European Platform Undeclared Work

Developing a Holistic Approach for Tackling Undeclared Work

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SUMMARY OF MUTUAL LEARNING

On 2 December 2016, the European Platform Tackling Undeclared Work organised a seminar in Brussels on developing a **holistic policy approach**. The aim was to enable Platform members and observers to consider a holistic policy approach towards tackling the undeclared economy. Consequently the seminar focused on an approach which uses, in a strategic and coordinated manner, the full range of both the direct and indirect policy approaches and measures available to increase the power of, and trust in, authorities respectively. The seminar brought together Platform members from all 28 EU Member States (MS) and Norway (EEA) – including representatives of national ministries, labour inspectorates, social security authorities, and tax and customs authorities - as well as European-level social partners and international organisations.

Key findings:

There was widespread support for a more holistic approach towards tackling the undeclared economy. It is an issue which affects many aspects of the economy and society, through for example breaches of workers' rights, unfair competition and reduced tax revenues. For this reason, a joined-up, integrated response is essential.

- Achieving a holistic approach to tackling undeclared work is nevertheless a challenge. A wide range of public sector stakeholders need to cooperate and work closely with social partners. Some countries have successfully developed new structures to ensure greater collaboration, which will lead to a more effective and efficient response to the problem of undeclared work.

- Examples of national action plans, national institutions and joint operations were presented at the seminar, ranging from national action programmes (Finland, Greece), to a national electronic register of employment (Estonia) and a new national labour inspectorate (Italy). Together with Norway and France, which presented examples of how to promote collaborative working, these practices showed how a more holistic approach can be achieved by stakeholders working together.

- It is a widely accepted policy objective not to aim to eradicate the undeclared economy, but rather to move undeclared work into the declared economy. The result is that the dominant policy approach across the Member States of using direct controls to deter engagement by increasing the risks of detection and penalties, i.e. 'sticks', is being increasingly complemented by a wider range of measures, including preventative and curative incentive measures, i.e. 'carrots'.

- How to most effectively combine and sequence these approaches and measures remains subject to debate and it is important to recognise that what works in one country may not work in another. There is an emerging evidence-based consensus, nevertheless, that the most effective approach is to concurrently improve both the power of authorities using direct measures, i.e. enforced compliance, as well as trust in authorities using indirect measures, i.e. voluntary cooperation. The slippery slope framework presented at the seminar suggests that a combination of both greater trust in authorities and greater power of authorities ensures compliant behaviour.

1 PURPOSE OF THE SEMINAR

Decision 2016/344 of 9 March 2016 of the European Parliament and of the Council on *Establishing a European Platform to Enhance Cooperation in Tackling Undeclared Work* explicitly states that "*A wide range of policy approaches and measures to tackle*

undeclared work have been introduced across the Member States…Tackling the complex problem of undeclared work still needs to be developed and requires a holistic approach".

To encourage mutual learning across Member States and the social partners about a holistic approach, the European Platform Tackling Undeclared Work organised its first seminar in Brussels on 2 December 2016 to facilitate such learning. This brought together Platform members from all 28 EU Member States (MS) and Norway (EEA) – including representatives of national ministries, labour inspectorates, social security authorities, and tax and customs authorities - as well as European-level social partners and international organisations, including the ILO, Eurofound, ETUC and European Federation of Cleaning Industries.

There is evidence of a currently heavy reliance in Member States on a narrow set of deterrence measures that tackle undeclared work by increasing the penalties and risks of detection. Barriers exist to the adoption of a wider range of measures, notably a perception that these deterrence measures are the most effective means of tackling undeclared work, despite the lack of evidence that this is the case. In order for the Platform to facilitate a more holistic approach, this seminar sought to address this problem and how Member States might start to develop a more holistic approach.

This Learning Resource reports the outcomes of the seminar. The first section reports the full range of policy approaches and measures available to Member States for tackling undeclared work - along with examples of good practice, examines the breadth of policy measures currently used in Member States, and evaluates the barriers Platform members and observers identified to the adoption of a wider range of policy approaches and measures. The second section then investigates the different ways of combining and sequencing these policy approaches and measures - along with the results of the discussion by Platform

members and observers on what is most effective.

Although no official universal definition exists of undeclared work, this learning resource adopts the definition widely adopted across the European Union (EU) which defines undeclared work as "*any paid activities that are lawful as regards their nature but not declared to public authorities, taking account differences in the regulatory systems of the Member States*"

The three key reasons for not declaring these otherwise lawful activities are:

- To avoid payment of income, value added or other taxes;

- To avoid payment of social security contributions; and

- To avoid having to meet certain legal labour standards, such as minimum wages, maximum hours, safety standards, etc.

Hence, the only feature differentiating undeclared from declared work is that it is not declared to the authorities for tax, social security and labour law purposes when it should be. If other differences exist, it is not undeclared work. If the goods and services provided are unlawful (e.g., the production or trafficking of drugs, firearms, persons or money laundering forbidden by law), it is part of the wider criminal economy (i.e., the 'shadow economy' is often defined as including both the undeclared economy and criminal economy), and if there is no monetary payment, it is part of the unpaid sphere.

2 POLICY APPROACHES AND MEASURES TO TACKLE UNDECLARED WORK

Key Questions:

- Which policy approaches and measures are available for tackling undeclared work?

- Are there examples of good practice that can facilitate learning?

- What are the most used and least used policy approaches and measures?

- What are the barriers preventing the adoption of a wider range of policy approaches and measures?

It is now widely accepted that the policy aim is not to eradicate the undeclared economy, but to move undeclared work into the declared economy[i]. Figure 1, below, shows that there are a wide range of policy approaches and measures available for transforming undeclared work into declared work.

