuable routes through which to connect with others, our favoured solution is to establish a randomised matchmaking service. Those taking part would be connected with different business owners on a regular basis and encouraged to meet face-to-face to share information and advice. This scheme is currently in operation at the RSA and Nesta. The main advantage is that it addresses the problem of ‘homophily’, whereby people tend to float towards like-minded others, thereby limiting their exposure to novel information.

We finish this report with an injunction for self-employment to be taken more seriously. The risky nature of self-employed work was easier to overlook when few people entered the world of business and when those that did were typically more affluent. Yet the self-employed now make up 15 percent of the workforce (up from 8 percent in 1980), and their numbers have been swelled by different groups that often require more support, such as young people, women and migrants. As such, self-employment should no longer be seen as a fringe activity but instead a mainstream form of work that merits more attention from policymakers. However, it is important to stress that a ‘serious’ approach does not simply constitute providing extra support to the self-employed. Indeed, we should be wary of incentivising self-employment among those who are better suited to working in a typical job. Rather, our approach means achieving the correct balance between **rights and responsibilities**. A right, for example, to greater welfare coverage such as a boost to their maternity and paternity pay. But an equally important responsibility to pay higher National Insurance rates to finance such protection. While not everyone will agree with the proposals we outline – which at this stage are only indicative – the reality is that it is only by having this more substantive conversation that the living standards of the self-employed will ever be enhanced.

Self-employment should no longer be seen as a fringe activity but instead a mainstream form of work that merits more attention from policymakers

Box 1: Three priority areas for supporting self-employed people on low incomes

Many self-employed workers struggle to survive on very low incomes. Our analysis of the Family Resources Survey shows that the poorest 20 percent of self-employed workers earn a quarter less than the poorest 20 percent of employees. The result is that many fall below the poverty line, defined as having a household income below 60 percent of the median. Thirty percent of households with one self-employed worker (and no other earners) are in poverty, compared with 14 percent of households with one employee (and no other earners). While some of these individuals will be 'cash-poor' and 'asset-rich' – that is, they may earn little but can rely on assets such as property for financial security – it appears the majority of low earners are poor in both senses of the word.

The question is what can be done to boost their living standards. In this report, we have set out several ideas to support the self-employed, in particular those on low incomes. However, there is only so much that can be achieved with limited resources at our disposal, and therefore we must prioritise and channel our efforts into a handful of policy areas that will have the greatest impact. In our view, the following three interventions have the clearest potential to assist the poorest self-employed:

- 1. Establish a more progressive National Insurance contributions system** – There is an opportunity to change NIC rates in such a way that would generate extra revenue to pay for greater welfare protections, while simultaneously making the poorest self-employed better off. As well as raising an additional £280m for the exchequer, our proposal would leave more money in the pockets of 38 percent of self-employed workers with earnings between £5,965 and £20,000 per year. A self-employed hairdresser with an annual income of £11,000, for example, would be £359 better off under our reform, while a self-employed builder on £15,000 would take home an extra £199 a year.
- 2. Redesign Universal Credit so that it reflects the reality of self-employed work** – The introduction of Universal Credit will leave many self-employed people on low incomes worse off, mainly because of the introduction of a Minimum Income Floor (MIF). In short, this will mean that anyone earning below a set threshold will not be given any more UC to make up for the difference (as would happen under Working Tax Credits). We estimate that our proposal to extend the 'Start-Up Period' – where people are exempted from the MIF – from one to two years would give 300,000 more self-employed people the time and space to raise their earnings above the floor.
- 3. Establish a universal self-employment service to help people start, sustain and formalise a business** – The New Enterprise Allowance and the Work Programme are the main sources of support for unemployed people who wish to work for themselves. Yet both have significant shortcomings relating to the quality and availability of the assistance they provide. Replacing them with a single comprehensive service that not only helps people to start a business but also to sustain one would be a major step forward. Such a service could also help business owners currently operating in the informal economy to move into legitimate self-employment.

Hundreds of thousands of self-employed workers on low incomes would be affected by these changes, and not in a small way. The first and second interventions would have a large and immediate effect in raising incomes for many workers, while the third intervention would help to raise people's earnings potential over time, primarily by boosting their business acumen.

Recommendations

R1 – Establish automated saving schemes for the self-employed on low incomes

The government should provide an option within the Universal Credit system that allows claimants to automatically channel a percentage of their benefits into a savings account. Banks should consider following suit by creating a 'Save When Paid' initiative for their self-employed clients, which would enable them to take a small amount off the value of every invoice and immediately transfer this into savings.

R2 – Establish a 'Right to Request' for more flexible terms on mortgage repayments and rental costs

The government should establish a statutory right for self-employed workers (and possibly employees) to ask for more flexible terms on their rent and mortgage payments, for example by switching to an interest-only mortgage. Providers would be obliged to clearly state the reasons behind their decisions, thereby bringing a degree of transparency to the process.

R3 – Introduce financial products and services that improve income forecasting

HMRC and the Department for Work and Pensions should work with behavioural economists to devise new ways to help the self-employed understand how their financial situation could change in light of different events, for example were they to fall ill or fail to take out a private pension.

R4 – Present a 'compulsory question' for enrolment onto a pension or ISA scheme

The government should present the self-employed with a compulsory question asking them whether they wish to join a workplace pension scheme and/or a government-backed ISA, for example one provided by the NS&I. To increase the likelihood of take-up, this should be done at a moment of financial reflection, such as when people complete their tax return or UC application.

R5 – Abolish Class 2 NICs and establish a more progressive Class 4 NICs system

The tax system should be overhauled in such a way that the self-employed as a whole pay more in National Insurance contributions, but where the greatest burden is placed on the highest earners. Our proposal is to:

- Increase the rate of Class 4 NICs from 9 percent to 13 percent of earnings above the NICs threshold.
- Raise the Class 4 NICs threshold to £10,600 (the basic rate Income Tax threshold).
- Abolish Class 2 NICs, which are currently levelled at a flat rate of £146 a year.

We estimate these reforms would raise close to £280m per year for the exchequer.

R6 – Consider opening up Statutory Maternity Pay and Statutory Paternity Pay to the self-employed

The government should consider extending Statutory Maternity Pay (SMP) and Statutory Paternity Pay (SPP) to the self-employed, regardless of whether changes to NIC rates are implemented. This would recognise that SMP and SPP are forms of protection not just for workers but also for new-born (or adopted) children, all of whom should benefit from the same level of care irrespective of their parents' occupation.

R7 – Initiate a campaign to inform the self-employed of their welfare entitlements

The government should work with business support organisations, accountants and the Post Office to raise awareness among the self-employed of the various benefits open to them, such as Tax Credits and the Maternity Allowance. The self-employed should also be encouraged to inform HMRC if their income changes, so as to minimise the chance of them being overpaid or underpaid in benefits.

R8 – Redesign Universal Credit so that it reflects the reality of self-employed work

As it stands, Universal Credit could leave the self-employed worse off than they are under the current welfare system, particularly those on the lowest incomes. Several adjustments should be made before the self-employed are transitioned onto this new programme:

- Extend the Start-up Period from 12 to 24 months.
- Establish 'Grace Vouchers' that can be used for a temporary MIF exemption.
- Transfer responsibility for Gateway Interviews from JCP staff to NEA advisers.
- Turn Post Office branches into Universal Credit portals.

R9 – Back the development of a collective income protection (IP) insurance scheme

The government should help to establish a collective income protection insurance scheme that would support the self-employed during periods of long-term sickness. This should be run by private sector organisations experienced in delivering insurance products, and could be partly funded using a portion of the extra revenue generated through the NICs reform.

R10 – Explore the potential for creating a social enterprise with a ‘cash-pooling’ service

Business support organisations such as the Federation of Small Businesses, the Forum for Private Businesses and Enterprise Nation should work together to consider the appetite and potential for establishing a new social enterprise that pools the finances of small business owners. The aim would be for this to limit the detrimental impact of late payments.

R11 – Identify ‘anchor institutions’ that can provide occupational health advice to the surrounding self-employed community

Business in the Community should work with local authorities to identify housing associations, FE colleges and other large organisations that would be willing to share health and safety knowledge with local self-employed people. This could range from conducting workplace visits to disseminating useful materials.

R12 – Fully open up the new Fit for Work service to the self-employed

The government should allow the self-employed to access the face-to-face assessment component of the new Fit for Work service, as well as the advice line. This would reduce the number of self-employed people who are off work with sickness for long periods.

R13 – Review tax-relief to support a wider breadth of sustained training

The government should consider allowing the self-employed to gain tax relief on training that develops a new skill, not just an existing one. It should also look at how the tax relief system could be used to support sustained training that takes place year after year.

R14 – Work with the BBC to establish a MyBusiness portal for training information

The BBC should consider creating a MyBusiness portal that collates and curates information about training – both the general business management kind and that related to specific industries. The BBC is the ideal organisation to run such a portal due to its unparalleled reputation, reach and resources. It also has a clear remit to 'inform and educate'.

R15 – Address the design flaws in the New Enterprise Allowance

The NEA could be improved through relatively simple changes, which would both encourage people to sign up to the scheme and ensure they stay the course:

- Put the value of the NEA payment on a par with Jobseeker's Allowance.
- Reduce the value of the payment gradually, rather than halving it after 13 weeks.
- Ensure every Job Centre Plus (JCP) office has a named Self-employment Adviser (SEA) who can raise awareness of the NEA among other advisers.

R16 – Introduce equal treatment under the Work Programme

The government should consider mandating that every Work Programme provider offer specific support to people who want to move into self-employment, so as to end the current postcode lottery. In the interests of fairness, the government should also look at whether Work Programme participants could be awarded the same allowance that is open to NEA claimants.

R17 – Establish a universal self-employment service to help people start, sustain and formalise a business

A long term objective should be to create a single employment service that is dedicated to helping people move into self-employment. Unlike the NEA, this would enable people not only to start a business but also to sustain their venture. Another feature would be to help informal traders transition into the legitimate world of business.

R18 – Develop a randomised matchmaking service to connect self-employed people in a given area

Local authorities should consider creating a scheme that randomly matches business owners in their locality, such that participants meet with a different person on a regular basis. The aim would be to expand their social network and expose them to new ideas and insights.

Introduction

Since the downturn began in 2008 more than half a million people have struck out on their own

The self-employment puzzle

Of all the economic trends witnessed in recent years, few have done more to capture the public imagination than the rise in self-employment – and for good reason. Since the downturn began in 2008 more than half a million people have struck out on their own, with the result that 4.5 million individuals – or one in seven of the workforce – are now self-employed.² Such is the magnitude of the recent increase that self-employment has been found to account for more than half of all jobs growth during the recessionary years since 2008.³ The same story is mirrored in the business population data, which shows that the number of microbusinesses – defined as firms with 0–9 employees – has swelled by more than half since 2000.⁴ Should these growth rates continue, the RSA predicts that the number of people in self-employment could soon outgrow the size of the public sector workforce.⁵ By most standards, this would be a seminal moment in the UK’s recent economic history.

The fact that the self-employed community is growing is seldom contested. Where there is disagreement, however, is in what lies behind the trend. At one end of the spectrum are commentators who see it as a sign of a resurgent entrepreneurial spirit, enabled by the emergence of new technologies and fuelled in part by shifting mindsets. At the other end are those who view the growth in self-employment through a more sceptical lens, seeing it as an indicator of a fragmented labour market and something that has been brought about by a lack of good quality jobs. Press headlines such as “Young jobless fuel growth in UK start-ups” and “Self-employment hits 20 year-high as people try to avoid unemployment” are testament to how widespread this view is.⁶ In recent months more measured responses have come to the fore that sit between these two opposing camps. This includes the view that the boom owes just as much to fewer people leaving self-employment (lower out-flow rates)

2. RSA analysis of the latest Labour Force Survey results (September to November 2014).

3. The number of people in self-employment grew by 718,000 between 2008 and 2014, compared with a 606,000 increase in employment. Excluding unpaid family workers and those on government training schemes, this means that self-employment accounted for 54 percent of all employment growth since 2008.

4. RSA analysis of the government’s Business Population Estimates (BPE) 2014.

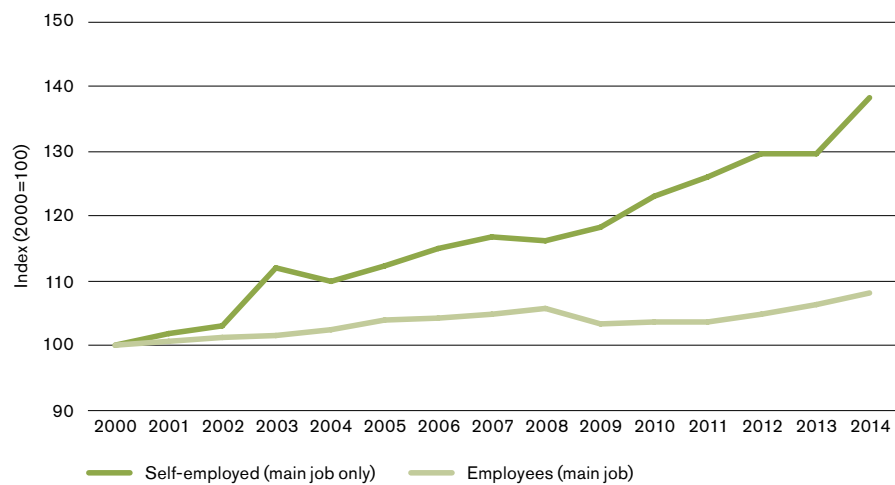
5. Dellot, B. (2014) *Salvation in a Start-up?* London: RSA. Note that the number of people in self-employment has fallen in the last two economic quarters (public sector employment has also fallen).

6. Available: www.ft.com/cms/s/0/f22ef8ec-c473-11e2-9aco-00144feab7de.html#axzz32eGKDrDE and www.telegraph.co.uk/news/uknews/9344366/Self-employment-hits-20-year-high-as-people-try-to-avoid-unemployment-ONS-says.htm

as to large numbers entering it (higher in-flow rates).⁷ The Resolution Foundation estimates that a lower than usual out-flow rate accounts for a quarter of self-employment growth in the post-recession period.⁸

Previous RSA research shows there are no easy answers to the self-employment puzzle. Take, for example, the widespread belief that unemployment has been a major driver. Our 2014 survey with Populus found that 27 percent of the newly self-employed started up to escape unemployment.⁹ Yet this still leaves 73 percent who were drawn into it for other reasons. There is also uncertainty regarding the quality and seriousness of these new jobs. A number of economists have argued that many of the newly self-employed are effectively odd-jobbers scratching around for work, and point to the substantial increase in part-time self-employment as evidence (see Box 2).¹⁰ But again, it is a perspective that only tells part of the story. A closer look at government data reveals that the biggest increases in self-employment between 2008 and 2013 were in professional occupations – one of the highest skilled labour groups.¹¹ In fact, the sectoral and occupational composition of the self-employed population only changed marginally over the course of the economic downturn.¹²

Figure 1: Growth in employment versus self-employment



Source: Labour Force Survey. July–September quarterly data 2000–2014 inclusive

7. D’Arcy, C. and Gardiner, L. (2014) *Just the job – or a working compromise?* London: Resolution Foundation.

8. Ibid.

9. Dellot, B. (2014) Op cit.

10. See, for example, Philpott, J. (2012) *Rise in self-employed ‘odd jobbers’ keeping the lid on unemployment.* London: CIPD.

11. Dellot, B. (2014) Op cit.

12. D’Arcy, C. and Gardiner, L. (2014) Op cit.

Box 2: Key features of the self-employment boom

The recent growth in self-employment throws up a number of questions: what types of businesses are becoming more commonplace, where are they springing up, and who is starting them? Our previous report, *Salvation in a Start-up?*, highlighted several key trends that have occurred since the turn of the century:

- **The rise of the one-person business** – Virtually all the growth (95 percent) in the number of microbusinesses since 2000 is accounted for by non-employing firms. The result is that one-person businesses now make up 75 percent of all businesses.
- **The proliferation of part-time self-employment** – The number of people working for themselves for less than 30 hours a week has grown by 60 percent since 2000, compared with a 20 percent growth in full-time self-employment.¹³
- **The growing importance of self-employment outside of London** – Self-employment accounts for a very large *proportion* of all jobs growth in a number of regions outside of London. For instance, 92 percent of all the jobs added in the North West since 2000 have been in self-employment.
- **The changing demographic of business owners** – The largest proportionate increases in self-employment have been among women, the under 25s and older people. The number of over 65s in self-employment has grown by 140 percent since the turn of the century.
- **The uniqueness of the boom to the UK** – Few other countries have experienced the same rapid increase in self-employment as the UK, and the proportion of the workforce in self-employment has even fallen in Germany, Canada and the US since 2008.

Turning our attention to living standards

Whatever the viewpoint taken, it is clear that the labour market is unlikely to return to business as usual in the foreseeable future. One of the clearest indicators of this is that self-employment has continued to grow despite improvements in the health of the economy (albeit with a dip in the last economic quarter). Last year alone the self-employed population expanded by 123,000.¹⁴ Indeed, many signs indicate that the growth in self-employment lies just as much in deep-rooted structural shifts as it does in a one-off cyclical blip. The number of people who work for themselves has been increasing nearly every year since the turn of the century – long before the economic crash occurred in 2008 (see Figure 1). Long-term drivers include changing values, evolving organisational styles, new technologies and an ageing population.¹⁵ The implication is that the government and others need to begin designing policies and interventions that go with the grain of this potentially enduring trend.