In the following sections, the full range of policy approaches and measures available for tackling undeclared work will be outlined first, followed by examples of good practice to facilitate learning. Third, the breadth of policy measures currently used in Member States will be described and finally, the barriers Platform members and observers identified to the adoption of a wider range of policy approaches and measures.

2.1 Introduction to the holistic approach

A **holistic policy approach** towards tackling the undeclared economy uses in a strategic and coordinated manner the full range of both the direct and indirect policy approaches and measures available to increase the power of, and trust in, authorities respectively.

Direct approaches reduce the costs and increase the benefits of operating on a declared basis, and increase the costs and reduce the benefits of operating undeclared. Viewing those participating or considering participation in undeclared work as rational economic actors, who weigh up whether the pay-off is greater than the expected cost of detection and punishment, the objective is to alter the cost/benefit ratio confronting them. To do this, it uses:

- *Deterrence measures* that detect and punish participation in undeclared work by:

    o *raising the penalties and sanctions for those caught* (e.g. besides fines, innovative forms of sanction are emerging in many countries, such as the use of 'black lists' which prohibit offenders from applying for public support programmes or public procurement tenders, or 'naming and shaming' initiatives where the names of offenders are made public), and/or

    o *increasing the perceived or actual likelihood of detection* (e.g. using workplace inspections; ICT systems to enable data matching; worker registration initiatives prior to starting work or on their first day of work; mandatory IDs in the workplace; coordinated data sharing initiatives across government; the coordination of operations between government departments; coordinating strategy across government, and the use of peer-to-peer surveillance (e.g. telephone hotlines).
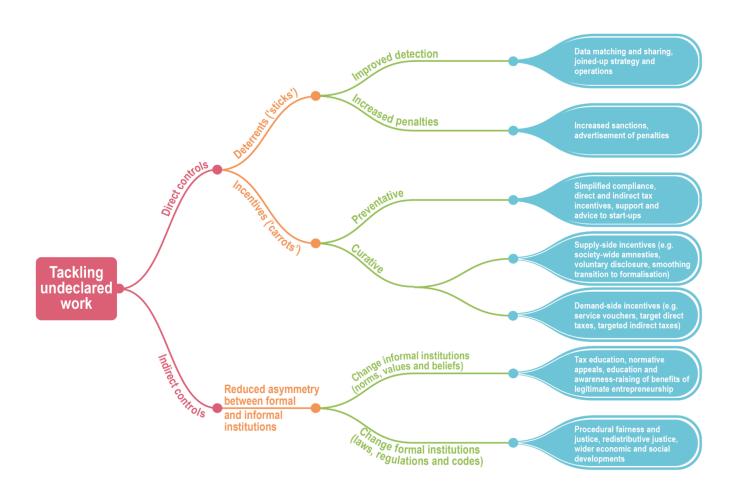
Figure 1: Policy approaches and measures available for transforming undeclared work into declared work

- *Incentive measures* that make it easier to undertake, and reward, participation in declared work. These include:

  o *Preventative measures* that discourage citizens from engaging in the undeclared economy (e.g. by simplifying compliance, using direct and indirect tax incentives to make it beneficial to operate on a declared basis, and providing support and advice about how to start-up legitimately), and

  o *Curative measures* that incentivise citizens, workers and businesses to make the transition from the undeclared to the declared realm. These are of two varieties:

    ▪ supply-side incentives targeting businesses and workers in the undeclared economy (e.g. society-wide amnesties, individual-level voluntary disclosure schemes, and advisory and support services to those wishing to move from the undeclared into the declared realm), or

    ▪ demand-side incentives targeting their customers with rewards for using declared goods and services (e.g. granting income tax deductions on the costs incurred of obtaining services on a declared basis; issuing of vouchers so that consumers only pay a

proportion of the hourly wage rate, leaving the remaining part to be covered by the state; and the use of indirect tax deductions).

Indirect approaches, meanwhile, recognise that citizens and businesses are not just rational economic actors (purely calculating the costs and benefits). They are also social actors who engage in undeclared work when formal institutional failings lead them to adopt norms and beliefs regarding participation in undeclared work that do not align with the laws and regulations, for example due to a lack of trust in the state and what it is seeking to achieve. From this perspective, therefore, all societies have institutions which prescribe, monitor and enforce 'rules of the game' regarding what is socially acceptable. On the one hand, there are formal institutions (i.e. the laws and regulations) that prescribe 'state morality' about what is socially acceptable, and on the other hand, informal institutions (i.e. the socially shared rules, usually unwritten) which describe 'citizen morality'. To align them, indirect policy approaches either:

- *Change the norms, values and beliefs* regarding the acceptability of participating in undeclared work, so that these are in symmetry with the laws and regulations (e.g. using awareness raising campaigns and educational initiatives), and/or

- *Change the formal institutional imperfections* that lead to a lack of alignment between the norms, values and beliefs of the population, and the laws and regulations. This can involve either:

  o *Changing the internal processes of formal institutions to improve the perception amongst citizens and businesses that there is procedural and distributive* fairness and justice, so as to improve trust in government. Procedural fairness refers to whether citizens and businesses receive what they perceive as procedurally fair treatment. Distributive justice

refers to whether citizens and businesses receive the goods and services they believe that they justly deserve given the taxes that they pay. Procedural justice refers to whether citizens and businesses believe that the authorities treat them in a respectful, impartial and responsible manner. Being treated politely, with dignity and respect, being given a say, and having genuine respect shown for one's rights and social status, all enhance compliant behaviour.

  o *Changing the products of formal institutions*. Reviewing studies that evaluate the relationship between cross-national variations in economic and social conditions, and cross-national variations in the size of the undeclared economy, the same findings consistently emerge. Whether the size of the undeclared economy is measured using Multiple Indicators Multiple Causes (MIMIC) method estimates or direct surveys, and whether studies compare the 28 Member States of the European Union, post-socialist transition economies or countries across the developing world, the finding is that reducing the prevalence of undeclared work is significantly associated with:

    - increasing GDP per capita;

    - improving the quality of governance and reducing corruption;

    - increasing expenditure on labour market interventions to help the most vulnerable groups;

    - increasing social expenditure, and

    - developing more effective social transfer systems so as to reduce the level of inequality and severe material deprivation.