Both main political parties have heeded this call and set out several proposals to support the small business community. David Cameron last year described small businesses as the “lifeblood of our economy”, while Ed Miliband promised to “go into the next election as the party

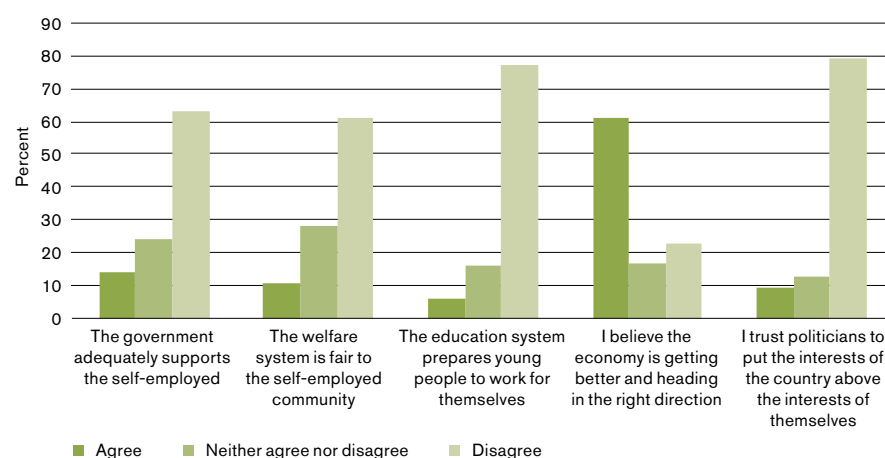
13. According to the Labour Force Survey (Jul–Sep 2014), approximately 29 percent of the self-employed community work part-time, compared with 27 percent of employees.

14. Figures based on the Labour Force Survey, Sep–Nov 2013 to Sep–Nov 2014.

15. Delloit, B. (2014) Op cit.

of small business and enterprise”.¹⁶ Among the measures introduced by this government are the Start Up Loans scheme, which channels low-cost finance to fledging business owners; the abolition or amendment of 3,000 regulations; and the introduction of multiple tax breaks, such as a National Insurance contribution holiday for employers and a cut in Corporation Tax. Labour have sought to match these initiatives with several of their own pledges, including a promise to establish a national Small Business Administration, which would seek to better coordinate business support efforts. It has also played a formative role in setting up the UK’s version of Small Business Saturday, which raises awareness of independent retailers among consumers.

Figure 2: Perceptions of support among the self-employed



Source: RSA/Populus survey of microbusiness owners (26 February–12 March 2014)

While each of these moves should be welcomed, they are overwhelmingly centred on supporting businesses as entities in themselves, rather than the individuals that sit behind these businesses. Put another way, they have sought to help businesses become profitable as opposed to making self-employed lives liveable; two objectives that are closely related but far from identical. There has been a notable absence of policy ideas aimed at improving the living standards of the self-employed – whether that relates to welfare, pensions, insurance or housing. In a clear sign that the self-employed currently feel overlooked by the state, just 14 percent of those surveyed in our RSA/Populus poll said that the government adequately supports people like them, and only 11 percent that the welfare system is fair to people who work for themselves (see Figure 2).¹⁷ Particular concerns have been raised over recent policies such as Universal Credit, which may have a detrimental impact on the low-income self-employed, as well as the Mortgage Market Review, which may make it more difficult for business owners to secure a mortgage.

There has been a notable absence of policy ideas aimed at improving the living standards of the self-employed

16. See Martin, D. (2013) *Labour is the party of small business, says Miliband* [article] BusinessZone: 7th December 2013; and Cameron, D. (2014) *Supporting small businesses* [Speech] Cabinet Office: 27th January 2014.

17. Dellot, B. (2014) Op cit. The RSA commissioned Populus to interview a random sample of 1,006 self-employed people, which took place between 26 February and 12 March 2014.

Box 3: What do we mean by ‘living standards’?

The Oxford English Dictionary defines living standards as ‘the degree of wealth or material comfort available to a person or community’. Similarly, the Resolution Foundation, which undertook a major Commission on Living Standards, understands it in terms of ‘the financial aspects of life, and in particular household earnings and incomes’.¹⁸ While these definitions may be relatively easy to measure, we believe it is preferable to have a more rounded account of living standards, which encompasses the non-material aspects of people’s lives such as their health, happiness and relationships. It is also important to consider not just how people feel at present, but also whether they have the resources to improve their circumstances in future years.

The new precariat?

A lack of consideration for the livelihoods of the self-employed is surprising, not least because they are theoretically one of the most vulnerable groups in the labour market. By their very nature they have no employer to fall back on during times of need or to help them progress within work. Statutory Maternity Pay, Statutory Sick Pay, paid holidays, training support and employer pension contributions are just a few of the occupational benefits that people forgo when they strike out on their own. Moreover, while some see the state as their last resort protector against unexpected shocks, the sizeable cuts being imposed on public spending are likely to erode the already-limited welfare support made available to them. Against this backdrop, it is perhaps understandable that self-employment has been put on a par with zero-hour contract work and viewed as inherently precarious. Indeed, one of the key features of self-employed life is that risk is individualised rather than pooled with others under the umbrella of a single organisation.

The academic Peter Miller goes as far as to say that the spread of self-employment has been championed by a dominant elite keen to “dump” the risks and tensions of capitalism on individual members of society, and away from large businesses and the state.¹⁹ According to this argument, the popular discourse of “personal responsibility” and “self-reliance” has been used to disguise and excuse the lack of protection for those who work for themselves. Similarly, Pascal Gielen, a Dutch sociologist, suggests that the growth in self-employment exemplifies a new world of work characterised by fluidity and “nomadism”, where rootless individuals are left to fend for themselves in the absence of supportive institutions.²⁰ What is more, Gielen argues that many of the self-employed have been persuaded to sacrifice their rights in the futile pursuit of self-realisation – something he describes as ‘self-precarisation’. These arguments portray the self-employed as just another legion within the growing army of precariats who find themselves in ‘in-work poverty’.²¹

18. For more information see www.livingstandards.org

19. Miller, P. and Rose, N. (2008) ‘The death of the social: Re-figuring the territory of government’ in *Governing the Present*. Cambridge: Polity.

20. Gielen, P. (2013) *Creativity and other Fundamentalisms*, Essay 007. Mondriaan Fund.

21. For more information about the extent of in-work poverty, see JRF’s research on monitoring poverty and social inclusion: www.jrf.org.uk/topic/monitoring_poverty

High levels of both job and life satisfaction are visible across broad swathes of the self-employed population – even among those earning below the minimum wage

While there is no doubt some truth in these depictions, they tend to overlook a fact that is borne out time and again within research studies: that the vast majority of the self-employed enjoy working for themselves. According to the Understanding Society Survey, around 84 percent of the self-employed community are satisfied with their job, compared with 76 percent of all employees (a quarter of the self-employed are ‘completely’ satisfied).²² People who work for themselves also outscore employees on life satisfaction, albeit to a much lesser degree. The same survey reveals that 76 percent of self-employed workers are satisfied with their life overall, compared with 75 percent of employees. Of course, not all groups in the self-employed community score so highly; the under 25s, for example, are noticeably less satisfied with their life than those in other age groups.²³ Moreover, life satisfaction among the self-employed (and among employees) has fallen since the economic crash in 2008. Yet, by and large, high levels of both job and life satisfaction are visible across broad swathes of the population – even among those earning below the minimum wage (see Table 1).

Table 1: Satisfaction with job and life overall by working status²⁴

| Satisfaction type | Employees overall | Self-employed overall | Newly self-employed (1 < year) | Long-term self-employed (> 1 year) | Self-employed below the min wage | Self-employed above the min wage |
|--------------------------|-------------------|-----------------------|--------------------------------|------------------------------------|----------------------------------|----------------------------------|
| Job satisfaction | 76.2% | 84.4% | 83.5% | 83.4% | 84% | 85% |
| Life satisfaction | 75.4% | 76% | 77.6% | 76.3% | 74% | 77.8% |

Part of the reason is because of the ‘soft’ benefits that self-employment confers on people, such as the opportunity to do more meaningful work, have greater autonomy and vent their creative talents. There are also several practical benefits to be had from working for yourself, not least being in a better position to work around the needs of family members and care for loved ones. Our RSA/Populus poll found that 37 percent of self-employed people believed that working for themselves was important in enabling them to care for an older relative, while 31 percent said the same of caring for a child.²⁵ What is more, self-employment may also help people to earn a living in a geographic area where few other options for work are available.²⁶ Taken together, this suggests that some people

22. These figures mirror the findings of the RSA/Populus survey conducted in 2014, which revealed that 84 percent of the self-employed feel more satisfied in their working lives than they would have done as an employee.

23. Only 68 percent of 18–25 year olds say they are satisfied with their life overall, according to the 2011/12 Understanding Society Survey (Wave 3).

24. RSA analysis of 2011/12 Understanding Society Survey data (Wave 3). To arrive at this figure, we have totalled the proportions who have said they are ‘somewhat’, ‘mostly’ and ‘completely’ satisfied. Were we to have excluded the ‘somewhat’ answers, the self-employed would still have scored higher than employees.

25. Dellot, B. (2014) Op cit.

26. Ibid.

may have taken a conscious decision to forgo the material advantages of wage work in return for the practical and inherent benefits that are associated with self-employment – something we have previously described as a ‘creative compromise’.²⁷

Learning to live with risk

Our task is therefore not simply to ‘save’ people from self-employment (although there are clearly a significant minority who wish to work in a typical job). Rather, it is to enable more workers to take part in *meaningful* self-employment, which at its best allows people to flourish as creative individuals. Central to this is helping the self-employed to live with the risks that are inherent to their work, as well as enabling them to improve their earnings potential more broadly. Any efforts to support the self-employed should also be mindful that the community is a highly heterogeneous group, with every individual having their own aspirations, business styles and challenges. Our recent segmentation exercise identified six different ‘tribes’ in the self-employed community (see Figure 3). Of greatest relevance to this discussion are the Survivors, who typically struggle on low incomes, are the most vulnerable to unexpected shocks, and are near to closing down their business entirely – even if they wish to continue working for themselves.

Slowly but surely policymakers are recognising these concerns and responding to the needs of the most vulnerable people in self-employment. Ed Miliband, for example, recently promised that a future Labour government would give the self-employed “equal rights” as employees, and there are signs that the Conservatives and Liberal Democrats are thinking along similar lines.²⁸ There is also an international precedent here, with the Canadian government having introduced a Fairness for the Self-Employed Act in 2009, which extended insurance coverage for people who work for themselves.²⁹ However, beyond a handful of disparate research studies and international examples, there is little evidence available in the UK to inform the development of new policies and interventions.

In a bid to plug this gap, the RSA and JRF set out to identify the barriers that prevent the self-employed from achieving a reasonable standard of living, as well as to consider how these challenges might be overcome. In doing so, we paid particular attention to the self-employed on low-incomes, who are naturally the most vulnerable to the perils and pitfalls that are intrinsic to this form of work. Our research highlighted three particular ways in which they could be supported in preparing for risks and boosting their earnings potential:

- **Managing risks through individual action** – This means encouraging self-employed workers to be personally mindful of the risks involved in their work, and enabling them to respond to

27. Ibid.

28. Martin, D. (2014) *Miliband pledges ‘equal rights for the self-employed’* [article] BusinessZone: 23rd September 2014.

29. For more information see Government of Canada (2009) *The Government of Canada delivers Employment Insurance fairness for the self-employed* [news release] Government of Canada: 3rd November 2009.

unexpected income shocks by boosting their savings and changing their spending patterns (eg by taking on flexible mortgages).

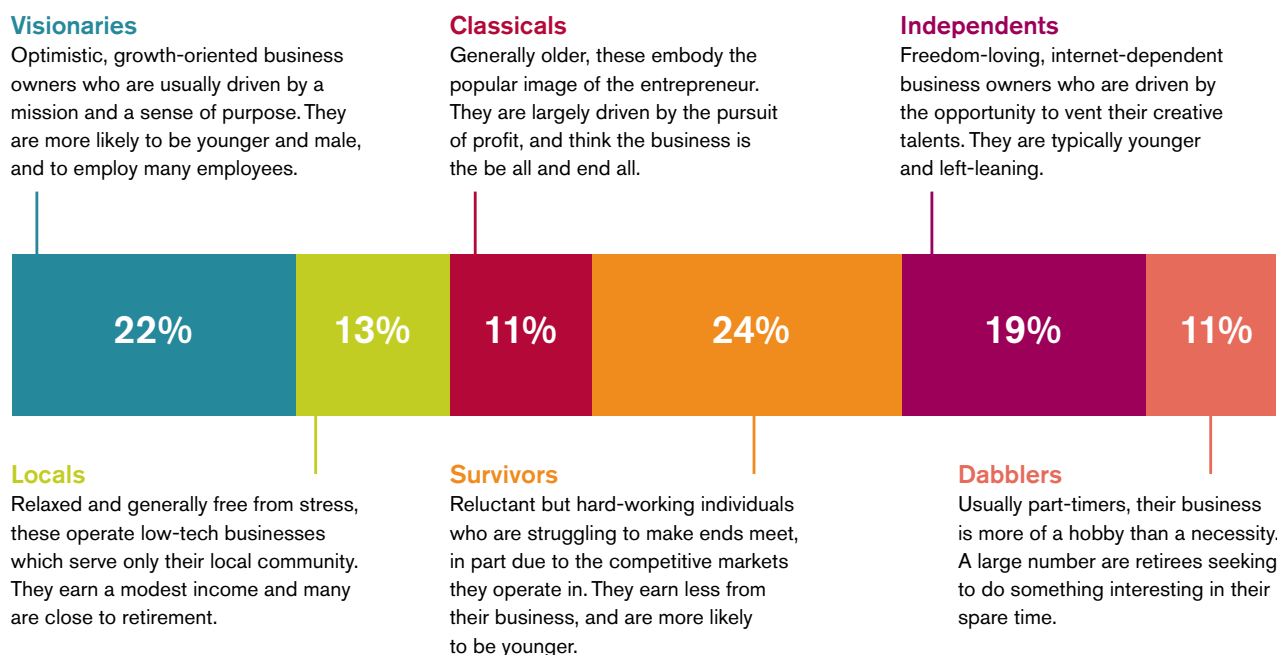
- **Spreading risks through collective action** – This means enhancing the protection people receive from the state through a new tax and welfare settlement, as well as encouraging the self-employed to support one another through new collective movements (eg by pooling their cash flow).
- **Minimising risks through personal development** – This means helping the self-employed to improve their earnings potential by developing their health and wellbeing (personal capital), relationships (social capital) and skills and knowledge (human capital) (eg by extending tax relief on training).

We use this framework to lay out our main findings and recommendations, which are based on the outcomes of desk research, expert interviews, stakeholder roundtables and extensive data mining (see Box 4 for more detail on our methodology). We hope the research detailed here adds another layer to people’s understanding of self-employed workers, and moves the public debate forward from the question of why this community is growing to what can be done to improve their living standards. We begin by examining in more detail the problems of income volatility, and how the self-employed can respond to these fluctuations on their own.

Box 4: Methodology

We used a mixed method approach that combines primary and secondary research. Our first task was to undertake a literature review in order to identify the most pressing issues, such as pensions provision and the introduction of Universal Credit. Where any gaps in knowledge existed, we sought to plug these by analysing the government’s survey data, such as that from the Wealth and Assets Survey, Labour Force Survey, Understanding Society Survey and Living Costs and Food Survey. We also held interviews with expert stakeholders, who were chosen either because of their general knowledge of self-employment or because of their expertise in a particular field (eg welfare, pensions or employment services). Our findings were then brought together and presented at three roundtables, each of which focused on a particular component of the living standards debate. A fourth and final roundtable was reserved for a discussion about the suitability of our policy recommendations. Throughout the research we were mindful of the need to hear about the experiences of individuals from across the spectrum, and therefore took pains to speak with organisations that represent groups that are often marginalised, such as migrants and people with disabilities.

Figure 3: The six tribes of self-employment



**Percentages refer to the proportion of the self-employed community who fall into these tribes*

Managing risks

In this chapter we examine in greater detail the earnings picture of the self-employed, and consider the extent to which fears over their financial health are justified. More importantly, we look at the different reasons why the self-employed experience income shocks, and suggest ways in which they could be helped to live with such volatility. Finally, we discuss whether the self-employed are doing enough to save for their retirement – not an unexpected event as such, but certainly one for which people struggle to prepare.

The earnings slump

The UK's economic recovery from the recent recession has often been described as a wageless one. According to the Resolution Foundation, median hourly wages fell in real terms by around 1.5 percent a year between 2009 and 2013, following on from an already weak period of earnings growth since 2000.³⁰ Yet for certain working groups the drop in wages has been more severe, particularly so for the self-employed. Our analysis of the Family Resources Survey indicates that the real median weekly wages of the full-time self-employed shrank by 12 percent between 2008 and 2012, compared with an 8 percent fall among employees.³¹ The result is that the full-time self-employed now earn close to a quarter less than their counterparts in a typical job, which equates to a weekly earnings shortfall of £167 (see Figure 4). This wage differential is likely to be even greater when looking at what people earn per hour, given that the self-employed typically have longer working weeks than employees.³² A similar wage gap exists between the self-employed and employees in part-time work, albeit to a lesser degree.