2.2 Examples of good practice

Platform members presented examples of how a more sophisticated strategic and coordinated approach is being adopted in Member States, especially with regard to improving the risk of detection in order to increase the power of authorities. For example, many Member States have established registers of employment not only so that effective workplace inspections can be conducted but also to enable data mining to identify instances of undeclared work. Box 1 reports how Estonia has merged several registers to enable undeclared work to be more efficiently tackled.

Box 1. Register of Employment: a data sharing good practice measure, Estonia

On 1 July, 2014, the Estonian register of employment was created under an amendment to the Taxation Act, to overcome the fact that the authorities dealing with unemployment and employment were using separate databases. The idea was to store data relating to employment in one place. Responsibility for the register of employment lies with Estonian Tax and Customs Board (ETCB). All employers must register all their employees before they start work, regardless of the form of contract, and it also includes people working on a voluntary basis. Registration can be by: E-Channel (E-Tax/E-Customs); at the ETCB office; by phone or SMS. By offering three ways of registering and eliminating paper submissions, the ETCB has tried to make the process easier for employers. Furthermore, employers can now access their 'live' data and make changes to it, at any point in time.

The following stakeholders have access to the data on the register: the Health Insurance Fund, the Unemployment Insurance Fund, the Police and Border Guard Board, the Social Insurance Board, and the Labour Inspectorate. Among other things, the data is used to: determine health insurance; determine unemployment benefits (on termination of employment); monitor foreigners' working conditions; monitor and investigate accidents at work, and verify tax compliance (labour taxes).

With the introduction of the employment register, joint inspections are now carried out by the labour inspectorate and police and border guard. Through the joint inspections, a media campaign and press releases, the ETCB drew attention to the register and its importance. These awareness-raising activities were necessary to encourage people to use the database. Moreover, alongside the electronic register, new IT tools have been introduced for the ETCB tax auditors. They can access the data they need for inspections 'live' whilst they are on site conducting an investigation.

The impact of the register has been estimated in relation to the additional tax revenue generated in 2014. During that year, an additional EUR 11.8 million was collected, which is linked to the registration of an additional 21,000 workers. Undeclared work has been reduced as a result of the employment register. The problem now is to tackle under-declared employment (i.e. employees declared in the register but their real income is not provided).

A further strategic and coordinated approach, this time regarding data analysis, is to be found in Finland. When pursuing data analysis, many Member States confront problems related to the sharing of data, not least the ability to share data with each other and the poor inter-operability of their databases. Finland has overcome this by establishing a single unit to provide data analysis (see Box 2).

Box 2. The Grey Economy Information Unit (*Harmaan talouden selvitysyksikkö*): a deterrence measure good practice, Finland

Established in January 2011, this specialist unit within the tax administration (in the Ministry of Finance) promotes the fight against the grey economy, including undeclared work, by producing and sharing information regarding the grey economy and its control. It produces general reports without identifying specific actors (under its task of information gathering and dissemination). The Unit gathers information and conducts investigations into undeclared work.

In addition the Unit produces compliance reports in order to support different authorities. A compliance report describes how the organisations and the persons or organisations that directly or indirectly are linked to the organisation in question act, have taken care of their finances and how they have fulfilled their statutory obligations. This information is gathered from different registers of authorities. A compliance report is conducted at the request of other organisations, such as the police, customs bureau and Finnish Centre for Pensions as well as authorities dealing with work safety, debt recovery and bankruptcies. The unit has the power to obtain information from the authority that requests the compliance report. A compliance investigation can also be a general phenomenon report in which the sectors, phenomenon and extent of the grey economy are studied.

The unit does not charge for the preparation of compliance reports and is entitled to obtain the necessary information free of charge. A compliance report can be used only for the requested purpose, although it can be used as basis for another report requested by the same authority on the same subject.

The Grey Economy Information Unit is authorised to keep a database within the meaning of the Data Protection Directive (95/46/EC, 1995), containing information necessary for the preparation of reports. According to the Act on the Grey Economy Information Unit (1207/2010), all information which is no longer needed must be deleted. In the Act there are provisions on obtaining the information, archiving and deletion. The data controller is the tax administration. The advantage of this centralisation of data analysis is that many of the problems witnessed in other Member States related to the inter-operability of databases are overcome.

Beyond using more effective data mining and sharing, Member States have also sought to improve the chance of detection by developing more strategic and coordinated approaches towards strategy and operations. In Italy, for example, the previous fragmented approach which resulted in various agencies having overlapping functions has been resolved by establishing a single national Labour Inspectorate so as to rationalise and simplify the organisation of the fight against undeclared work (see Box 3). In France, meanwhile, there has been a concerted effort to join up operations and strategy between the local, regional and national levels, and importantly, to do so by listening to local inspectors about what they require (Box 4). As outlined in Box 5, Norway, similarly, has not only joined up the local, regional and national levels to improve the risk of detection, but also formally integrated the social partners into the decision-making process.

Box 3. Legislative reform of the labour inspections system: the establishment of the Italian National Inspectorate for Labour Inspections (NLI), Italy

Between 2014 and 2016, Italy created a new national authority, the Italian National Inspectorate for Labour Inspections (NLI), which joins together all three relevant stakeholders in the field: the Ministry of Labour and Social Policies, the National

Institute of Social Security (INPS), and the National Institute for the Insurance against Accidents at Work (INAIL).

This legislative reform of the labour inspections system was developed to answer rising public criticism about the labour inspections system, which was perceived as unfair, uncoordinated and inefficient. To rationalise and simplify the organisation and the execution of the inspections and controls, it was agreed to create a single body that joins the competences and the know-how of the three most important authorities. New data sharing agreements were developed; which are expected to result in a better planning of the inspections, and in a more transparent documentation of the outcomes. Moreover, the three authorities will share good practice, e.g. in relation to inspection techniques.

As a result, the stakeholders expect higher acceptance of the National Labour Inspectorate, and better compliance with its procedures. The new body will apply a mixture of methods; including deterrence measures like detection and punishment of activities related to undeclared work; and preventive measures like simplifying rules for compliance, and providing support and consultancy to companies on how to act legitimately.

The reform will be in effect as of 1 January 2017. A joint monitoring framework based on common indicators will be agreed between the three institutions (based on the previous monitoring arrangements in place by each individual institution). First public reactions to the reform were positive; the efforts to achieve rationalisation and simplification were acknowledged. An evaluation is planned for 2017/2018, to get a more detailed insight into outcomes and effects of the reform.

Box 4. Legislative reform of the labour inspections system and creation of the regional units to support and monitor the fight against undeclared work, France

In 2012, the French Ministry for Labour, Employment, Vocational Training and Social Dialogue initiated a reform of the Labour Inspectorate and the creation of regional units to support and monitor the fight against undeclared work. This reform aimed at strengthening coordination at its different levels. The new organisation of the Labour Inspectorate now comprises local control units *(unités de contrôle)*, supported by regional units to support and monitor the fight against undeclared work (*unité régionale d'appui et de contrôle en matière de travail illégal*), which provide support to the local units that do not always have time and resources to invest in the fight against undeclared work. Finally, the reform introduced a *National Group for monitoring, support and control* which supports local services on subjects of national importance. This National Group is not a dedicated group on undeclared work but this topic has however been its main focus since its creation. This body is seen as a very useful central monitoring point to identify new complex frauds and but also respond to requests from other services. The strength of this reform is that it has developed based on feedback from local officers.

Box 5. Joint operation groups between public agencies: an effective tool against work-related crime and social fraud, Norway

Launched in January 2015, the new strategy for combating work-related crime aims to increase cooperation between public agencies at national, regional and local level to streamline approaches, enhance information exchange and coordinate resources. Established on the basis of a dialogue between the main employer and employee federations, the new strategy is bringing together different public agencies and authorities in joint offices across the country. So far five joint offices, consisting of staff members from the Labour Inspection Authority, the Labour and Welfare

These initiatives all exemplify good practice in that they pursue a more effective, integrated and coordinated approach towards tackling undeclared work. However, they all focus upon improving the risk of detection by either improving data mining and sharing, or data analysis, or developing a more joined-up approach to operations or strategy. To pursue further improvements, however, what is required is to understand which approaches and measures are currently under-utilised.

2.3 Most and least used policy approaches and measures

Having outlined the range of policy approaches and measures available, and examples of good practice, it is important to recognise that some approaches and measures are under-utilised. In 2010, when evaluating the feasibility of establishing the European Platform, a web-based survey was undertaken of senior officials responsible for tackling undeclared work in 31 European countries in labour inspectorates, tax administrations, social security administrations, trade unions, employer organizations and other relevant agencies (e.g., customs, border police, and immigration). Table 1 displays the percentage of the 31 countries adopting various policy measures.

Table 1: Percentage of 31 countries adopting specific policy measures, 2010

Policy approach/measure		
Direct deterrence penalty measures	Administrative sanctions for purchasers/companies	87%
	Administrative sanctions for suppliers/employees	83%
	Penal sanctions for purchasers/companies	74%
	Penal sanctions for suppliers/employees	53%
Direct deterrence – improved detection rates	Workplace inspections	100%
	Data matching and sharing	83%
	Registration of workers prior to start/on first day	74%
	Certification of businesses and/or payment of social contribution and taxes	65%
	Coordinated data sharing across government	65%
	Use of mandatory IDs in the workplace	65%
	Coordination of operations across government	61%
	Coordinated strategy across government	57%
	Peer-to-peer surveillance (e.g. telephone hotlines)	39 %
Direct incentives to prevent	Simplified compliance procedures	87%
	Training and support for business start-ups	61%

Policy approach/measure		
citizens and businesses entering the undeclared economy	Direct tax incentives (e.g. exemptions, deductions)	61%
	Advice on how to formalise	61%
	Micro-finance for business start-ups	52%
	Reduced regulations	48%
	Technology innovations (e.g. certified cash registers)	43%
	Social security incentives	35%
	Factsheets on record keeping	22%
	Free advice/training on record keeping	22%
	Targeted VAT reductions	17%
	Free record keeping software for businesses	13%
	Changes minimum wage downwards	9%
Direct curative incentives on the supply side	Initiatives to ease the transition from unemployment into self-employment	65%
	Initiatives to ease the transition from employment into self-employment	44%
	New categories of work (e.g. for small or mini-jobs)	35%
	Formalisation advice to business	30%
	Formalisation support services to businesses	30%
	Individual-level amnesties for voluntary disclosure	17%
	Supply chain responsibility	17%
	Gradual formalisation schemes	13%
	Society-wide amnesties	9 %
Direct curative incentives on the demand side	Targeted direct tax incentives at customers of undeclared work	61%
	Service vouchers	26%
	Targeted indirect taxes at customers of undeclared work	17%
Indirect measures	Measures to improve tax/social security/labour law knowledge	65%
	Campaigns on risks and costs of undeclared work	61 %
	Campaigns to inform users of undeclared work of the risks and costs	61%
	Campaigns on benefits of formalising their work	57%
	Campaigns to inform users of the benefits of declared work	52%
	Normative appeals to people to declare their activities	52%
	Campaigns to encourage a culture of commitment to declaration	39%

Policy approach/measure	
Adopting a commitment rather than compliance approach	30%
Measures to change the perceived fairness of the system	26%
Measures to improve the procedural justice of the system	17%

Source: Williams, Windebank, Baric and Nadin (2013: Table I)

In 2010, therefore, deterrence measures were widely used in all 31 countries. Many countries also used incentives to make it easier and/or reward compliant behaviour as well as indirect controls to elicit a commitment to legitimate behaviour and self-regulation, albeit these were less commonly used than deterrence measures.