To concentrate on the median, however, would be to ignore the large number of self-employed workers sitting at the low income-end of the spectrum. Recent analysis of HMRC data by the Office for Budget Responsibility reveals that the proportion of self-employed workers reporting incomes lower than the tax-free personal allowance rose from 21 percent in 2007–08 to 35 percent in 2011–12.³³ Our own analysis of the Family Resources Survey data shows that 23 percent of self-employed workers are in the bottom 10 percent of all earners, and that 36 percent

Our analysis of the Family Resources Survey indicates that the real median weekly wages of the full-time self-employed shrank by 12 percent between 2008 and 2012

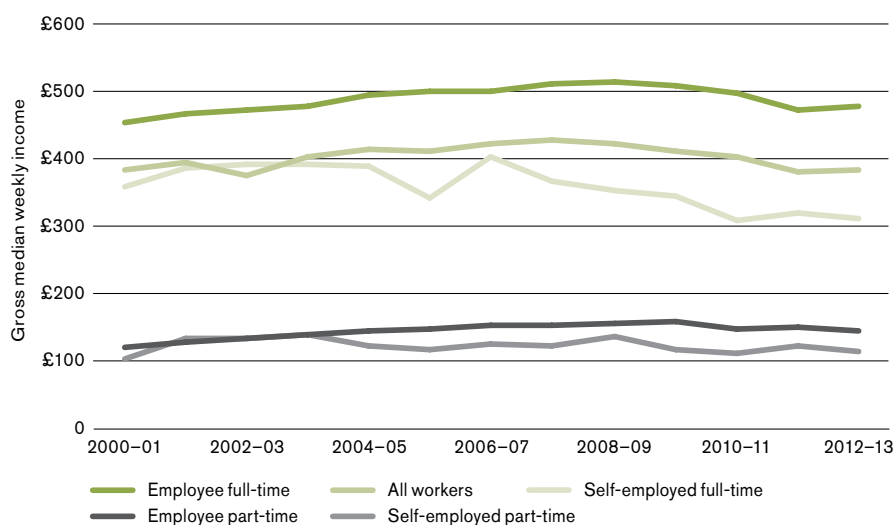
30. Corlett, A. and Whittaker, M. (2014) *Low Pay Britain 2014*. London: Resolution Foundation.

31. RSA analysis of 2012/13 Family Resources Survey. There is a significant time lag between the collection and release of the data under the Family Resources Survey, meaning we are only able to show earnings data up to 2012/13.

32. According to the ONS, 35 percent of self-employed workers usually worked more than 45 hours or more per week in 2014, compared with 23 percent of employees. See Office for National Statistics (2014) *Self-employed workers in the UK*. London: ONS.

33. Office for Budget Responsibility (2014) *Welfare Trends Report*. London: OBR.

Figure 4: Changes in gross median weekly income of the self-employed and the employed (PT/FT)



Source: RSA analysis of Family Resources Survey 2012/13

are in the bottom 20 percent.³⁴ Moreover, the income distribution of the self-employed community is more unequal than among employees, partly because a considerable number are on very low incomes. The poorest 20 percent of self-employed workers earn a quarter of what the poorest 20 percent of employees do (see Figure 11 in the Appendix for a full breakdown of the income distribution among employees and the self-employed).

The result is that many of the self-employed find themselves below the poverty line, according to the most widely used measure (see Box 5). The Family Resources Survey shows that close to a third of households with a single worker who is self-employed are in poverty, compared with 14 percent of households with a single worker who is employed.³⁵ For comparison, the overall household poverty rate is 16 percent (see Table 2).

Table 2: Poverty rates by the employment status of household earners³⁶

| All households | Households with no-one in work | Households with one self-employed worker, no employees | Households with more than one self-employed worker, no employees | Households with one employee, no self-employed | Households with more than one employee, no self-employed | Households with a mix of self-employed and employees |
|----------------|--------------------------------|--|--|--|--|--|
| 15.9% | 44.0% | 30.0% | 19.8% | 13.7% | 2.8% | 9.4% |

34. RSA analysis of 2012/13 Family Resources Survey.

35. Poverty rates are calculated based on disposable incomes after benefits have been factored in.

36. RSA analysis of 2012/13 Family Resources Survey.

While these figures offer a useful snapshot of the overall financial situation of the self-employed, it is also important to try and understand how the earnings of individual workers change over time. The Understanding Society Survey, which tracks the same respondents over several years, shows that the real median earnings of the self-employed appear to increase in line with the amount of years they have spent working for themselves. People who have been self-employed for three years or more earn nearly four times as much as those who have worked for themselves for less than a year (see Table 3). This is partly a result of people becoming more proficient and adept at running their business over time, but it also reflects the fact that large numbers of workers earn very little at the outset of their business and cease trading shortly after starting (with the effect of pushing the median earnings figure up in the long run). The latest results from the government's Small Business Survey show that 20 percent of non-employing business owners anticipate the closure of their venture in the next five years.³⁷

Table 3: Median gross monthly earnings of workers by duration in self-employment³⁸

| < 1 year | 2–3 years | 3+ years |
|----------|-----------|----------|
| £308 | £665 | £1,163 |

Box 5: What do we mean by poverty?

We have chosen to use the most widely understood measure of poverty in the UK, which is deemed as having a household income below 60 percent of the median. Direct taxes are taken into account but not housing costs. However, there are other forms of poverty measures, such as the Minimum Income Standard (MIS). This is not tied to the median average but rather a set amount based on what the public think people need for a minimum acceptable living standard. A recent study commissioned by JRF found that self-employed workers are at a relatively high risk of falling below the MIS, particularly under 35s and lone parents.³⁹

Self-employed workers are only marginally more likely to be dissatisfied with their income than employees

Muddying the waters

Taken together, these findings suggest that many of the self-employed are in a financially perilous state, particularly new starters whose businesses have yet to take root and who may be struggling to turn a profit. Yet while most economic commentators would agree that the self-employed are indeed worse-off than employees, there are concerns that the official data may exaggerate the difficulties they face. One indicator of this is that, according to the Understanding Society Survey, self-employed workers are only marginally more likely to be dissatisfied with their income

37. BIS (2013) *Small Business Survey 2012: Businesses with no employees*. London: BIS.

38. RSA analysis of 2011/12 Understanding Society Survey data (Wave 3).

39. Padley, M., Valadez, L. and Hirsch, D. (2015) *Households below a minimum income standards*. London: JRF.

than employees, with 38 percent and 35 percent saying so respectively.⁴⁰ This is difficult to square with the aforementioned finding that the self-employed earn considerably less than wage workers.

One reason to be wary of the topline earnings data is that business owners do not always declare their full income to HMRC or within government surveys. HMRC estimates that it is owed an extra £34 bn in tax revenues from across the UK economy – the so-called ‘tax gap’ – and that as much as 15 percent of this relates to business owners completing inaccurate self-assessments.⁴¹ A number of studies echo these concerns, with estimates that the underreporting of self-employed earnings amounts to between 28 to 40 percent of the total value of income actually declared.⁴² Further evidence of underreporting can be found in people’s consumption patterns, which are often a better proxy for financial health than earnings information. A study by Mike Brewer at the University of Essex found that the self-employed are more likely than employees to engage in high levels of consumption at lower levels of reported income, suggesting they are materially better off than their self-assessment returns imply.⁴³

A second caveat to bear in mind is that the official earnings data will often only reveal the circumstances of individuals, rather than the broader household. Yet understanding the latter is critical to appreciating the full set of resources that people can draw upon, not least because earners within households often pool their budgets. In many cases, people will only take the decision to work for themselves when they know there is another earner in the household – often a typical employee – who can supplement their income. It is noteworthy that households with a mix of self-employed and employee earners are the group that is least at risk of poverty (see Table 2). It is also important to note that the decision to become self-employed may have been a strategic one aimed at reducing major household expenses, in particular childcare, which today costs a third more than it did in 2009.⁴⁴ A survey undertaken by NatCen in partnership with JRF in 2003 found that 47 percent of self-employed mothers said that the cost of childcare was one of the main reasons for deciding to work for themselves.⁴⁵

A third reason why the earnings data may overstate the difficulties facing the self-employed is that it does not convey the assets that people have access to, whether that be savings, shares or housing. The Wealth and Assets Survey shows that households with self-employed workers are more likely to own their house outright and less likely to be renters of property (see Figure 5). The same survey also reveals that the

40. RSA analysis of 2011/12 Understanding Society Survey data (Wave 3). To arrive at these figures, we have totalled the proportions who have said they are ‘completely’, ‘mostly’ and ‘somewhat’ dissatisfied with their income.

41. HMRC (2014) *Measuring tax gaps 2014 edition: Tax gap estimates for 2012–13*. London: HMRC.

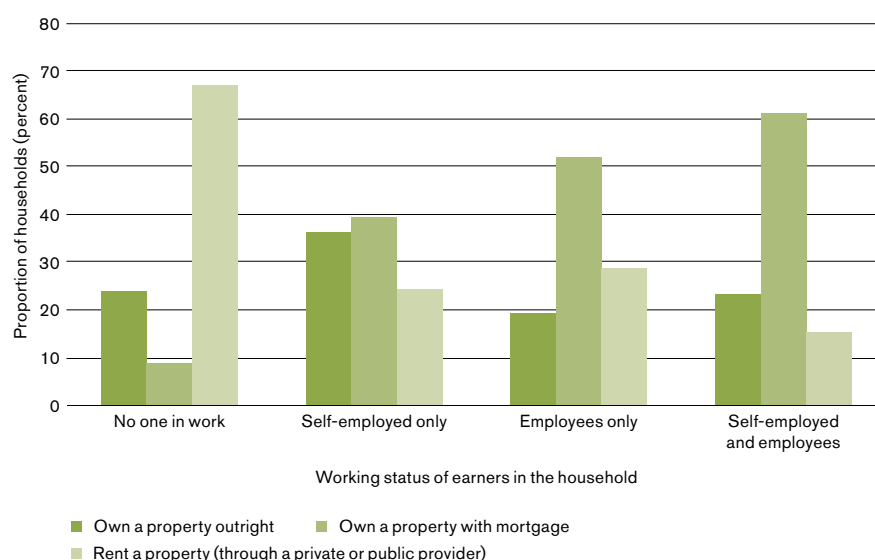
42. See Carter, S. L. (2011) *The rewards of entrepreneurship: Exploring the incomes, wealth and economic wellbeing of entrepreneurial households*. University of Strathclyde Business School.

43. Brewer, M. and O’Dea, C. (2012) *Measuring living standards with income and consumption: evidence from the UK*. Institute for Social and Economic Research.

44. Rutter, J. and Stocker, K. (2014) *Childcare Costs Survey 2014*. Family and Childcare Trust.

45. Bell, A. and La Valle, I. (2003) *Combining self-employment and family life*. York: JRF.

Figure 5: Housing tenure by household working status



Source: RSA analysis of Wealth and Assets Survey 2010/12 (Wave 3)

median financial wealth of households with self-employed workers is higher than employee-only households (see Table 4). Indeed, the proportion of self-employed-only households in ‘material deprivation’ – an indicator of poverty that often takes into account assets – appears to be no higher than the proportion of employee-only households (see Table 9 in the Appendix). It may be that running a business encourages people to stow away savings, thereby boosting asset ownership. However, a more likely explanation is that people have built up their wealth before becoming self-employed. Repeated studies show, for example, that being given an inheritance sharply increases the chances that people will go on to work for themselves.⁴⁶

Table 4: Median wealth by household working status⁴⁷

| Type of wealth | Households with no-one in work | Households with only self-employed workers | Households with only employees | Households with a mix of self-employed and employees |
|---|--------------------------------|--|--------------------------------|--|
| Financial wealth (eg ISAs and current accounts) | £200 | £12,500 | £4,278 | £12,200 |
| Financial liabilities (ie debt) | £46 | £60 | £840 | £1,000 |

This suggests that many of the self-employed may be ‘cash-poor’ but ‘asset-rich’. As with the analysis of earnings, however, it is important to look beyond the median when assessing the extent of asset ownership among the self-employed. There may be a large number of workers that are both cash-poor and asset-poor. The nature of the data collected

46. See for example Blanchflower, D. and Oswald, A. (1998) *What makes an entrepreneur?* Dartmouth College and Warwick University.

47. RSA analysis of the 2010/12 Wealth and Assets Survey (Wave 3).

through government surveys makes it difficult to determine the exact proportions that fall into these different camps. However, we know from the Family Resources Survey that 75 percent of self-employed-only households in the bottom fifth of households (ranked by net disposable income, adjusting for household size) own their own homes outright, compared with 59 percent of employee-only households. While this appears to give some backing to the notion of there being a large cash-poor, asset-rich contingent, the same survey reveals that 23 percent of households with at least one self-employed worker are in debt (the figure is 31 percent for employee-only households). Thus, there are likely to still be many who are poor in both senses of the word.

Box 6: The dividend distraction

Self-employed people who register their business as a company have the option of paying themselves in dividends as well as wages. Since dividends do not attract NICs, it is suspected that many business owners are remunerating themselves in this way, and that this may help to explain the relatively low level of earnings reported in survey data. Our analysis, however, finds little evidence for this claim. When adding investment income (which includes dividend payments) to the earnings data collected by the Family Resources Survey, we find that it does little to change the overall financial picture for the self-employed. The median weekly earnings of self-employed workers stays the same, while the earnings of those in higher income brackets increases only marginally.⁴⁸

Honing in on volatility

There are clearly, then, several points of contention regarding the financial circumstances of the self-employed, and this debate is likely to rumble on in the coming months and years. Yet regardless of your standpoint, there is one feature of self-employed life that most people would agree on: that the earnings of the self-employed are inherently more volatile and subject to fluctuations. Whereas most employees receive the same level of earnings irrespective of their employer's performance, the take-home pay of the self-employed ebbs and flows according to consumer demand and market fluctuations – whether that is a bad harvest for an agricultural worker or dry construction spell for a self-employed builder. Moreover, while employees would probably walk away from their job were their pay to tumble significantly, the self-employed are more likely to try and see the bad times through, thereby extending their experience of low pay. This was seen most visibly in the recent recession, when levels of underemployment among the self-employed rose from around 8 percent in 2006 to 13.5 percent in 2013.⁴⁹ Among employees, underemployment increased from 8 percent to 11.5 percent over the same period.

Yet it is not only the health of the market that can cause income volatility, it is also the health of individual workers. An accident at work or the onset of a chronic health problem can put self-employed people

While employees would probably walk away from their job were their pay to tumble significantly, the self-employed are more likely to try and see the bad times through

48. RSA analysis of 2012/13 Family Resources Survey. The median weekly earnings of the self-employed in 2012/13 stays at £236 when investment income is included. The weekly earnings of the top 10 percent of self-employed earners changes from £867 to £882 when investment income is included.

49. D'Arcy, C. and Gardiner, L. (2014) Op cit.

out of action for months or years at a time, with knock-on effects for their finances. The Association of British Insurers (ABI) estimates that each year one million workers find themselves unable to work due to a serious illness or injury, and that close to 60 percent of households would see their income decrease by at least a third were the main earner to fall ill.⁵⁰ The problem is particularly acute for the self-employed, since they have no recourse to Statutory Sick Pay and would therefore have to rely on Employment Support Allowance (ESA), which usually amounts to around £110 a week and becomes strictly means-tested after a year (unless the claimant has a severe illness or disability.) The ABI believes that 80,000 self-employed people move onto ESA every year.⁵¹

Added to the risk of falling ill is the prospect of being paid late by a client. According to the Federation of Small Businesses, £46bn was owed to small and medium-sized enterprises (SMEs) in late payments last year, more than double the figure in 2008.⁵² Nor is this a problem limited to a select number of established firms. The government reports that 85 percent of small businesses have experienced a late payment in the last two years.⁵³ Not surprisingly, unpaid invoices of this kind serve to disrupt the cash flow of businesses, which has a knock-on effect on the personal finances of self-employed workers. It is increasingly common, for example, for business owners to seek ‘invoice financing’, whereby they are given a proportion of the value of an invoice (usually between 70–90 percent) by a third party company that will ultimately be paid the full amount by the client. The result is that the self-employed lose a significant amount of what they were originally owed – an unfair outcome by any standards.

Flowing with fluctuations

Whether it is a result of personal illness, market forces or unpaid invoices, the degree to which people are affected by income volatility depends on a number of factors. Self-employed people with savings, for instance, will be better placed to weather unexpected income shocks than those without. Yet as noted before, despite typically having greater financial wealth than employees, around a fifth of self-employed workers are in debt. The debt support charity StepChange believes that every family should have at least £500 stowed away, which is the equivalent of the average payday loan debt of their clients.⁵⁴ Of course, people need to earn enough money to save in the first place, which requires having a sustainable business that turns a healthy profit (an issue we will examine later in the report). But regardless of their level of income, it is important that people are encouraged to get into the habit of saving.

One way to support this behaviour would be to establish more innovative savings schemes based on automation. Lloyds Bank, for instance, recently created a ‘Save the Change’ offer for its clients, which

50. Association of British Insurers (2014) *Welfare reform for the 21st century*. ABI.

51. Ibid.

52. Federation of Small Businesses (2014) *FSB Manifesto for the 2015–20 Government*. London: FSB.

53. BIS (2014) *Building a responsible payment culture*. [Government response to consultation].

54. Stepchange (2014) *Life on the edge: Towards more resilient family finances*.

works by rounding up people's transactions to the nearest pound and transferring the extra amount to a savings account. Here the action happens at the moment when people spend, but a savings mechanism could also kick in at the point at which people are paid. With a particular focus on the self-employed, banks could establish a 'Save When Paid' system so that a proportion of the value of every invoice is immediately deposited into savings when processed. Another option – and one better suited to low-income groups such as the self-employed hairdresser or gardener – would be for DWP to embed a procedure that enables people to voluntarily sign up to an automated saving system within the new Universal Credit programme. Under this scheme, claimants would have the option of channelling a small percentage of their benefit into a savings account as soon as they are paid every month.