However, these figures do not reveal which measures are viewed as the most important means of tackling undeclared work. To evaluate this, stakeholders were asked to rank the different sets of policy measures from those accorded the most importance to the least importance in their country. As Table 2 displays, 57% state that deterrence measures are accorded the most importance in their country and just 43% other measures (with 19% citing supply-side incentive measures, 14% demand-side incentives and just 10% indirect controls). Indeed, examining the type of policy measure accorded the least importance; only 16% cite deterrence measures. The clear intimation is that the deterrence approach is predominantly viewed as the most important means of tackling undeclared work.

Table 2: Stakeholder opinion of the relative importance accorded to different types of policy measure in their country, 2010

% citing:	Most important	2nd Important	Least important
Direct controls: deterrents	57	17	16
Direct controls: supply-side incentives	19	46	23
Direct controls: demand-side incentives	14	19	32
Indirect controls	10	18	29

Source: Williams, Windebank, Baric and Nadin (2013: Table V)

To update this 2010 data on the most and least used approaches, Platform members and observers in the seminar considered the relative importance attached to these policy approaches in their Member States. The strong consensus was that the deterrence approach that seeks to increase the sanctions and risks of detection was dominant. This was particularly the case in many East-Central and Southern European Member States which tended to be closer to a 'pure' deterrence approach and to adopt a less 'mixed' (i.e. holistic) approach than many Western and Nordic Member States.

Indeed, the consensus among both Member State seminar participants as well as social partners was that deterrence approaches were a necessary tool for tackling undeclared work. Most Member States had therefore focused upon developing more strategic and coordinated initiatives to deter engagement in undeclared work. This included not only more sophisticated sanction systems, such as 'white lists' and 'black lists', but also more effective systems for detecting undeclared work, ranging from the development of data mining and sharing, the greater use of targeted inspections and cooperation across enforcement agencies. Indeed, all of the examples of good practice (in Section 2.2 above) have as their focus improving the risk of detection either by enhancing data mining and sharing, and analysis (Boxes 1 and 2), or by joining-up strategy and operations (Boxes 3, 4 and 5). This reflects the heavy emphasis Member States put on this deterrence approach.

Beyond improving the risk of detection, nearly all Platform members and social partners at the seminar also voiced that there had been some expansion in the range of incentives of a curative and preventative variety both on the supply and demand-side over the past few years. They furthermore voiced that there was additionally now much greater understanding of the importance of indirect controls, especially awareness raising campaigns. Ireland, for example, had established a call centre providing a 'helping hand' to businesses as a preventative tool.

2.4 Barriers to adopting a fuller range of policy approaches and measures

Asked to rank the policy approach they view as most effective, second most effective and least effective at tackling undeclared work, Table 3 reveals that the majority (55%) of stakeholders surveyed in 2010 assert that deterrence measures are the most effective means of tackling undeclared work. Just 20% view supply-side incentives, 15% demand-side incentives and 10% commitment measures as the most effective approach.

Only a minority, therefore, believe that either an approach that rewards and encourages compliant behaviour or an indirect controls approach, aimed at improving the social contract between the state and its citizens, is more effective at eliciting compliance than the detection and punishment of non-compliant behaviour.

Table 3: Type of policy measures stakeholders view as most and least effective in Europe, 2010

	Most effective	2nd most effective	Least effective
Direct controls: deterrents	55	13	12
Direct controls: supply-side incentives	20	41	13
Direct controls: demand-side incentives	15	27	31
Indirect controls	10	19	44

Source: Williams, Windebank, Baric and Nadin (2013: Table IV)

In the December 2016 seminar, Platform members and observers expressed a similar, albeit more nuanced, view. The consensus was that deterrence measures continue to prevail for two major reasons. On the one hand, there was a strong view among Platform members and observers that non-deterrence approaches are a more long-term approach and do not provide the 'quick wins' required, and that this therefore constrained the resources devoted to them.

On the other hand, the issue was raised that there was a lack of evaluation of these non-deterrence policy approaches and measures, and this acted as a barrier to their adoption. Although evaluations of deterrence measures show that they can either reduce, have no effect, or even increase, undeclared work, at least there are some evaluations, even if they are often relatively out-of-date. There was thus a view that the lack of evaluation of the effectiveness of these non-deterrence policy measures hindered the adaptation and redirecting of approaches towards these non-deterrence measures.

Indeed, reviewing both the views of the Platform members and observers, and the wider evidence on the effectiveness of different policy approaches and measures, four conclusions can be drawn:

- there is currently little ex-ante and ex-post evaluation of policy measures;

- when evaluations are undertaken, they often use different indicators to assess the effectiveness of policy measures (e.g. revenue-to-cost ratios, number of declared jobs created; reductions in instances of undeclared work);

- the effectiveness of policy measures is often measured only from the perspective of one stakeholder (e.g. revenue-to-cost ratios evaluate the effectiveness of a measure for tax authorities), whilst its effectiveness from the viewpoint of other stakeholders is not evaluated, such as from the perspective of suppliers and customers. This is problematic because what might be an effective measure for one stakeholder (e.g. a tax authority) might not be for other stakeholders (e.g. purchasers of undeclared goods and services, or trade unions), and

- even when policy measures have been evaluated, how to assess the cross-national transferability of policy measures for tackling undeclared work has been seldom addressed.

It was also felt that policy measures which have been evaluated need to be reported via the Platform's repository of 'good practices'.

Consensus Observations

- There remains a focus upon deterrence measures when tackling undeclared work in most Member States;

- The widespread perception is that deterrence measures are the most effective means of tackling undeclared work;

- Although there is greater use in Member States of incentive measures, and awareness raising campaigns, only a small proportion of resources are dedicated to these measures;

- There is currently little formal evaluation of the contemporary effectiveness of different policy approaches and measures across Member States, which results in a weak evidence base, and a barrier to the adoption of a wider range of approaches and measures.

3 COMBINING AND SEQUENCING POLICY APPROACHES AND MEASURES

Key Questions:

- What are the different ways of combining and sequencing policy approaches and measures?

- More particularly:

  o What is the 'responsive regulation' approach?

  o What is the 'slippery slope framework'?

  o What is the cutting-edge evidence-base on the effectiveness of different ways of combining and sequencing policy measures?

It is not only the range of approaches adopted which is important but also how they are combined and sequenced. For example, governments might seek to change the culture of government departments towards a more customer-oriented approach and introduce public campaigns about the importance of working declared, whilst simplifying regulatory compliance and introducing incentives (e.g. amnesties, tax deductions) to enable undeclared work to move into the declared realm. In relation to those who fail to comply, they may also pursue improvements in the probability of detection and tougher sanctions for those subsequently caught. Until now, however, there has been little attempt to evaluate which combination of measures is most effective, and neither has there been discussion of whether sequencing them
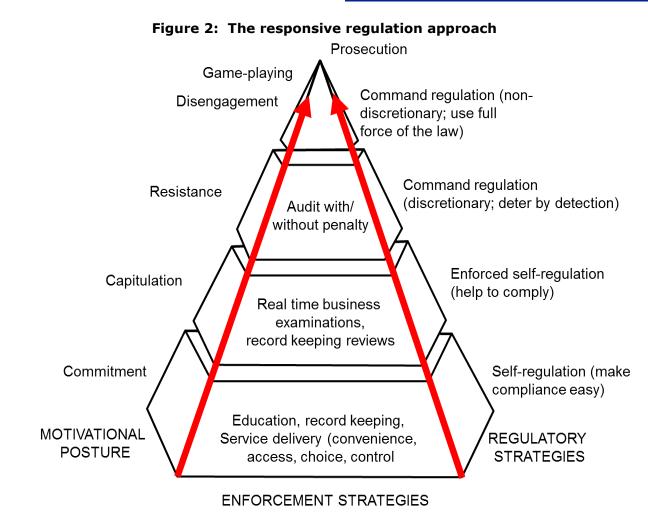
in some particular order is more effective.

As one Platform member highlighted at the seminar, the importance of sequencing is apparent in his MS where the absence of preventative measures has resulted in a large number of potential violations being reported which must by law be investigated, meaning the agency is unable to find resources to develop preventative measures. For this participant, this signalled that starting with deterrence measures has hindered the development of preventative measures, and that it would have been more rational to start with preventative approaches. Another Platform member recognised that the way measures are combined is important by citing an example of how a focus upon developing a 'black list' of businesses needs to be combined with formalisation services to help offenders become legitimate. Otherwise this means that many black-listed businesses have no means of *rehabilitating* themselves and therefore tend to reoffend.

There is a need to understand, therefore, how to combine and sequence these different direct and indirect policy approaches and measures to produce the most effective and efficient compliance system in different contexts. Below, two alternative perspectives regarding how policy measures might be combined and sequenced are presented.

3.1 Responsive Regulation

The responsive regulation approach envisages a regulatory pyramid, sequenced from the least intrusive indirect policy measures at the bottom and used first, to the most intrusive direct controls of deterrents at the top and used last (see Figure 2).

Figure 2: The responsive regulation approach

Source: adapted from Braithwaite (2003)

The premise underpinning this approach is that in most cases an authority does not need to use deterrents to achieve compliance. Instead, it can start with indirect policy measures, and if these fail to elicit behavioural change with some groups, then incentives should be used on these groups, with deterrents only used as a last resort. The level of intrusiveness therefore escalates up the pyramid until it reaches the policy intervention that elicits the desired response.

The recognition, therefore, is that there is a continuum of attitudes towards compliance and that different policy responses are appropriate for these different motivational postures. The result is a temporal sequencing of policy measures starting with indirect policy measures applied to the majority who adopt a positive posture (i.e. commitment, capitulation), and feel morally committed to follow the rules, then direct incentives for those with less positive postures (i.e. capitulation, resistance), and only after these fail are sanctions used for the disengaged. The Australian Government for example has adopted this 'responsive regulation' approach. However, whether this is the most appropriate combination and temporal sequencing of measures is open to debate.

3.2 Slippery Slope Framework

An alternative perspective on the combining and sequencing of policy approaches and measures is the 'slippery slope framework' which shows how governments can get on a slippery slope if they lose the trust of citizens and/or their power to enforce compliance. This firstly distinguishes between voluntary compliance which depends on the trust that individuals have in authorities (and is enhanced

using indirect measures), and enforced compliance which depends on the power of authorities (and is enhanced using direct measures).