R1 – Establish automated saving schemes for the self-employed on low incomes

The government should provide an option within the Universal Credit system that allows claimants to automatically channel a percentage of their benefits into a savings account. Banks should consider following suit by creating a 'Save When Paid' initiative for their self-employed clients, which would take a small amount off the value of every invoice and immediately transfer this into savings.

As well as having a savings cushion to fall back on, the ability of people to respond to income dips also depends on whether they can **reduce outgoings** at short notice. For the majority of the self-employed who do not own their homes outright, this means first and foremost delaying or reducing their rental costs or mortgage repayments. There have been several promising developments in this regard. A number of lenders have signed up to the government's Homeowners Mortgage Support (HMS) scheme, which enables people to switch to an interest-only mortgage for a temporary period. Moreover, banks like Aldermore are already looking at options for mortgage products that give the self-employed flexibility with over and underpayments – even allowing them to take out money when it suits their needs.⁵⁵ It is tempting to suggest that further progress could be made by simply mandating that all mortgage providers and landlords offer more flexible terms to their clients. However, this is a crude policy lever, and an unintended consequence may be that providers become even less willing to offer mortgages and rental agreements to the self-employed in the first place.

A more measured intervention would be to establish a statutory 'Right to Request' process, whereby every self-employed worker would be eligible to ask for more flexible terms on their mortgage repayments or rental costs. In practice, this could mean asking to switch to an interest-only mortgage or to freeze rent payments entirely. Providers would then be obliged to consider every proposal and state in clear terms the reasons behind their decision. This would ensure that every homeowner and

55. Partlington, S. (2014) *Aldermore sets sights on self-employed market* [article] Mortgage Solutions: 21st August 2014.

renter benefits from a clear and transparent appraisal of their situation, which could in turn lead to a more appropriate decision being made by their provider. The number of positive outcomes to such requests could also be made publicly available, so as to incentivise providers to do their best to meet the needs of their clients. Alongside establishing a Right to Request process, the government should also convene relevant stakeholders to consider the scope for devising new mortgage products and rental agreements for the self-employed, which cater better to those with income fluctuations.

R2 – Establish a ‘Right to Request’ for more flexible terms on mortgage repayments and rental costs

The government should establish a statutory right for self-employed workers (and possibly employees) to ask for more flexible terms on their rent and mortgage payments, for example by switching to an interest-only mortgage. Providers would be obliged to clearly state the reasons behind their decision, thereby bringing a degree of transparency to the process.

A third important factor is the degree to which the self-employed are **mindful of risks** and aware of their potential consequences. Those who can comprehend the dangers posed by a market crash or sudden illness are far more likely to take early action, whether that is by building up a ‘rainy-day’ fund or diversifying their household income streams. However, a growing body of evidence from the field of behavioural science reveals that people are generally poor at planning for unforeseen events, which leaves them susceptible to hardship. This may be particularly true of business owners, who are often left too cognitively strained from the task of running their venture to think carefully about the future.⁵⁶ Added to this is the tendency of business owners to be over-optimistic about their prospects.⁵⁷ An intriguing US study found that over 80 percent of business owners believed their likelihood of ‘success’ was at least 70 percent, while a third said their chance of failing was zero.⁵⁸ This is despite the survival rate for firms being just 35 percent at the time the research was reported.

With this in mind, it is critical to find a means of focusing the attention of the self-employed on the risks they face, so as to encourage them to prepare for the future. The aim should be to help them understand, for example, how much they would lose were they to fall ill and have to rely on ESA, or how much they should expect were they to become pregnant and only have access to the Maternity Allowance (the next chapter explores welfare support in more detail). One option would be for HMRC to provide a forecasting service when people complete their Self-Assessment return or monthly Universal Credit report, which

56. Dellot, B. (2014) *Everyday Employers*. London: the RSA.

57. A study of people supported into business by the Prince’s Trust found that the most ‘risk averse’ individuals had the highest survival rates. See Meager N., Bates P. and Cowling, M. (2003) *Business start-up support for young people delivered by The Prince’s Trust: a comparative study of labour market outcomes*. DWP Research Report no.184.

58. Cooper, A. C., Woo, C. Y. and Dunkelberg, W. C. (1988) “Entrepreneurs’ perceived chances for success” in *Journal of Business Venturing* 3(1).

would present a number of potential scenarios that might face them in the future. The government could also provide financial backing to new ‘quantified venture’ apps that help the self-employed make better sense of their financial information and that of their business.

R3 – Introduce financial products and services that improve income forecasting

HMRC and the Department for Work and Pensions should work with behavioural economists to devise new ways to help the self-employed understand how their financial situation could change in light of different events, for example were they to fall ill or fail to take out a private pension.

Where next for pensions?

While some income shocks are unpredictable, one that is almost guaranteed is the moment at which people leave employment and enter retirement. Despite its inevitability, however, many of the self-employed are failing to contribute to a private pension that could support them in old age. Media articles such as ‘Self-employed facing pensions time bomb’ and ‘Self-employed? You’re walking into a pensions nightmare’ paint a bleak picture of what awaits them in retirement – and these views are to some extent corroborated by government data.⁵⁹ The Family Resources Survey shows that just 26 percent of the self-employed are currently contributing to a private pension, down from 42 percent in 2002. In contrast, 50 percent of employees are signed up to a private pension scheme (see Figure 6). Yet it is not just the proportion of self-employed workers making contributions that is relatively low, it is also the overall size of their pension pots. The Wealth and Assets Survey finds that 55–64 year-olds in self-employment (the group closest to retirement) have a median average of £50,000 in private pension wealth, which is around half the £98,700 enjoyed by their counterparts in a typical job.

Just 26 percent of the self-employed are currently contributing to a private pension, down from 42 percent in 2002

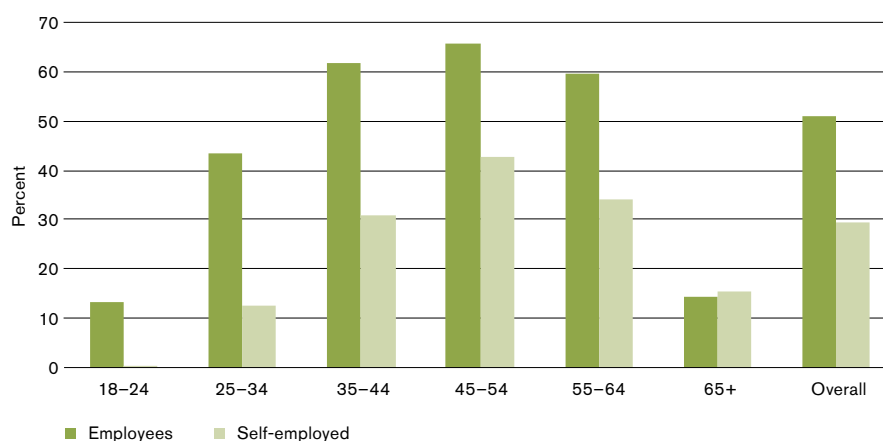
There are several potential factors that account for this pensions shortfall. One of the main reasons is that self-employed people do not benefit from employer contributions, which act as a major incentive for employees to sign up to an occupational scheme. According to the pensions firm Prudential, people who strike out on their own forgo an average of £91,500 in employer contributions over their lifetime.⁶⁰ A related issue is that, unlike employees, the self-employed do not have a Human Resources department that will regularly prompt them to take part in a scheme, nor an in-house pensions expert who can handle the administrative tasks involved in enrolment. Indeed, the pensions gap between the self-employed and employees is likely to widen further with the introduction of auto-enrolment, which will eventually mandate that every employer must enrol their staff automatically onto a pensions scheme. Despite being open to the self-employed, the state-backed pension

59. See www.nexuswealthplanning.co.uk/self-employed-facing-pensions-timebomb and www.telegraph.co.uk/finance/personalfinance/11174288/Self-employed-Youre-stumbling-into-pensions-nightmare.html

60. Prudential (2013) Self-employed miss out on £91,500 in retirement, Pru reveals. Available: www.pru.co.uk/guides_tools/articles/801594981-Self-employed-mi/

provider Nest says that just 800 have voluntarily signed up with them, compared with 1.9 million employees who have been auto-enrolled by their employer (three million have been enrolled in other private schemes).

Figure 6: Proportion of workers contributing to a pension (by age)



Source: RSA analysis of Family Resources Survey 2012/13

Alongside the absence of employer support, another reason why the self-employed contribute less to pensions is that they tend to have lower incomes (as discussed earlier). Given that many earn below the minimum wage it is understandable that the community has low rates of participation. Our analysis shows that just 23 percent of self-employed workers below the poverty line are currently contributing to a pension.⁶¹ Added to this is the volatile nature of self-employed earnings, which makes it more difficult to regularly siphon off money into long-term savings. Around 10 percent of self-employed people have pension contributions that are ‘frozen’, a decision they may have made in response to an unexpected drop in income. The fact that it can take time for a business to turn a reliable and steady profit may also help to explain why the self-employed appear to start saving at a later age. As Figure 6 shows, very few 25–34 year-olds in self-employment are contributing to a pension in comparison with employees of the same age. The reason this matters is because of compounding interest, which strongly favours those who save earlier in life (see Box 7) Each of these factors pose a considerable challenge to long-term saving, yet it is important to be aware that some people may have taken a positive decision not to contribute to a personal pension. Many of the self-employed, for example, appear to have opted to put their savings into Individual Savings Accounts (ISAs) as an alternative nest egg for retirement. The Wealth and Assets Survey reveals that 55 percent of households with a self-employed worker have savings in an ISA, with the mean average for self-employed-only households amounting to around £17,000 versus £8,000 for employee-only households.⁶² ISAs are attractive to the self-employed in part because they allow people to access their savings more

61. RSA analysis of 2012/13 Family Resources Survey.

62. RSA analysis of 2010/12 Wealth and Assets Survey (Wave 3).

Box 7: The importance of compounding interest

The public debate around pensions tends to focus on the question of how we can encourage more people to sign up to a private scheme. Yet far less attention is paid to the important matter of how we can prompt them to do so early on in their careers. The nature of compounding interest – where the return from savings grows exponentially over time – means that people who begin saving at an early age often end up with a much larger pension pot than others who save the same amount but begin at a later age. The Money Advice Service estimates that someone saving £100 a month for 40 years would be rewarded with £190,000 upon retirement, assuming an average annual growth rate of 6 percent.⁶³ However, someone saving £200 over 20 years would end up with a pension pot of just £90,000, despite stowing away an equal amount.

readily, which is useful for a business owner who needs to plug a dip in income or make a large one-off purchase. The terms of ISAs are also usually more understandable. A recent study undertaken by Nest found that people felt more in control of savings when they were in a cash ISA rather than a pension, in part because ISAs involve fewer intermediaries.⁶⁴ For these reasons, ISAs may be a particularly important route to saving for people on low-incomes (although it should be noted that having large ISA savings may adversely affect people's benefit entitlements under Universal Credit).⁶⁵

Whether it is through a pension or ISA, it is critical that we find new ways of encouraging the self-employed to save for their retirement. The government's decision to open up the new Single-tier State Pension to the self-employed will undoubtedly be helpful, but public provision should not be seen as a panacea. One solution would be to introduce greater financial incentives, such as extra tax relief on self-employed pension deposits, which would partly make up for the lack of employer contributions. Yet it is easy to see how this could be abused through false self-employment, to say nothing of the extra cost burden. In any case, one of the clearest messages from the Pensions Commission conducted nearly a decade ago was that efforts to boost pension enrolment through financial incentives had failed.⁶⁶ An alternative policy response is to apply techniques drawn from the field of behavioural economics, such as those which formed the basis for auto-enrolling employees onto a pension scheme. The outcomes of this policy have so far proven very promising: five million workers are now signed up to a workplace pensions scheme and only 9 percent have chosen to opt out – a much lower proportion than originally anticipated. Moreover, Nest itself has shaken up the pension industry by charging just 0.5 percent commission versus a sector average of 1–3 percent a year.

63. See <https://www.moneyadvice.service.org.uk/en/articles/pensions-for-the-self-employed>

64. Nest (2014) *Improving consumer confidence in saving for retirement*. London: Nest.

65. Michael Johnson presents a persuasive case for ISAs in Johnson, M. (2010). *Simplification is the key*. London: CPS. However, an emerging issue is that ISA savings will be included within the capital assessment for Universal Credit. Anyone with savings over £16,000 will not be able to receive UC, meaning it may act as a disincentive to save in any scheme other than a pension.

66. Accessible via www.news.bbc.co.uk/1/hi/business/4482460.stm

Box 8: Is the business a pension in itself?

One common explanation for why the self-employed are less likely to contribute to a pension scheme is that many consider their business assets to be a nest egg. The theory is that business owners spend their careers building up capital such as property and machinery, knowing these items can be sold on upon retirement. However, it is difficult to determine how many people do this or how much their assets are worth. The conclusion of the Pension Commission's report, at least, was that the sale of business assets was only feasible for a 'very small minority' of the self-employed.⁶⁷

This begs the question of whether the self-employed should also be auto-enrolled onto a workplace pension scheme like Nest. Putting the administrative challenges to one side, our view is that it would be unwise to do so, mainly because of the aforementioned issue of volatile incomes but also because of the clear preference among some to have more flexible access to their savings. A more appropriate option would be to present a 'compulsory question' to the self-employed when they complete their tax return or Universal Credit application, whereby they would have to declare – yes or no – whether they wanted to save into a workplace pension scheme like Nest, and/or a government-backed ISA. A study of one such 'forced choosing' scheme, albeit among employees rather than the self-employed, found that pension enrolment rates in the first four months of job tenure jumped from 9 percent to 34 percent after it was introduced.⁶⁸ The implication is that the use of a compulsory question could result in potentially hundreds of thousands more self-employed people preparing for retirement.

R4 – Present a 'compulsory question' for enrolment onto a pension or ISA scheme

The government should present the self-employed with a compulsory question as to whether they wish to join a workplace pension scheme or a government-backed ISA, for example one provided by the NS&I. To increase the likelihood of take-up, this should be done at a moment of financial reflection, such as when people complete their tax return or UC application.

67. See Sainsbury, R., Finch, N. and Corden, A. (2006) *Self-employment and retirement*. DWP.

68. Carroll, G. (2005) *Optimal defaults and active decisions* [NBER Working Paper].

Spreading risks

In this chapter we consider how the risks associated with self-employment, such as the income volatility noted in the last section, might be spread and pooled with others. In doing so we look at whether there needs to be a new tax and welfare settlement for the self-employed, given that this has historically been the primary route through which risk has been shared. We also look at whether improvements could be made to the way welfare is delivered in practice, including through the new Universal Credit programme. Finally, we explore the degree to which the self-employed could support one another in the absence of government intervention, for example through a collective cash-pooling scheme.

The welfare dilemma

While taking action to boost savings and change spending patterns is important, we have to acknowledge that there is only so much that the self-employed can do on their own to manage the risks they face. The only way to fully prepare for the prospect of a severe illness or market meltdown is to pool risk among many, such that the least affected support the most affected. This is the founding principle of welfare, by which we mean the various social security protections offered to workers by the state, or which employers are mandated to provide. The self-employed were originally excluded when David Lloyd George introduced the first elements of social security in 1911, and it was only in 1945 with the birth of the full welfare state that ‘persons working on their own account’ were absorbed into the National Insurance programme.⁶⁹ Today self-employed workers have access to many of the same protections enjoyed by employees, including Working Tax Credit, Housing Benefit and the Council Tax Reduction. Moreover, it was recently announced that the self-employed will be eligible for the Single-tier State Pension when it is introduced in 2016 (just as employees will be).⁷⁰

The self-employed were originally excluded when David Lloyd George introduced the first elements of social security in 1911

However, there are several areas where welfare coverage is still limited for the self-employed. A self-employed taxi driver or artist who leaves their business to search for other work, for example, will usually not be able to access contribution-based Jobseeker’s Allowance (CBJSA). The income-based version is open to them, but to be eligible claimants must earn below a low threshold and work fewer than 16 hours a week. Those who work for themselves also lose out on Statutory Maternity Pay, and instead have access to the less generous Maternity Allowance. The latter is paid at a set rate of just over £138 a week, whereas the former

69. Social Security Advisory Committee (2014) *Social security protection and the self-employed*. London: SSAC.

70. For more information regarding the impact of the SSP, see Crawford, R., Keynes, S. and Tetlow, G. (2014) *A single-tier pension: what does it mean for individuals?* London: IFS.

amounts to 90 percent of previous earnings for the first six weeks. Other benefits that self-employed people forgo include employer pension contributions, Statutory Paternity Pay and Statutory Sick Pay, to name a few (see Table 5). The absence of Statutory Sick Pay may be one reason why the self-employed are significantly less likely than employees to take time off from work due to an illness.⁷¹

Table 5: Social security protections not presently open to the self-employed⁷²

| State-led | Mixed-responsibility | Employer-led |
|---|---|--|
| <ul style="list-style-type: none"> ▪ Jobseeker's Allowance (contribution-based) ▪ Industrial Injuries Disablement Benefit | <ul style="list-style-type: none"> ▪ Statutory Maternity Pay ▪ Statutory Paternity Pay (employers can claim a large proportion of SMP and SPP payments back from the state) | <ul style="list-style-type: none"> ▪ Employer pension contributions ▪ Statutory Sick Pay (until recently employers could claim most of this back from the state) |

The question is whether such gaps in welfare can and should be addressed. The optimal scenario would be for the government to extend more social security protections to the self-employed. However, with all parties committing to substantial spending cuts throughout the next parliament, it is difficult to see how this would be financially feasible under current arrangements. The fundamental stumbling block – both in terms of fairness and finance – is that the self-employed contribute proportionally less in National Insurance contributions (NICs) than their counterparts in wage work (see Table 6). A self-employed worker on £15,000 a year pays only £771 in NICs – including the £146 a year in Class 2 contributions – whereas an employee earning the same amount has £830 deducted, plus the £947 paid by their employer (the situation is slightly different for part-time employees, whose employers typically do not have to pay employer NICs given their low earnings). Many economic commentators such as the tax expert Judith Freeman believe that the self-employed already receive more protection than their NIC contributions merit.⁷³ Indeed, HMRC estimates that the self-employed community pay £2.9bn less in taxes than they would have done were they to face the same NIC rate as employees (even accounting for their lower social security entitlements).⁷⁴

71. The Understanding Society Survey (2011/12) shows that 1.7 percent of the self-employed took time off leave due to illness in the week prior to the survey, compared with 2.3 percent of employees. This may be a result of them being more committed to their work, but it could also reflect an inability to forgo earnings from lost working days.