As Figure 3 displays, the argument of the slippery slope approach is that citizens and businesses abide by the law either because they fear detection and fines due to the power of authorities (enforced compliance) or because they feel a commitment to be honest because they have trust in the authorities (voluntary cooperation). When there is effective enforced compliance as well as high voluntary cooperation (i.e. both power and trust), undeclared work is low. When there is ineffective enforced compliance and little voluntary cooperation, undeclared work is extensive.
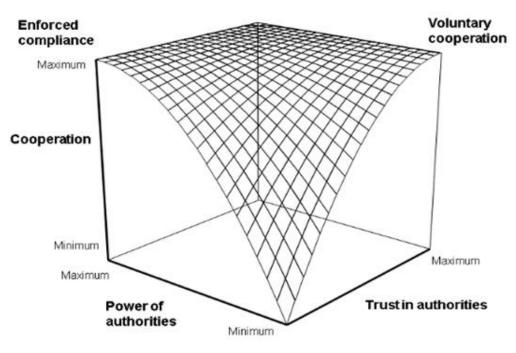
Figure 3: The slippery slope framework

Source: Kirchler et al. (2008)

For example, Wahl et al. (2010) randomly presented participants in a laboratory experiment with one of four different descriptions of a fictitious country, in which the authorities were depicted as either trustworthy or untrustworthy on the one hand, and as either powerful or powerless on the other hand. Respondents were most compliant when both trust and power were high, and lowest when trust and power were low. This has been since further reinforced by surveys of real-world taxpayers. The common finding in studies of Austria, Hungary, Romania and Russia, is that compliance is highest, if both power of authorities and trust in authorities are high.[ii]

On an EU-28 level, evidence that concurrently pursuing voluntary compliance (using indirect measures) and enforced compliance (using direct measures) might be the most effective approach is provided by an analysis of over 27,000 interviews conducted with citizens across the EU-28 for the 2013 Eurobarometer survey on undeclared work. A regression analysis explored the likelihood of individuals participating in undeclared work according to: (a) the perceived level of penalties and risks of detection, and (b) citizens' views on the acceptability of undeclared work (i.e. their level of commitment to compliance). The finding is that those perceiving both the penalties and risks of detection as higher are significantly

less likely to engage in undeclared work. Similarly, the more acceptable undeclared work is perceived to be, the greater the likelihood of participation.[iii]
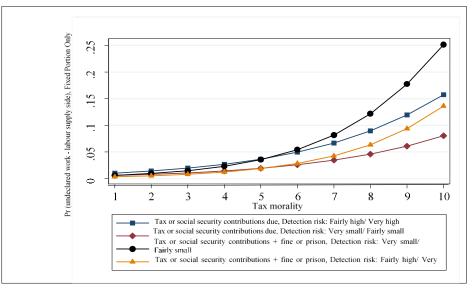
To further explore this, Figure 4 presents the predicted probabilities of a 'representative' EU citizen engaging in undeclared work by their level of commitment to compliance and what they perceive as the likely penalties and risk of detection. This shows that for those with greater commitment to compliance, deterrence measures have little impact on reducing the probability of participation in undeclared work. It is only when commitment to compliance is low that raising the level of deterrents has impacts, with increasing the perceived risks of detection leading to higher reductions in the likelihood of participation in undeclared work than

increasing the expected punishments. The clear lesson is that:

- Increasing commitment to compliance (using indirect measures) is effective as a means of tackling undeclared work;

- It is only in populations with a low commitment to compliance that raising the level of deterrents has an impact, with increasing the risks of detection having a greater impact than increasing the penalties.

Whether this is the case in each and every Member State now needs evaluation. Such an evidence-based approach to policy formulation is important if the effectiveness and efficiency of the fight against undeclared work is to be improved in Member States.

Figure 4: Predicted probability of a "representative" EU citizen participating in undeclared work: by expected sanctions, detection risk, and tax morality

*Sourc*e: Williams and Horodnic (2017)

During the seminar in December 2016, Platform members and observers were asked to discuss the following questions:

- What do you believe causes a lack of trust in Member States? Can this be overcome?

- What limits the power of authorities? Can this be overcome?

- Do you think that in practice enhancing power is always compatible with enhancing trust?

- Do we need a better understanding of what limits the power of authorities and trust in authorities in Member States? If so, how can this be achieved?

Lack of trust was argued to be a cultural and mind-set issue. It takes a long time to change cultural attitudes. More concretely, lack of trust was associated with lack of information about the law and the necessity of specific laws. Moreover, negative reports in the media were responsible, as was a lack of investment in education and awareness raising campaigns about the benefits of declared work. Complex laws, bureaucratic rules and lack of transparency were also thought to contribute to the lack of trust in authorities.

The lack of power of authorities was attributed to malfunctioning legislation, insufficient fraud detection, varying penalties, lack of political will, and lack of cooperation between different parties. Raising public awareness and the provision of greater resources to increase detection were deemed necessary to improve the situation. New forms of work (e.g. the 'collaborative economy') were thought in the current period to be major challenges to the power of authorities.

The question of whether power is always compatible with enhancing trust was thought to depend on firstly, how power is used (e.g. whether it is used in a proportional and just manner) and secondly, whether citizens and businesses perceive the use of power by authorities as procedurally just and fair. If the threat of sanctions is applied to those who already wish to comply and are compliant, then it was believed that trust could be destroyed.

How can a better understanding of power and trust be achieved? The Platform members and observers mentioned the need for more and appropriate studies on an EU level, country surveys, and generally more evidence to facilitate policy-making. Monitoring communication between the public and the authorities, coaching employees, training staff, simplification of the rules, procedural justice and distributional fairness, fighting corruption, the proportionality of sanctions, and protection of the weak were all deemed relevant. It was agreed that social partners need to be engaged and the various parties needed to collaborate closely in fighting undeclared work.