72. State-led protections are those financed exclusively by the state, mixed-led are those financed partly by the state and employers, and employer-led are those paid for exclusively by employers.

73. Houlder, V. (2014) *Calls to end national insurance tax subsidy for self-employed* [article] Financial Times, 21st September 2014.

74. Cited in Corlett, A. (2013) *Ending the self-employment tax break*. Centre Forum.

Table 6: National Insurance contributions by worker type (2015/16 rates)

| Tax | Self-employed | Employees |
|---------------|--|--|
| Employee NICs | Pay two classes of NICs: Class 2 – Levied at £146 a year for those earning more than £5,965 Class 4 – Levied at 9% of profits from £8,060 to £42,385 a year, and 2% over that amount | Pay one class of NICs: Class 1 – Levied at 12% of earnings between £8,060 and £42,380, and 2% over that amount |
| Employer NICs | Not applicable | Employers pay 13.8% of the employee's earnings above £8,112 a year |

N.B. As self-employed workers and employees already pay the same level of income tax, there is little scope or appetite to adjust rates in this area.

Something for something

What, then, should our answer be to this welfare dilemma? In determining our response it is worth considering the approach taken by other comparable countries. While Denmark offers equal social security protections to all workers, a more popular system in Europe is to allow the self-employed to ‘top-up’ a basic allowance of welfare by paying higher taxes. Aside from being more financially sustainable for the state, the attraction of having a voluntary model is that it gives people the freedom to choose the protections best suited to their needs, such as extra maternity pay if they believe they are likely to have a child in the future. However, this model has a number of drawbacks – not least that it excludes those who cannot afford the extra protection. Another shortcoming is that it relies on people to be mindful of the risks that unexpected events could occur, for example that they could fall ill. Yet as discussed in the last chapter, people are generally poor at planning adequately for the future. This may explain why there tends to be low voluntary take-up of social security protections in the places that offer them, such as Hungary and the Czech Republic.⁷⁵

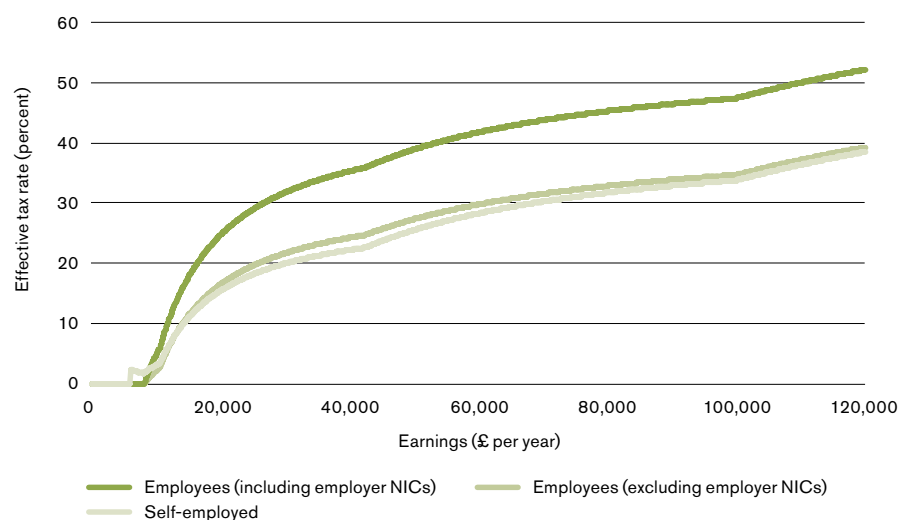
The honest answer is that there is no possibility of extending welfare coverage in a way that is fair or affordable without increasing the tax rates paid by the self-employed – a move that may hurt in the short-run, but which will improve the living standards of many workers over time. In doing so, however, two main principles should be followed. The first is that the best part of the extra burden be placed on the highest earners, who currently benefit substantially from the existing tax system (see Figure 7, which shows the proportion of people’s income that is deducted through Income Tax and NICs). A self-employed person earning £60,000 a year pays close to £900 less in NICs than someone earning the same amount as an employee, to say nothing of the extra £7,000 forgone in employer NICs. The second principle is that the self-employed should not have to pay *exactly* the same level of tax as employees. The point of this relief is not to reward the part they play in creating jobs or developing

The honest answer is that there is no possibility of extending welfare coverage in a way that is fair or affordable without increasing the tax rates paid by the self-employed

75. European Employment Observatory Review (2010) *Self-employment in Europe*. Social Europe.

innovative products, which can be achieved through more targeted tax breaks, but rather to recognise that self-employment as a form of work is essential to a flexible and dynamic economy.

Figure 7: Effective tax rates paid according to employment status (Income Tax and NICs)



In practice we propose that the next government follows through with George Osborne’s recent commitment to abolish Class 2 NICs, which are levelled at a flat rate of £146 a year. Most self-employed people are required to pay this regardless of how much they earn, making it a regressive poll tax that is hard to justify. The second major change would be to increase the rates of Class 4 NICs. We argue that the self-employed should pay 13 percent on their profits above the NICs threshold, rather than 9 percent at present. While this is 1 percent higher than the Class 1 NICs rate paid by employees, the effective tax rate paid by most self-employed people would still be lower when taking into account the absence of employer contributions. In keeping with our commitment that low earners are not overwhelmed by these changes, the earnings threshold at which NICs kick-in would be increased to £10,600 (the basic rate Income Tax threshold).

Our analysis of the impact of these changes using the Landman Economics/IPPR tax-benefit model shows that they would raise around £280m per year extra for the exchequer, while having a progressive distributional impact overall. Around 38 percent of self-employed workers (with incomes from self-employment between £5,965 and approximately £20,000 per year) would gain from the reforms, with those earning more than £20,000 (around 34 percent of self-employed people) losing and the remaining 27 percent earning too little to be affected by the reform. A self-employed hairdresser with an annual income of £11,000, for example, would be £359 better off under our proposals, while an independent business consultant on £45,000 a year would pay £801 more in National Insurance.

One potential and positive by-product of these tax changes is that they could diminish the incentives for false self-employment, which is often born out of attempts to limit the amount of NICs paid in typical employment (see Box 9). However, a potential disadvantage is that they create incentives for higher earners to incorporate their business, allowing them to pay themselves in dividends and thus avoid National Insurance levies. At the other end of the income scale, a perverse effect may be to encourage vulnerable people to move into self-employment when they are clearly better suited to working for somebody else. Further work should be done to explore how we can ameliorate behaviour of this kind.

R5 – Abolish Class 2 NICs and establish a more progressive Class 4 NICs system

The tax system should be overhauled in such a way that the self-employed as a whole pay more in National Insurance contributions, but where the greatest burden is placed on the highest earners. Our proposal is to:

- Increase the rate of Class 4 NICs from 9 percent to 13 percent of earnings about the NICs threshold.
- Raise the Class 4 NICs threshold to £10,600 (the basic rate Income Tax threshold).
- Abolish Class 2 NICs, which are currently levelled at a flat rate of £146 a year.

We estimate these reforms would raise close to £280m per year for the exchequer.

Box 9: The impact of tax in fuelling false self-employment

False self-employment describes cases where a worker is taxed as self-employed but is an employee for all intents and purposes (eg they take orders from someone else and do not set their own hours). Behaviour of this kind is thought to be an endemic problem within the construction industry, but there is also evidence of dubious self-employment becoming commonplace in more structured sectors such as teaching and local government. The reason some employers encourage their staff to declare themselves as self-employed is so they can avoid paying employer NICs. In the short-term this is ostensibly good for the employee, since they end up paying lower NICs themselves. However, they may not realise that they lose access to important protections such as sick pay and redundancy payments. Increasing the NIC rates of the self-employed would go some way towards addressing this problem since it would remove the incentive for the employee to switch roles. However, clearly some workers have less discretion than others and may be forced by their employer to continue engaging in false self-employment against their will. It should be stressed that evidence for false self-employment is only anecdotal, and therefore we recommend that more work be done to understand the true scale of the problem.

Increasing NIC rates along these lines would go some way towards financing the extension of contributory benefits to the self-employed. However, every individual form of protection – from maternity cover to sickness insurance – will vary in terms of its costs, the likely benefits and the extent to which it may invite abuse and manipulation. Therefore

the sensible approach is to consider every benefit separately and take a view as to whether it can be extended to the self-employed. It is beyond the remit of this paper to undertake a full review of welfare, but there is a strong argument in particular for opening up Statutory Maternity Pay and Statutory Paternity Pay to the self-employed – even if the government decides not to raise National Insurance rates. The primary reason is because SMP and SPP are forms of protection not just for workers but also for their new-born (or adopted) children, who should be able to receive the same level of care regardless of the occupation their parent has chosen. This would follow the precedent set by the new Tax-Free Childcare scheme, which allows both employees and the self-employed to access financial support to pay for childcare.

R6 – Consider opening up Statutory Maternity Pay and Statutory Paternity Pay to the self-employed

The government should consider extending Statutory Maternity Pay and Statutory Paternity Pay to the self-employed, regardless of whether changes to NIC rates are implemented. This would recognise that SMP and SPP are forms of protection not just for workers but also for new-born (or adopted) children, all of whom should benefit from the same level of care irrespective of their parents' occupation.

Welfare in action

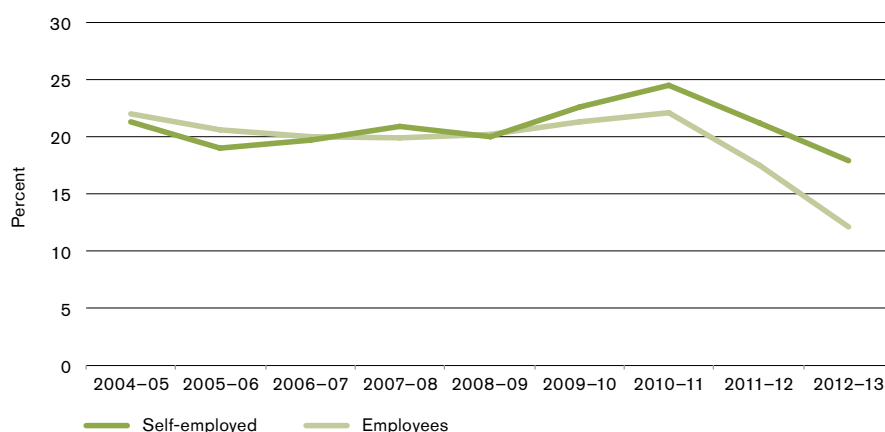
Clearly any attempt to solve the welfare dilemma will require imaginative thinking and bold interventions from the incoming government, particularly at a time of unprecedented spending cuts. Yet to focus only on the task of extending eligibility for social security protections would be to ignore the equally important matter of improving the way that self-employed people interact with welfare as it stands. It is worth looking in particular at how the self-employed use Tax Credits, given the large number that rely on them to bolster their low incomes. At present, close to 18 percent of self-employed people – the equivalent of 810,000 workers – are in receipt of either Working Tax Credit or Child Tax Credit, compared with 12 percent of employees. Figure 8 shows that the proportion of claimants rose sharply after the recession took hold in 2008, but dipped back to its pre-crisis level after 2010, perhaps in part due to tougher eligibility criteria coming into force.⁷⁶ It is interesting to note that prior to 2006/07, the self-employed were marginally less likely to be claiming Tax Credits than people in wage work.

Despite the relatively high proportion currently in receipt of Tax Credits, one of the issues we identified is that there are still many who are not claiming their entitlement. Using the Landman Economics/IPPR tax-benefit model, we calculate that the 'take-up' rate among the self-employed is just 61 percent, compared with 87 percent among employees

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76. The sizeable fall in Tax Credit claimants that occurred during the coalition government years may be due to changes in eligibility criteria, such as the increase at the rate at which the Family element is withdrawn, and the introduction of a requirement for couples with children to work 24 hours before they qualify for Tax Credits. For more information see O'Connor, M. (2014) Straw Men? [Blog] Available: www.strongerinnumbers.com/blog15.html

Figure 8: Proportion of workers receiving Tax Credits over time



Source: RSA analysis of Family Resources Survey 2012/13

(see Figure 9).⁷⁷ Of the 350,000 self-employed not claiming their entitlement, some may have taken a conscious decision to eschew benefits for reasons of personal pride. Others, however, may simply be unaware of the protections open to them. A second issue with Tax Credits is that those who use them are far more likely than employees to be claiming for a long period of time. The Understanding Society Survey shows that around 9 percent of self-employed workers claimed Tax Credits in each of the three years the survey was undertaken, compared with 5 percent of employees.⁷⁸ The implication is that some of these workers may be better off in typical employment, or could at least benefit from more support in making their business viable (a topic we revisit in the next chapter).

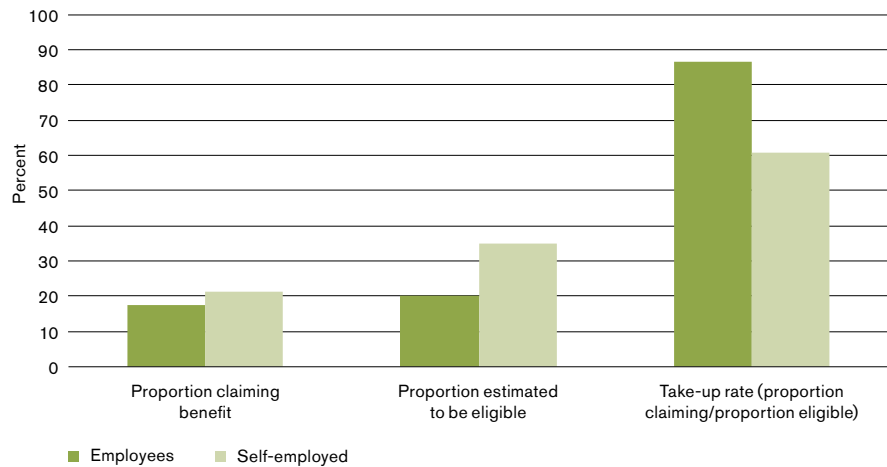
A third problematic feature of the Tax Credits system relates to overpayments. The amount of Tax Credits self-employed workers are entitled to is determined at the start of every tax year for the following 12 months, but this is only an estimate based on their current circumstances and how much they earned the year previously. While self-employed workers are encouraged to report any unexpected changes in income or family status to HMRC, in practice very few remember to. The result is that those who earn a few thousand pounds more than anticipated often face a large one-off bill, which in turn puts them in financial difficulty. Unfortunately, our Freedom of Information request for an estimate of the number of people affected was declined by HMRC, on the grounds that the data is too complex to assess. However, anecdotal evidence in the form of feedback from Citizens Advice and StepChange advisers suggests overpayments are common. Although claimants are in theory able to lodge an appeal, HMRC has complete discretion over what is classed as an overpayment. Indeed, it is concerning that HMRC was recently given powers to settle unpaid tax bills by directly accessing people's current

⁷⁷. This model currently uses Family Resources Survey data from 2011/12. A model that uses 2012/13 data has yet to be developed. For more information about the Landman Economics/IPPR tax benefit model, please contact Howard Reed at Landman Economics www.landman-economics.co.uk/

⁷⁸. RSA analysis of Understanding Society Survey data (Wave 1 = 2009/10, Wave 2 = 2010/11, and Wave 3 = 2011/12).

accounts and ISAs.⁷⁹ The department estimates that 17,000 people a year will be affected, most of whom are likely to be self-employed.

Figure 9: Proportion of workers taking up their Tax Credit entitlement



Source: Family Resources Survey (2011–12) and the Landman Economics/IPPR tax benefit model

A straightforward response to these challenges would be to establish a campaign aimed at informing the self-employed about their rights. The self-employed should know, for example, that they are entitled to Working Tax Credit, the Maternity Allowance and, in the coming years, the new Single-tier State Pension. The campaign could also remind those who are currently in receipt of Tax Credits to inform HMRC if their income changes, so as to improve the accuracy of their payments. One way of running the campaign is to work with business support organisations such as the Federation of Small Businesses and Enterprise Nation, who could act as a conduit for information. Accountants could also act as messengers, given they are widely trusted and come into contact with the self-employed on a regular basis. The government’s Small Business Survey reveals that 38 percent of non-employing business owners who had taken advice in the last 12 months did so from an accountant, versus 6 percent who had used the internet.⁸⁰ Perhaps the best vehicle for this campaign, however, would be the Post Office, since half of business owners are thought to visit their local branch at least once a week.⁸¹

Transitioning to Universal Credit

While it is important to continue making improvements to the existing benefits system, we should not forget that the self-employed will soon make the transition to Universal Credit (UC). Indeed, the government believes that the arrival of UC will help to solve the worst of the aforementioned challenges by streamlining the welfare system and rolling six means-tested benefits into one, including Jobseeker’s Allowance, Housing

79. Jones, R. (2014) *The Revenue doubles use of bailiffs to recover unpaid tax* [article] The Guardian: 17th May 2014.

80. BIS (2013) Op cit.

81. Dellot, B. (2014) *Making the Connection*. London: RSA.

R7 – Initiate a campaign to inform the self-employed of their welfare entitlements

The government should work with business support organisations, accountants and the Post Office to raise awareness among the self-employed of the various benefits open to them, such as Tax Credits and the Maternity Allowance. The self-employed should also be encouraged to inform HMRC if their income or family circumstances change, so as to minimise the chance of them being overpaid or underpaid in benefits.

Benefit and Tax Credits. Self-employed people who wish to make a claim for UC will first need to attend a Gateway Interview with a Jobcentre Plus (JCP) adviser to assess whether they are ‘gainfully self-employed’. Should they qualify, they will not be required to search for other work or attend interviews. However, they will have their Credit entitlement pegged to a Minimum Income Floor (MIF), which will be the equivalent of the minimum wage (c. £950 a month). Essentially, this means that anyone earning below the MIF will not have the difference made up in extra Credit. For example, someone earning £600 a month will be given the same amount as someone on £800, while anyone earning more than the MIF will see their entitlement gradually diminish in line with their income. Part of the rationale for introducing the MIF is to prevent people from claiming Tax Credits while running a business that has little expectation of making a profit.

The DWP estimates that replacing the existing benefits system with UC will save the government £38bn over 12 years from its inception.⁸² Yet it is no secret that the flagship welfare programme has been beset by difficulties – both in terms of its delivery and design.⁸³ A number of concerns have been raised in particular about the treatment of self-employed households, over a million of which are expected to be in receipt of UC. One of the central complaints is that the new monthly assessment period could put those with more volatile incomes at a disadvantage. For example, an agricultural worker with three months of very high income and nine months of very low income could be worse off under the new system, since during the good months they will earn so much that they do not qualify for UC, while during the bad months they will not be compensated with any more UC than the MIF allows. Case studies 1 and 2 in Table 7 show how two different people with the same income can be entitled to significantly different amounts of UC depending on whether or not their earnings fluctuate (with thanks to the team at Ferret Information Systems for creating these case studies).

It is no secret that the flagship welfare programme has been beset by difficulties – both in terms of its delivery and design

82. National Audit Office (2014) *Universal Credit: Progress update*. London: NAO.

83. Ibid.

Table 7: The impact of Universal Credit on different types of self-employed workers (Based on estimates using Ferret's Future Benefits Model, FFBM)⁸⁴

| Case study | Circumstances | Current monthly benefit entitlement | New entitlement under Universal Credit | Difference in amount received |
|------------|---|-------------------------------------|--|-------------------------------|
| 1 | <ul style="list-style-type: none"> ▪ Earnings: £15,000 gross a year (in regular monthly payments) ▪ Expenses: £2,400 a year ▪ Hours: 35 hours full-time ▪ Relationship status: Single and childless ▪ Rent: £150 a week | £298.24 | £434.47 | +46% |
| 2 | <ul style="list-style-type: none"> ▪ Earnings: £15,000 gross a year (alternating monthly between £625 and £1,875) ▪ Expenses: £2,400 a year ▪ Hours: 35 hours full-time ▪ Relationship status: Single and childless ▪ Rent: £150 a week | £298.24 | £302.73 | +1.5% |
| 3 | <ul style="list-style-type: none"> ▪ Earnings: £9,000 gross a year (in regular monthly payments) ▪ Expenses: £1,000 a year ▪ Hours: 35 hours full-time ▪ Relationship status: Single with a child ▪ Rent: £150 a week | £1,109.29 | £923.92 | -17% |
| 4 | <ul style="list-style-type: none"> ▪ Earnings: £9,000 gross a year (in regular monthly payments) ▪ Expenses: £1,000 a year ▪ Hours: 35 hours full-time ▪ Relationship status: Single and childless ▪ Rent: £150 a week | £572.13 | £482 | -16% |

Another concern is that the MIF has been set too high, based as it is on an erroneous assumption that the majority of the self-employed can earn the equivalent of the minimum wage.⁸⁵ Using income data from the Understanding Society Survey, we estimate that as many as 42 percent of self-employed workers currently have an income that would fall below the MIF (see Table 8). Not all of these individuals will apply for UC, but those

84. This analysis was kindly undertaken by Gareth Morgan from Ferret Information Systems. Ferret produces a wide variety of systems, designed to provide support tools for advice workers, and also to provide information and advice directly to the public.

85. The government implicitly acknowledges that many self-employed workers will never earn the equivalent of the minimum wage, and that they will necessarily have to either cease claiming or start searching for other work. However, it is unclear whether the government and those in the DWP are aware that such a large number will fall into this bracket (42 percent according to our estimate).

who do are likely to be financially worse off under the new system. Case study 3 in Table 7, for example, shows that a lone parent earning £9,000 a year could have their benefit entitlements cut by 17 percent. The government acknowledges that it can take time to create a viable business that turns a profit, and as such has introduced a ‘Start-up Period’. This will mean that the newly self-employed are not subjected to the MIF rules for their first 12 months. Yet many people take longer than a year to find their footing, particularly those who are new to the world of business. Even with the year-long Start-up Period, we calculate that 32 percent of self-employed workers would still fail to reach the MIF in time (see Table 8).

Table 8: Proportion of workers who fall below the MIF, by duration in self-employment⁸⁶

| All self-employed workers | Workers who have been self-employed for 1+ year | Workers who have been self-employed for 2+ years |
|---------------------------|---|--|
| 42.1% | 32.1% | 25.5% |

While some will see their benefit entitlements diminish, others may struggle to be classified as self-employed in the first place. There are several benefits of having a Gateway Interview that determines whether people are gainfully self-employed, not least that it will give workers some assurance of their employment rights and tax status. However, it is still unclear as to whether JCP advisers are the best people to undertake these assessments. JCP offices tend to focus on helping people into typical employment, and as such their advisors will not necessarily have the expertise to determine, for instance, whether a claimant’s business plan is feasible. Another cause for concern is that a good number of self-employed workers may lack the numerical and IT skills to submit their financial information to the authorities online every month – a particular issue for migrants, people in rural areas with limited internet access, and those lacking formal education. The campaigning group GO:ON UK estimate that one in five adults still do not have basic online skills, while the National Numeracy charity says there are 17 million adults with numeracy skills below that needed for the lowest GCSE grade.⁸⁷

None of this is to say that UC will be wholly detrimental to the self-employed. The RSA backs the underlying principles of this new welfare programme, and believes that it is right to encourage people to grow their business in pursuit of profit. However, there are clearly several changes that need to be made before we can be confident that UC will have a positive impact. The government has already taken several steps in this regard, for example by considering the possibility of allowing people to ‘carry over’ losses from month to month. But we believe further progress could be made before the self-employed are transitioned onto UC. Our first proposal is that the Start-up Period be extended from 12 to 24 months,

There are clearly several changes that need to be made before we can be confident that UC will have a positive impact

86. RSA analysis of Understanding Society Survey data (Wave 1 = 2009/10, Wave 2 = 2010/11, and Wave 3 = 2011/12).

87. For more information see www.go-on.co.uk/opportunity/ and www.nationalnumeracy.org.uk/what-is-the-issue/index.html

given that it often takes longer than a year for new business owners to earn the equivalent of the minimum wage. Based on data from the Understanding Society Survey, we calculate that extending the Start-up Period to 24 months would reduce the proportion of workers below the MIF from 32 percent to 26 percent (see Table 8). Put another way, it would mean lifting almost 300,000 self-employed workers above the floor.

Another suggestion is to establish 'Grace Vouchers', which the self-employed could cash-in for a temporary month's exemption from the MIF. As discussed, the nature of monthly reporting under UC means that self-employed claimants with significant fluctuations in income may be worse off than under the old annualised system. The current government proposal to allow the self-employed to carry over losses from month to month may alleviate the problem for some, but certainly not everyone.⁸⁸ An additional response would be to allow the self-employed to take themselves out of the MIF rules entirely for a short period when faced with extenuating circumstances, whether that is a fruit picker dealing with a particularly bad harvest or a taxi driver whose vehicle is temporarily out of action. Grace Vouchers could be accumulated over time and awarded to those who surpass the MIF on a regular basis, thereby ensuring that only genuine business owners are able to use them. Another idea is to provide a set quota of these Vouchers to the self-employed who work in seasonal industries such as farming or fishery, given the inevitable income fluctuations they will face.

Box 10: Could Universal Credit be personalised?

It is expected that hundreds of thousands of self-employed people will eventually be in receipt of Universal Credit. Given that each of these will have different abilities and needs, there is an argument for introducing an element of personalisation into the UC system. For example, claimants could be allocated different Start-up Period lengths dependent on how long it is likely to take them to create a viable business. An experienced individual with previous experience of self-employment may only need six months, whereas a younger claimant entirely new to the world of business could require 18 months. Such a tailored approach could result in higher business survival rates and even lower costs. However, it demands that the advisers making the decisions are well informed about the individuals concerned, and knowledgeable about business matters more generally.

A third proposal is to transfer responsibility for the Gateway Interviews from JCP staff to New Enterprise Allowance advisers. The latter group are solely focused on helping people into business and will therefore have a better sense of whether or not somebody should be classed as gainfully self-employed. This would entail extra cost but it

88. The advantage of being able to 'carry forward' losses is that the self-employed with volatile incomes may be able to claim UC in the few periods where their income is very high, as the inclusion of losses will bring down their income below the necessary threshold. However, some self-employed claimants may face many months of losses before they receive a windfall (think of seasonal staff such as agricultural workers). If they have to rely on minimal amounts of UC throughout this period, it may result in them having to close their business before they can benefit from the carry forward.

is also likely that the NEA advisers will impart valuable guidance as part of the interviews (the NEA will be discussed in more detail in the next chapter). Finally, we advocate that Post Office branches be turned into Universal Credit portals. In practice this could mean setting up computers in branches to allow people to interact with the UC system, or simply informing subpostmasters about how UC works, such that they can pass on advice to their customers. It is understood that the DWP have already earmarked JCP branches to provide such a role, but these offices are not always within reach of claimants. In contrast, around 95 percent of the population live within a mile of a Post Office, and many subpostmasters already dispense advice about benefits.⁸⁹

R8 – Redesign Universal Credit so that it reflects the reality of self-employed work

As it stands, Universal Credit could leave the self-employed worse off than under the current welfare system, particularly those on the lowest incomes. Several adjustments should be made before the self-employed are transitioned onto this new programme:

- Extend the Start-up Period from 12 to 24 months.
- Establish 'Grace Vouchers' that can be used for a temporary MIF exemption.
- Transfer responsibility for Gateway Interviews from JCP staff to NEA advisers.
- Turn Post Office branches into Universal Credit portals.

Even were the government to enact all the changes we suggest, there is no guarantee they would be fully protected from the income shocks detailed in the last chapter

Harnessing the crowd

So far we have discussed how the welfare state – in its present and future forms – might improve the way it treats self-employed workers. However, even were the government to enact all the changes we suggest, there is no guarantee they would be fully protected from the income shocks detailed in the last chapter. This is because the welfare state was only designed to be a 'safety net' providing basic support. As such, we need to consider whether the self-employed can pool risks in other ways, for example by forming collective agreements among themselves. One option would be for the self-employed to band together under a group insurance scheme that delivers income protection (IP) to its members. There are no available figures for the number of self-employed workers signed up to a private IP scheme, yet the insurance experts we spoke with believe that participation rates are very low. Part of the reason is because premiums are prohibitively expensive, particularly for older workers and those operating in dangerous industries. A leading insurer gave us a quote of £29 a month to cover a 30-year-old web developer, but £115 a month to cover a 50-year-old builder.⁹⁰

One reason why premiums are costly is that there are multiple insurance firms, each of which have a relatively small group of clients and therefore high administrative costs. In contrast, a collective insurance

89. Dellot, B. (2014) *Making the Connection*. London: RSA.

90. For more details see www.rsablogs.org.uk/2014/enterprise/time-collective-insurance-scheme-selfemployed.

scheme that brought the self-employed together under one umbrella would amass a large enough pool of insurance recipients to deliver economies of scale. While this should be an independent initiative run by the private sector, possibly in the mould of the Nest pension scheme, the government could act as the orchestrator. Indeed, it may be that the only way for the scheme to work in practice is if it were made compulsory, as otherwise only the most at-risk groups would join, with the effect of keeping premium costs prohibitively expensive. To make participation in this programme less costly for the self-employed, one option would be for the government to channel some of the extra revenue generated through the NICs reform into the collective insurance pot.

R9 – Back the development of a collective income protection (IP) insurance scheme

The government should help to establish a collective income protection insurance scheme that would support the self-employed during periods of long-term sickness. This should be run by private sector organisations experienced in delivering insurance products, and could be partly funded using a portion of the extra revenue generated through the NICs reform.

While a collective insurance scheme would clearly benefit from the involvement of the government, there are other ways for the self-employed to spread risks that are independent of the state. A good example is co-operatives like the French-based BEC, which organises its members to support one another as they grow their fledgling businesses. Once established, the members become ‘salaried employees’ who contribute 10 percent of their sales to the co-operative in return for legal, book-keeping and insurance support.⁹¹

Yet the self-employed do not necessarily have to be sewn together through tight legal arrangements. A less demanding approach is to remain a distinct entity but to pool finances with others. In Belgium, a non-profit organisation called the Societe Mutuelle pour Artistes (SMart) works on behalf of its self-employed members to process their invoices and chase payments.⁹² One of its key features is that it pools income in a mutual guarantee fund, meaning that members can be paid immediately when they hand over their invoices to the SMart team. Our recommendation is that business support organisations in the UK work together to explore whether there is scope to establish a similar cash-pooling scheme here, possibly run by a new social enterprise that would charge a nominal fee per invoice processed.

91. For more information see www.eurofound.europa.eu/observatories/eurwork/case-studies/attractive-workplace-for-all/coopaname-france-business-creation-and-entrepreneurship

92. Highlighted by Joel Dullroy, Editor of Independents Unite! Dullroy, J. (2015) *Freelancers unite to get sickness and other employment benefits* [article] The Guardian: 14th January 2015.

R10 – Explore the potential for creating a social enterprise with a ‘cash-pooling’ service

Business support organisations such as the Federation of Small Businesses, the Forum for Private Businesses and Enterprise Nation should work together to consider the appetite and potential for establishing a new social enterprise that pools the finances of small business owners. The aim would be for this to limit the detrimental impact of late payments.

Minimising risks

In the previous two chapters we looked at how the self-employed might be able to cope with risks, principally by dealing with the fallout of income shocks. We examined, for example, how savings, collective insurance and the welfare state might cushion the blow of an illness, accident or market dip. In this section we turn our attention to how the self-employed might minimise risks *ex ante*. In the short-term this means preventing mishaps from occurring (eg through adequate health and safety measures), while in the long-term it means increasing the earnings potential of the self-employed by boosting their ‘capital’: **personal** (mental and physical health), **human** (skills and knowledge) and **social** (relationships).

Boosting occupational health

Let us begin by considering how the self-employed can preserve and improve their mental and physical health. Looking first at the former, we might expect the self-employed to experience on average higher levels of stress and depression, given their responsibilities. However, the evidence for this is patchy, with multiple studies revealing different findings. Some academic papers show that self-employed workers are more prone to feeling ‘burned-out’,⁹³ yet the UK’s own Health and Safety Executive (HSE) reports that the self-employed actually experience less stress, anxiety and depression than their counterparts in typical jobs.⁹⁴ The Labour Force Survey echoes this finding, showing that only 2.8 percent of people who work for themselves suffer from depression, a marginally lower rate than among employees.⁹⁵ What most parties do agree on, however, is that the self-employed are more likely to feel isolated, possibly because most work from home and have no employees or colleagues to interact with (an issue we pick up on later in this chapter).⁹⁶

With regards to physical health, the self-employed appear more likely to be afflicted by a number of conditions. For example, data from the Labour Force Survey shows that 6.2 percent of self-employed workers say they suffer from back problems, compared with 4.3 percent of employees.⁹⁷ Moreover, the rate of work-related fatalities in the self-employed community is twice that seen among conventional workers.⁹⁸ A concerning finding from the 2010 European Working Conditions

6.2 percent of self-employed workers say they suffer from back problems, compared with 4.3 percent of employees

93. See for example Jamal, M. (1997) ‘Job stress, satisfaction and mental health’ in *Journal of Small Business Management*, 35(4); and Benavides, F. G. et al. (2000) ‘How do types of employment relate to health indicators?’ in *Journal Epidemiology Community Health*, 54.