In conclusion, both the research evidence-base and the discussion at the seminar revealed that a full house of compliance strategies is necessary to combat non-compliance. How, therefore, might a Member State move towards a holistic policy approach that uses in a strategic and coordinated manner the full range of direct and indirect policy approaches and measures available to increase the power of, and trust in, authorities respectively? The way in which Greece has pursued such an approach provides an example (see Box 6).

Box 6. Towards a holistic policy approach: the case of Greece

With an undeclared economy equivalent to some 25% of GDP, in August 2015, as part of a three-year European Stability Mechanism (ESM) support programme for Greece, a Memorandum of Understanding (MoU) was signed by the European Commission and Greek Government setting out the detailed policy conditions attached to the financial assistance to Greece (European Commission, 2015a). One key deliverable of the MoU was for the Greek authorities to adopt an integrated action plan to fight undeclared and under-declared work. Facilitated by the ILO, a national action plan was subsequently formulated based on a holistic approach and is being implemented from 2016 onwards.

Given that Greece had neither a single agency responsible for tackling undeclared work, nor a central body responsible for ensuring coordinated action, a first step was to propose a national coordinating body responsible for the integrated holistic strategy towards the undeclared economy. Moreover, given that Greece previously relied on a relatively narrow approach and range of measures to tackle the undeclared economy, and based on a multi-stakeholder diagnostic of the causes, circumstances and forms of undeclared work in Greece, a coordinated and evidence-based approach was formulated based on a package of policies that involve: more effective deterrence measures; simplifying compliance to help individuals operate on a declared basis; the provision of various incentives to businesses to operate on a declared basis, suppliers of labour to make their work known, and purchasers of goods and services to hire declared work; as well as a range of indirect tools to resolve the failings of formal institutions so as to engender a culture of trust and commitment among the population to operate on a declared basis.

The full report is available at http://www.ilo.org/emppolicy/pubs/WCMS_531548/lang--en/index.htm, and the detailed Road Map at http://www.ilo.org/employment/units/emp-invest/WCMS_533853/lang--en/index.htm.

Consensus Observations

1. To be effective, there is a need to combine the full range of the direct and indirect policy approaches and measures available to increase the power of, and trust in, authorities respectively.

2. Using penalties and increasing the risks of detection is important to protect cooperative and compliant citizens and businesses from being exploited by free-riders. Audits need to be focused on at-risk groups and effectively implemented. They need to be perceived as a manifestation of power with the goal of protecting cooperative citizens from free-riders. Negative sanctions need to be appropriate in level and form.

3. Authorities combating undeclared work need to be well-trained, and they need to cooperate intensively with each other, wider stakeholders, and international authorities in order to fight undeclared work. There is also need to strengthen the dialogue and cooperation between public officials, social partners and researchers.

4. Laws need to be simplified so that citizens and businesses understand and abide by them. Instead of a plethora of rules with exceptions, principles of behaviour need to be fixed in law to minimize the space for interpretation and negotiation. Services to support and encourage businesses and citizens to operate on a declared basis need to be improved. Citizens and businesses need

to be segmented, so that appropriate services can be offered to facilitate rule compliance.

5. Distributive justice and procedural justice need to be taken seriously. The use of collected money needs to be transparent; advertising campaigns should be used to inform the public of the services available, so that the fair exchange of contributions on the one hand for state services on the other hand is clear. Procedures for determining contributions need to be transparent and fair, and authorities need to ensure adherence to these procedures.

6. Establishment and communication of social norms of correct behaviour is necessary. The power of social norms, as acknowledged by nudging units operating for various governments, is widely proved. Measures need to be taken that strengthen the identification of citizens and businesses with the wider community, which is a prerequisite to accept societal norms and to follow them.

4 KEY LEARNING OUTCOMES

4.1 Coordination and Integration

It is important for Member States to develop a **coordinated and integrated** approach that uses both direct controls (deterrents and incentives) and indirect controls (that align citizens and businesses norms and beliefs with the laws and regulations) to concurrently improve both the power of authorities, i.e. enforced compliance, as well as trust in authorities, i.e. voluntary cooperation.

4.2 Evaluation

There is a need for **evaluation** of policy measures to guide policy making by identifying the most effective policy approaches and measures to tackle undeclared work, and the important role social partners can play[1]. Until now, deterrence measures have been deemed the most effective. However, the evidence-base is weak. There is currently little ex-ante and ex-post evaluation of policy measures and even when evaluations exist, their effectiveness is often measured only from the perspective of one stakeholder, and considering how to assess the cross-

national transferability of policy measures has been seldom addressed.

4.3 Combining and sequencing

There is not only a need for greater evidence on the effectiveness of individual policy measures, but also how they can be **combined and sequenced**. The consensus is that using both direct and indirect measures produces the most effective and efficient compliance system. How to best combine and sequence these measures in different contexts, however, is open to debate. Although many authorities have started to develop approaches based on the belief that awareness raising and incentives should be used first, and deterrents only used as a last resort, this seminar started to rethink this approach and to reveal the effectiveness of concurrently enhancing both the power of authorities using direct measures, i.e. enforced compliance as well as trust in authorities using indirect measures, i.e. voluntary cooperation.

4.4 Further implications

Given this outcome that the most effective approach is to concurrently improve both the power of authorities using direct measures (i.e. enforced compliance) as well as trust in authorities using indirect measures (i.e. voluntary cooperation), what is now

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[1] The LU Platform representative did not agree with the inclusion of this point.

required is to consider the **implications** of these findings when tackling various **specific parts of the undeclared economy** (e.g. bogus self-employment, undeclared work in the construction and transport sectors, the sharing economy, under-declared employment).

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END NOTES

[i] Eurofound, 2013; European Commission, 2007; ILO, 2015

[ii] Kogler et al., 2013, 2015; Muehlbacher et al., 2011a,b

[iii] Williams and Horodnic, 2017

NOTES