94. Health and Safety Executive (2014) *Stress-related and Psychological Disorders in Great Britain 2014*. HSE.

95. RSA analysis of Jul–Sep 2014 Labour Force Survey.

96. BIS (2013) *Op cit*.

97. RSA analysis of Jul–Sep 2014 Labour Force Survey.

98. Health and Safety Executive (2013) *Annual statistics report for Great Britain*. HSE.

Survey was that 28 percent of the self-employed believed their health and safety was at risk due to their work.⁹⁹ Part of the problem is that the self-employed – whether plumbers, taxi drivers or gardeners – are more likely to operate in poorly equipped work environments, with no human resources team to oversee their wellbeing. By law, every self-employed person must undertake a risk-assessment to see if their work poses a danger to themselves and others, but this is not checked nor verified by a third party. A study by the Health and Safety Executive also reveals that small business owners typically have a poor understanding of legislation on occupational health, and tend to operate in a fire-fighting mode whereby they deal with issues only as and when they arise.¹⁰⁰

In a bid to boost occupational health, large businesses often choose to bring in outside consultants to advise them on how to improve their physical environment and working patterns. Such is the demand for these services that NHS hospitals have created their own ‘Health at Work’ teams, which charge local businesses for guidance. Yet this kind of support is likely to be too expensive for many self-employed people, particularly the large number earning below the minimum wage. One cost-effective alternative would be to identify ‘anchor institutions’ in local areas, such as FE colleges, large businesses or housing associations, some of whom may be able and willing to freely share their excess resources with the surrounding self-employed community. In practice this might involve them offering spare places at internal health and safety courses, or setting aside time for their team to make workplace health and safety visits. At the most basic level, it could simply mean businesses sharing their written materials. Given its track record and existing connections, a charitable body like Business in the Community would be the ideal facilitator of such a scheme.

R11 – Identify ‘anchor institutions’ that can provide occupational health advice to the surrounding self-employed community

Business in the Community should work with local authorities to identify housing associations, FE colleges and other large organisations that would be willing to share health and safety knowledge with local self-employed people. This could range from conducting workplace visits to disseminating useful materials.

As well as introducing more robust health and safety measures, another way to boost occupational health is to respond to illnesses with rapid treatment – in other words, to nip problems in the bud. This is the government’s rationale for introducing the new ‘Fit for Work’ service, which will help people who have been off sick for more than 4 weeks to return to employment. The service has two key features: an advice line to offer guidance, and a face-to-face assessment with an occupational health professional. However, while employees have access to both

99. European Employment Observatory Review (2010) Op cit.

100. Health and Safety Executive (2000) *Occupational health advisory committee report and recommendations on improving access to occupational health support*. HSE.

these components, as it stands the self-employed are only entitled to the advice line. Putting issues of equal treatment to one side, there is a compelling business case for fully opening up the Fit for Work service to the self-employed, not least because helping them back into work would boost tax receipts and minimise the chances of them becoming dependent on ESA. Approximately £1bn in earnings is already lost every year as a result of sickness absence among the self-employed.¹⁰¹

R12 – Fully open up the new Fit for Work service to the self-employed

The government should allow the self-employed to access the face-to-face assessment component of the new Fit for Work service, as well as the advice line. This would reduce the number of self-employed people who are off work with sickness for long periods.

To focus only on the challenges would be to ignore the opportunities that self-employment provides for those looking to manage existing health conditions

The impression one is left with is of a workforce that is more vulnerable to falling ill and being prey to accidents, hence the need for new interventions. However, to focus only on the challenges would be to ignore the opportunities that self-employment provides for those looking to manage existing health conditions. Perhaps the most striking finding from our RSA/Populus survey was that 54 percent of our respondents thought being self-employed was important in helping them to work around their physical health problems.¹⁰² A study by the Work Foundation found that self-employment is particularly attractive to people with musculoskeletal disorders, in part because it gives them more freedom to determine when and where they work.¹⁰³ Indeed, self-employment may become increasingly important for disabled people as tougher benefit eligibility criteria mean they are forced to look for work.

Self-employment may also be an ideal form of work for those suffering from a mental illness. Polling undertaken by the Depression Alliance found that one in three people have found it hard to cope at work because of depression, stress or burnout, while a study by the DWP concluded that employers do not always respond well to people's disclosures of mental illness.¹⁰⁴ The result is that it is common for workers with a mental health condition to find themselves poorly paid or employed in roles that do not reflect their full talents.¹⁰⁵ It is therefore not surprising that many decide to strike out on their own, partly in a bid to accommodate their fluctuating health but also with the wider goal of realising their potential. According to the Priory Group, over 90 percent of their clients awaiting a mental health diagnosis felt that the stigma around mental health would lead them, or has led them, to consider self-employment.¹⁰⁶

101. Black, C. and Frost, D. (2011) *Health at work: An independent review of sickness absence*.

102. Dellot, B. (2014) Op cit.

103. Summers, K., Bajorek, Z. and Bevan, S. (2014) *Self-management of chronic musculoskeletal disorders and employment*. London: Work Foundation.

104. Irvine, A. (2008) *Managing mental health and employment*. London: DWP; and Depression Alliance (2014) One in three people struggle to cope at work [Press release].

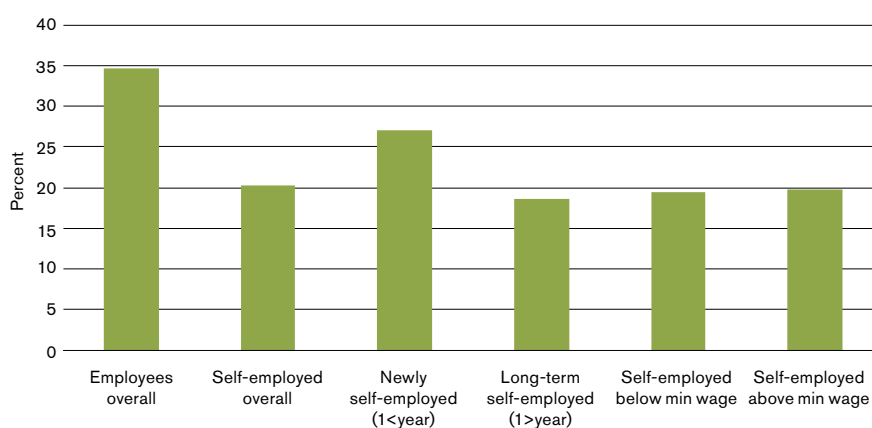
105. Lelliott, P. et al. (2008) *Mental health at work*. Royal College of Psychiatrists.

106. For more information see www.news.mitrefinch.co.uk/article.aspx?art_id=801741326

Improving access to training

If occupational health services can serve to boost mental and physical wellbeing, then training is the primary means through which to develop human capital – that is, skills and knowledge. A substantial body of evidence shows that self-employed people who have taken part in training are more likely to run a business that turns a profit.¹⁰⁷ The concern, however, is that many people who work for themselves lack exposure to personal development opportunities. Our analysis of the Labour Force Survey shows that 8 percent of the self-employed have no qualifications whatsoever, compared with 5 percent of employees.¹⁰⁸ Similarly, the Understanding Society Survey reveals that self-employed workers are almost half as likely as employees to have had access to training in the past 12 months (see Figure 10). Limited engagement with training may be one reason why, according to the UK Commission for Employment and Skills (UKCES), large numbers of self-employed people lack a good understanding of basic business practices, including marketing, management systems and cash flow.¹⁰⁹ Those who do not take part in training will also find it difficult to maintain the technical skills that are necessary for operating in their industry – whether that is carpentry, hairdressing or construction.

Figure 10: Access to training in the past year by working status



Source: RSA analysis of Understanding Society Survey 2011/12 (Wave 3)

There is a belief among some that the absence of formal training is not a major concern, since it is compensated by subtle skills development that happens on a day-to-day basis. The argument runs that people who work for themselves are exposed to more aspects of a business, which allows them to develop and hone a wider range of skills. Indeed, it is common for self-employed people to be engaged in a wide range of business activities. They must not only create a product or service but also liaise with customers, find suppliers, oversee marketing and manage their books. A related point is that the self-employed may be

107. See for example UKCES (2011) *Skills for self-employment*. London: UKCES.

108. RSA analysis of Jul–Sep 2014 Labour Force Survey.

109. UKCES (2011) Op cit.

It would be naïve to think of informal learning as a panacea for the self-employed

better placed to utilise their existing skills, since they direct the content of their work and can often choose to do tasks that align with their expertise.¹¹⁰ While these arguments present a compelling case for the importance of informal learning, it would be naïve to think of it as a panacea for the self-employed. One major issue is that informal learning does not result in qualifications, which may be necessary if workers eventually want to move into the more structured world of paid employment.

Our primary concern, then, is how to improve people's access to formal training. There are potentially several reasons why take-up among the self-employed is relatively low. One of these relates to the costs involved, with self-employed people either unable to afford the training or to lose business from taking time off work. The conventional policy response to this challenge has been to subsidise training costs, primarily through tax relief. Yet as was highlighted in a recent report by Demos, it is only possible to claim relief on training that develops an existing skill, rather than one in a new area.¹¹¹ This means that many who wish to diversify their service offer, or to switch careers entirely, are at a disadvantage.¹¹² We therefore back the call for businesses to be able to claim tax relief on more types of training. However, as is the case in France, the government should consider reserving the most generous tax relief for those who engage in training that takes place year after year. The rationale is that this would encourage sustained skills development rather than participation in a one-off course, usually at the start of a career. Indeed, the ambition should be to bring the training rates of the long-term self-employed in line with those of the newly self-employed, which is substantially higher (see Figure 10).

R13 – Review tax-relief to support a wider breadth of sustained training

The government should consider allowing the self-employed to gain tax relief on training that develops a new skill, not just an existing one. It should also look at how the tax relief system could be used to support training that takes place year after year.

Another issue is that self-employed workers do not always recognise the need for training when it exists. The government's Small Business Survey found that only 17 percent of non-employing business owners believed that a lack of skills was a problem for their business, compared with 20 percent who cited the suitability of their premises.¹¹³ A skills shortage may not be a problem for some, but it is surprising that so few recognise the need for further personal development. Part of the reason is that many self-employed people do not see themselves as

110. Baumberg, B. and Meager, N. (forthcoming, 2015) "Job quality and the self-employed: is it still better to work for yourself?" in Felstead, A, Gallie D. and Green, F. (eds.) *Unequal Britain at Work: The Evolution and Distribution of Intrinsic Job Quality in Britain*, Oxford: Oxford University Press.

111. O'Leary, D. (2014) *Going it Alone*. London: Demos.

112. Although we should acknowledge that tax relief would make no difference to low-income self-employed people who earn below the Income Tax threshold.

113. BIS (2013) *Op cit*.

‘business owners’, and therefore fail to grasp the importance of having business management skills.¹¹⁴ However, lacklustre demand may also be a result of poor marketing on behalf of training providers, with the self-employed bewildered at the array of options available to them and unsure of where to begin.¹¹⁵ A recent study by the Federation of Small Businesses identified 891 government-led support programmes in place.¹¹⁶ This has led the Small Business Minister Matt Hancock to call for publicly funded support schemes to be “streamlined” or even terminated, and Labour to promise the establishment of a ‘Small Business Administration’ that would take charge of co-ordinating business support efforts.

While both these proposals are admirable, there is only so much that the government and its bodies can do to steer the provision of training – not least because there is substantial private sector involvement. This points to the need for an independent organisation that could curate and collate information about different training programmes. Rather than establish a new body, however, we recommend that the BBC be nominated to use the resources at its disposal to create a MyBusiness portal.¹¹⁷ This would bring together training content from across the web, including links to the growing number of Massive Open Online Courses (MOOCs). The BBC could also work with the Sector Skills Councils to display information about skills and training courses that are relevant to specific industries, whether that is in catering, social care or the creative sector. There is also a strong argument for establishing interactive forums where the self-employed can share ideas and advice, just as business owners do on platforms like Etsy and LinkedIn.¹¹⁸ The rationale for nominating the BBC for this role is that it already has a remit to ‘inform and educate’, has significant resources at its disposal, and appeals to people from across the spectrum, including low-income groups.

R14 – Work with the BBC to establish a MyBusiness portal for training information

The BBC should consider creating a MyBusiness portal that collates and curates information about training – both the general business management kind and that related to specific industries. The BBC is the ideal organisation to run such a portal due to its unparalleled reputation, reach and resources. It also has a clear remit to ‘inform and educate’.

114. UKCES (2011) Op cit.

115. This may be one reason why less than 15 percent of the funding available through the Growth Vouchers scheme has been taken up by businesses. Growth Vouchers is a government scheme that subsidises the costs of training for people wishing to grow their business. For more information see Goodfellow, C. (2015) *Exclusive: Only 10% of government Growth Voucher funding used with six weeks until deadline* [article] BusinessZone, 8th February 2015.

116. Federation of Small Businesses (2013) *Enterprise 2050: Getting UK enterprise policy right*. London: FSB.

117. A similar idea was floated by Rohan Silva at the RSA’s 2015 Self-employment Summit.

118. For more information about how online platforms like Etsy encourage collaboration, see Dellot, B. (2014) *Breaking the Mould*. London: RSA. The value of online forums was revealed only recently when business owners used them to spread news of the VAT MOSS changes, as well as to mobilise to take action against it.

Box 11: Accreditation in a digital age – licences or open badges?

While training is valuable in its own right, another reason why people engage in learning is to acquire accreditation that can demonstrate their credentials to potential customers. This begs the question of whether we should introduce licences for more occupations, such that self-employed workers (and employees) would need to up-skill before they could begin trading. However, such a move may inadvertently serve to punish low-income groups that cannot afford the licencing tests, to say nothing of the potential price hike it may create for consumers.¹¹⁹ Another way of helping workers to demonstrate their skills would be to support the spread of 'open badges', which are awarded by peer-verified individuals or institutions. Although principally designed to convey people's participation in online learning, badges can also be used to show the skills and knowledge developed through traditional routes - whether that be schools, the workplace or community schemes. An upcoming RSA report will call for a series of 'Cities of Learning' pilots, which would seek to promote existing open badge schemes that are embedded in local learning activities.¹²⁰

Bolstering employment services

While training can boost the human capital of existing business owners, employment services are vital for improving the prospects of the newly self-employed transitioning from unemployment. The Resolution Foundation estimates that movements from unemployment into self-employment accounted for around a quarter of the overall growth in self-employment during the economic downturn.¹²¹ There are presently two main sources of support for unemployed people that wish to work for themselves: the New Enterprise Allowance (NEA) and the Work Programme. The former provides people with an allowance of up to £1,274 over six months, as well as mentor support and the opportunity of a loan. It is open to any adult on JSA, ESA and Income Support, providing they have a feasible business plan. Whereas the NEA is only concerned with helping people into self-employment, the Work Programme is a much larger government initiative aimed at enabling people to find sustained work of any kind, and it is targeted specifically at the long-term unemployed. The self-employment support offered through the Work Programme varies from provider to provider, since each has the freedom to determine the type of activities they offer to their clients.

The effectiveness of both these initiatives is difficult to determine, in part because they are still relatively new and in part because there is little publicly available data on client outcomes.¹²² However, the small amount of data that is available suggests there may be room for improvement. The NEA, for example, has struggled to retain

119. The problems of licensing were examined in an interesting US study on the Uber taxi service (n.b. the report was funded by Uber, although the authors stress their independence). See Hall, J. V. and Krueger, A. B. (2015) *An analysis of the labour market for Uber's driver-partners in the United States*.

120. Painter, A. and Bamfield, L. (Forthcoming) *Democratic Digital: Social mobility rich or inequality poor technological change*. RSA: London.

121. D'Arcy, C. and Gardiner, L. (2014) Op cit.

122. A concerning response to our Freedom of Information (FoI) request was that the government does not hold (and therefore presumably does not collect) outcome data from NEA private providers.

Both the NEA and Work Programme contain several flaws in their design that mean people are not adequately supported

people who enrol on the scheme. Only 42,000 of the 83,000 people who signed up to the NEA between 2011 and the end of 2013 made it past the initial business planning phase.¹²³ Likewise, according to the best estimate from the Employment Related Services Association (ERSA), only 10 percent of job outcomes under the Work Programme have been in self-employment (despite reports that some clients have been irresponsibly encouraged to start up in business). It is reasonable to expect this figure to be much higher, not least because the Work Programme began operation during the recessionary period when 90 percent of all jobs growth was owed to self-employment.

The poor outcomes of these initiatives may simply be due to a lack of enthusiasm for self-employment among those who are out of work. A more likely explanation, however, is that both the NEA and Work Programme contain several flaws in their design that mean people are not adequately supported. One possible reason for the low take-up rate of the NEA is that the money claimants receive is around a third less than the typical amount given to people on Jobseeker's Allowance, thereby creating a disincentive to join the scheme.¹²⁴ Another problem is that the Allowance is abruptly cut in half from £65 to £33 a week midway through the programme. There are also concerns that Jobcentre Plus staff are failing to bring the option of the NEA to the attention of unemployed clients with business potential, either because they are not aware of the NEA themselves or because they have taken a wrong judgement call that the individual is not suitable for self-employment.¹²⁵ Each of these challenges can be addressed through relatively simple tweaks, including by tapering the reduction in the NEA allowance and having a named self-employment adviser in every JCP branch.

R15 – Address the design flaws in the New Enterprise Allowance

The NEA could be improved through relatively simple changes, which would both encourage people to sign up to the scheme and ensure they stay the course:

- Put the value of the NEA payment on a par with Jobseeker's Allowance.
- Reduce the value of the payment gradually, rather than halving it after 13 weeks.
- Ensure every JCP office has a named Self-employment Adviser (SEA) who can raise awareness of the NEA among other advisers.

With regards to the Work Programme, the main issue is that not all of the providers offer a specific support component for people who want to move into self-employment. An investigation by the All Party Parliamentary Group on microbusinesses found that only half of contractors in the Work Programme offer specific advice and guidance

123. These figures were given to the authors by a civil servant in the DWP during a phone call in Feb 2015.

124. Over 25s receive £72.40 a week on JSA. NEA claimants receive £1,274 over 26 weeks, which equates to £49 every week on average.

125. DWP (2013) *New Enterprise Allowance: Qualitative evaluation*. London: DWP.

on self-employment.¹²⁶ The result is a postcode lottery, with the long-term unemployed in different parts of the country receiving different amounts of support. Another drawback is that participants taking part in the Work Programme are not entitled to the same period of ‘test trading’ as NEA participants, meaning that when they move into self-employment they face losing their out-of-work benefits. Again, however, these shortcomings are relatively simple to address. For example, when the Work Programme contracts are renewed in 2016, the government could mandate that applicants must set out how they plan to assist people into self-employment. Of course, this goes against the ‘black box’ model of the Work Programme, which gives providers free rein to determine their service offer. Yet it is difficult to justify why a postcode lottery of support should continue. In the spirit of equal treatment, the government could also ensure that participants in the Work Programme are able to claim the same allowance as NEA participants.

R16 – Introduce equal treatment under the Work Programme

The government should consider mandating that every Work Programme provider offer specific support to people who want to move into self-employment, so as to end the current postcode lottery. In the interests of fairness, the government should also look at whether Work Programme participants could be awarded the same allowance that is open to NEA claimants.

Making the aforementioned tweaks to the NEA and Work Programme would go a long way towards improving the prospects of people moving from unemployment into self-employment. However, it is worth considering whether there needs to be a more fundamental overhaul of employment services, such that there is a single stream of support for people who wish to work for themselves. As Avanta and others have suggested, this could mean creating a more comprehensive version of NEA, which would be made available across the country and delivered by trained business support advisers. Unlike existing initiatives, the service would not only help people to move into self-employment but also sustain their business over the long run, possibly linked to the BBC’s MyBusiness portal (see above). This would of course come with cost implications, but the service could be positioned as an important complement to Universal Credit, which will encourage in-work benefit claimants to grow their business in a short period of time.

The service could also make it a priority to help business owners operating in the informal economy to move into legitimate self-employment. At present, employment services do little to reach out to informal traders, despite the fact that many wish to move away from cash-in-hand work.¹²⁷ A previous RSA/YouGov poll found that one in five business owners had

¹²⁶. All Party Parliamentary Group on Microbusinesses (2013) *Microbusinesses and the Work Programme*.

¹²⁷. Barbour, A. and Llanes, M. (2013) *Supporting people to legitimise their informal businesses*. London: JRF.

traded informally at some point in the past, but that the vast majority saw this as a temporary solution to getting their business off the ground.¹²⁸

R17 – Establish a universal self-employment service to help people start, sustain and formalise a business

A long term objective should be to create a single employment service that is dedicated to helping people move into self-employment. Unlike the NEA, this would enable people not only to start a business but also to sustain their venture. Another feature would be to help informal traders transition into the legitimate world of business.

Joseph Schumpeter, the founding father of the entrepreneurial movement, used the term Socialökonomik to describe how the spheres of business and society are inseparable

Expanding social networks

While the benefits of human capital and personal capital are largely self-explanatory, the advantages of social capital require more unpacking. This is because entrepreneurship is often viewed as an individual pursuit, rather than one built on the minds and resources of many. The reality is that self-employed people rely heavily on others to progress and grow their business. Indeed, Joseph Schumpeter, the founding father of the entrepreneurial movement, used the term Socialökonomik to describe how the spheres of business and society are inseparable. Family members, for example, are frequently the first port of call for start-up capital, particularly for people from poorer backgrounds.¹²⁹ We also know that being plugged into networks increases people's exposure to business opportunities, whether that is finding a more reliable supplier or identifying a lucrative customer. Moreover, relationships can be a source of emotional support, which is often invaluable for those whose business is entering a rough patch. Taken together, it is therefore unsurprising that effective networking has been linked with better firm performance.¹³⁰

The problem is that self-employed people are immediately disadvantaged in their access to social capital. Unlike employees, they do not have the luxury of relying on the ready-made relationships that are embedded within a traditional workplace. Moreover, the fact that 70 percent of the self-employed work from home means they are less able to forge useful connections with others.¹³¹ The challenge is particularly acute for low-income groups, whose networks tend to be less extensive and rewarding than those from more affluent backgrounds. Several research studies have shown that business owners from 'higher social classes' are not only tapped into richer networks, but also have the skills and time to extract value from them.¹³² To some extent, internet-based platforms such as LinkedIn and Mumsnet offer a route for people to connect with others. However, it is unclear whether online relationships are as fruitful

128. Dellot, B. (2012) *Untapped Enterprise*. London: RSA.

129. Baines, S., Wheelock, J. and Gelder, U. (2003) *Riding the roller coast: Family life and self-employment*. JRF.

130. See for example Dodd, S. D. (2007) 'Mumpsimus and the Mything of the Individualistic Entrepreneur' in *International Small Business Journal*, 25(4).

131. BIS (2013) Op cit.

132. Jayawarna, D., Rouse, J. and Macpherson, A. (2009) *Life Course Pathways to Entrepreneurship*.

as face-to-face ones.¹³³ Business owners also have the option of attending professional networking events – the best example being those run by Chambers of Commerce – yet these are often time intensive.

Our favoured solution – and one we have advocated for in previous reports – is to establish a randomised matchmaking service. Anyone taking part would be connected with a different business owner every few weeks, and encouraged to meet face-to-face to share information and advice. This scheme is currently in operation at the RSA and Nesta, the latter having described it as ‘institutionalised serendipity’.¹³⁴ The main advantage is that it addresses the problem of ‘homophily’, whereby people tend to float towards likeminded others, thereby limiting the chance of them being challenged or hearing about novel information. Another benefit to the matchmaking service is that it would help people to forge multiple ‘weak ties’, rather than a handful of strong ones. As the sociologist Mark Granovetter has shown, it can often be better to have a large number of fleeting connections, as this will increase people’s exposure to new ideas and insights rather than redundant information.¹³⁵ Given the place-based nature of the service, it would make sense for local authorities to take on the role of developing such a scheme. However, our vision is of a system that largely runs of its own accord, with business owners taking on the responsibility to meet once they have been matched (albeit with safety procedures in place).

R18 – Develop a randomised matchmaking service to connect self-employed people in a given area

Local authorities should consider creating a scheme that randomly matches business owners in their locality, such that participants meet with a different person on a regular basis. The aim would be to expand their social network and expose them to new ideas and insights.

¹³³. A study by the What Works Centre for Local Economic Growth found that business support programmes using a hands-on approach may perform better than those using a light-touch delivery model, such as providing advice through a website. Note, however, that this conclusion is based on only one direct comparison study and ignores the question of cost-effectiveness.

¹³⁴. For more information about Nesta’s experience, see www.nesta.org.uk/blog/institutionalising-serendipity-productive-coffee-breaks

¹³⁵. Granovetter, M. (1973) ‘The strength of weak ties’ in *American Journal of Sociology*, 78(6).

Taking self-employment seriously

We began this report by asking whether the self-employed represent a newkind of precariat, as is often thought to be the case. The simple answer is no: a wealth of evidence shows that they tend to be more satisfied with their work, as well as with their lives overall. Yet it would be wrong to dismiss the significant hazards that face people who work for themselves. One of the fundamental issues for the self-employed is that the burden of dealing with risks largely falls to them alone. They have no recourse to sick pay should they fall ill, nor to maternity pay if they become pregnant. Moreover, their income in general is often more volatile, with highs and lows that mirror the state of the market. However, to focus only on income fluctuations would be to ignore the large number of self-employed people who experience persistently low levels of income year-in, year-out. While our research reveals considerable contention regarding the financial health of the self-employed, the Family Resources Survey clearly shows that the median earnings of people who work for themselves full-time are 25 percent lower than their counterparts in wage work.

Any efforts to improve the living standards of the self-employed must therefore make it a priority to address risks and mollify their impact, as well as to improve the general earnings potential of the self-employed. In this report we suggest a three-pronged approach: managing, spreading, and minimising risks. The first method refers to how the self-employed can deal with the fallout of unexpected events on their own, for example by building up a rainy-day savings fund or swiftly changing their spending patterns to minimise outgoings. The second approach describes how the self-employed can cope with risks by sharing them with others. Perhaps the best way of achieving this is through the welfare system, and as such we propose that the government consider extending more social security protections to the self-employed (albeit with the request that they pay higher taxes). However, risk could also be distributed through non-state initiatives, such as a collective insurance scheme or cash-pooling service. Finally, by minimising risks we mean preventing mishaps from occurring in the first place, as well as improving the general earnings potential of the self-employed – whether through occupational health interventions or training.

The reader may wonder why we should treat the self-employed any differently today, when they have always been a contingent in the workforce. The simple answer is that the composition of this community

has changed considerably in recent years, with new entrants that are arguably more vulnerable than the traditional cohort. The perils and pitfalls highlighted in this report were easier to overlook when the self-employed only formed a small proportion of the workforce and when business owners were typically affluent. Yet the self-employed now make up 15 percent of the workforce (up from 8 percent in 1980), and their numbers have been swelled by different groups that may require more support, such as young people, women and migrants. Indeed, one of the central messages of this paper is that self-employment should no longer be seen as a fringe pursuit, but rather as a mainstream form of employment. In short, we need to begin taking self-employment seriously.

Our recommendations are put forward in this spirit. While some constitute minor policy tweaks and others more fundamental changes, behind every proposal is a recognition that the self-employed have both **rights and responsibilities**. A right, for example, to greater welfare coverage such as a boost to their maternity and paternity pay. But an equally important responsibility to pay higher National Insurance rates to finance such protection. As a result, not all of our recommendations will prove immediately popular with the self-employed community, and they may even encourage people to look for more conventional work as a result of their implementation. Yet it is important to remember that they are all geared towards boosting the living standards of the self-employed in the long-run, in particular the lowest earners. Indeed, throughout this paper we have tried not to lose sight of our fundamental aim: that of enabling people to take part in *meaningful* self-employment, which enables them to flourish as creative individuals.

Over the coming months we will endeavour to progress with this mission by refining and unpacking our recommendations. In practice this will mean gauging the appetite for our ideas among the self-employed, as well as undertaking a rigorous cost-benefit analysis of their expected impact. What will people think of a compulsory question for pension enrolment? Would the self-employed want to participate in a collective insurance scheme? And how much would it cost to extend Statutory Maternity Pay to the self-employed? These are just some of the questions we hope to answer in future work.

If you would like to contribute your expertise or ideas to this process, please do get in touch with us.

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Throughout this paper we have tried not to lose sight of our fundamental aim: that of enabling people to take part in meaningful self-employment

Appendix

Box 12: Demographic spotlight

Our research indicates that certain demographic groups score better than others on key indicators of living standards. Note that these patterns may also be reflected among employees.

- **Earnings** – The self-employed across all age groups saw their real median weekly earnings decline between 2000 and 2011, bar the over 55s.¹³⁶ The fall was particularly acute for 45–54 year-olds, whose earnings shrank by 40 percent in that period. It is also worth noting that self-employed women earn just over half that of their male counterparts.
- **Poverty** – Overall, a third of self-employed-only households are in poverty.¹³⁷ However, the figure is closer to 60 percent for Asian, Pakistani and Bangladeshi households where all the earners are self-employed. In terms of age, the data suggests that a large proportion of the under 25s are below the poverty line, however this may be a skewed result borne out of an inadequate sample size.
- **Pensions** – Only 11 percent of Black / Black British self-employed people are currently contributing to a private pension, and only 17 percent of Asian / Asian British self-employed people.¹³⁸ This compares with a third of all self-employed workers. There is also a sizeable gender split, with 25 percent of self-employed women contributing to a personal pension, versus 31 percent of men.
- **Welfare** – Just over 21 percent of the self-employed community are in receipt of tax credits.¹³⁹ Yet the figure is 42 percent for Asian / Asian British self-employed people, and 35 percent for the Black / Black British self-employed. The take-up rate does not vary significantly by gender or ethnicity, however older groups are less likely to claim their tax credit entitlements.
- **Universal Credit** – 52 percent of women would fall below the Minimum Income Floor (MIF) as it stands, compared with 37 percent of men.¹⁴⁰ There is little difference when looking at age, except for the over 65s, 58 percent of whom would not earn enough to reach the MIF.
- **Training** – Self-employed women are nearly twice as likely as men to have had access to training in the past year, with 27 percent and 17 percent saying so respectively.¹⁴¹ Young people in particular are more likely to have engaged in training. Twenty-nine percent have participated in the last year compared with 20 percent of the self-employed population as a whole.

136. RSA analysis of 2012/13 Family Resources Survey.

137. Ibid.

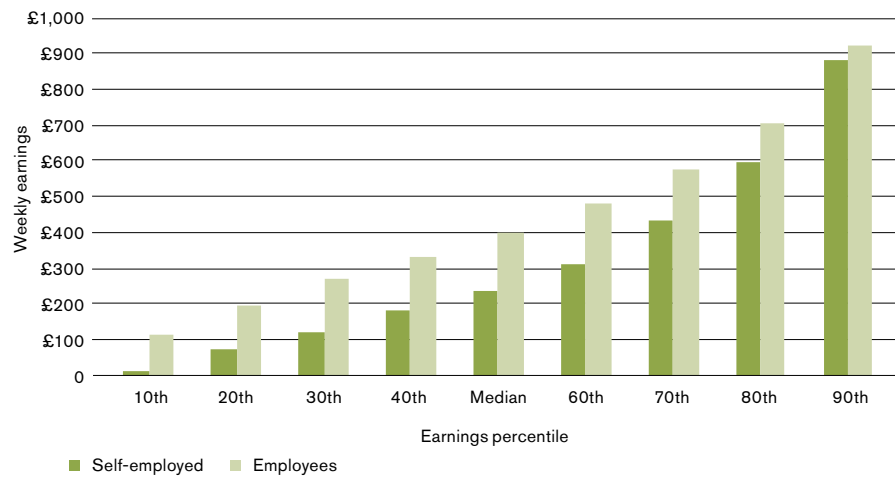
138. Ibid.

139. Ibid.

140. RSA analysis of 2011/12 Understanding Society Survey data (Wave 3).

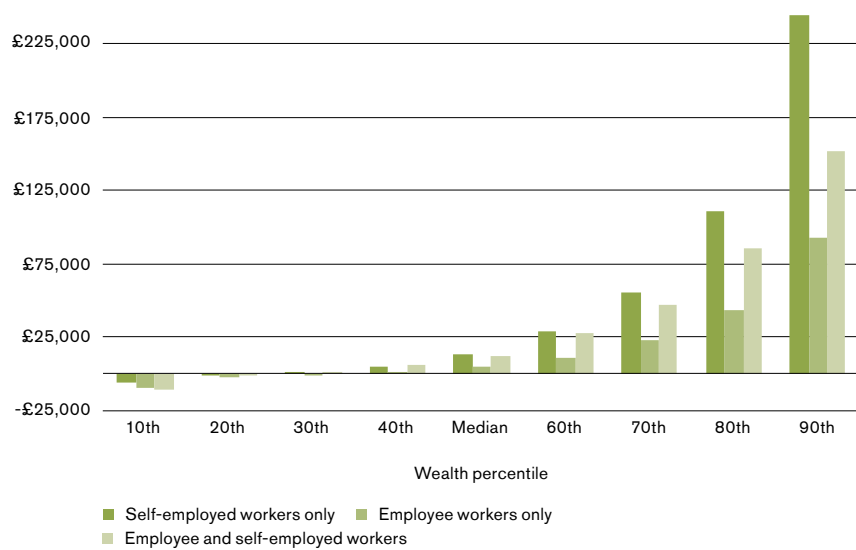
141. Ibid.

Figure 11: Income distribution among employees and the self-employed



Source: RSA analysis of Family Resources Survey 2012/13

Figure 12: Financial wealth distribution by household working status



Source: RSA analysis of the Wealth and Assets Survey 2010/12 (Wave 3)

Table 9: Material deprivation indicators by household working status (for families with children only)

Figures refer to the proportion of families in each category who would like to do the stated activity but cannot afford to.

| Activity | Not working | Households with one self-employed worker, no employees | Households with more than one self-employed worker, no employees | Households with one employee, no self-employed | Households with more than one employee, no self-employed | Households with a mix of self-employed and employees |
|--|-------------|--|--|--|--|--|
| Attends regular organised activity outside of school each week | 19.8% | 9.3% | 3.0% | 9.6% | 3.8% | 8.2% |
| Enough bedrooms for every child over 10 to have his/her own | 22.5% | 15.9% | 1.6% | 14.7% | 7.6% | 3.4% |
| Celebrations on special occasions | 9.0% | 3.7% | 0.0% | 3.1% | 0.6% | 0.4% |
| Leisure equipment such as sports equipment or a bicycle | 17.1% | 7.0% | 2.7% | 8.0% | 2.0% | 0.9% |
| Holiday away from home at least 1 week a year with family | 73.0% | 40.6% | 25.6% | 39.9% | 20.0% | 18.9% |
| A hobby or leisure activity | 13.8% | 7.0% | 0.8% | 5.5% | 2.2% | 1.8% |
| Go on a school trip at least once a term | 13.0% | 5.5% | 2.4% | 6.1% | 1.3% | 1.5% |
| Eat fresh fruit or veg every day | 10.1% | 1.9% | 2.0% | 4.0% | 1.0% | 0.9% |

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