



**European Platform Undeclared Work**

# **Member State Factsheets**

***2017***

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This publication has received financial support from the European Union Programme for Employment and Social Innovation "EaSI" (2014-2020). For further information please consult:

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## 1 Introduction

In 2016 factsheets were produced for each Member State to provide an overview of the state of play regarding efforts to address undeclared work, as part of preparations for the launch of the Platform Tackling Undeclared Work. The factsheets were produced by national experts from the European Employment Policy Observatory and covered a range of topics, including:

- The definition, characteristics and scale of estimated undeclared work (UDW) in each Member State;
- The institutional framework for addressing UDW – including the characteristics of the authorities responsible for identifying, tackling and/or preventing UDW, and the degree of cooperation between organisations within and between Member States; and
- The policy approach and measures used to tackle UDW in each Member State – including their effectiveness, the challenges and barriers faced in tackling UDW, and examples of good practice.

In 2017, following the first year of operation of the Platform, each Member State was given the opportunity to update their 2016 factsheets to reflect changes in the previous 12 months. A total of 20 Member States provided an update to their factsheets (as shown in Table 1 below), with an additional three reporting that no changes were required.

*Table 1. Member States Updating Factsheets - 2017*

	<b>Member State</b>
Member States updating factsheets	Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, France, Germany, Greece, Hungary, Italy, Latvia, Lithuania, Netherlands, Portugal, Slovakia, Slovenia, Spain, UK
Member States reporting that no changes were required	Finland, Ireland and Sweden
Member States not responding	Croatia, Luxembourg, Malta, Poland and Romania

The remainder of this document provides factsheets for all 28 Member States. In each case, the headings describe whether these were updated for 2017 (including Member States reporting no change) or whether the original 2016 factsheet is provided.

## **2 Member State Factsheets**

This section provides the factsheets for each Member State. As described above, they include:

- Factsheets where updates were provided marked as 2017;
- Factsheets where responses indicated no changes were required (marked as 2017); and
- Factsheets where no responses were received, and where the original 2016 factsheets are included (marked as 2016).

## Factsheet on Undeclared Work – AUSTRIA (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

Legal definitions in Austria can be found in the Criminal Code (Strafgesetzbuch - StGB), where § 153e defines “organised undeclared work” as “professional recruitment or placement of people in independent or dependent employment without the required registration for social insurance or without the required business license”. The law combating social security fraud (Sozialbetrugsbekämpfungsgesetz – SBBG) addresses and specifies several forms of social fraud, namely partial / no payment of social security contributions in the form of undeclared work (envelope wages, bogus part-time work, falsely declared employment), organised undeclared work or bogus registration to the social security system to obtain benefits or to avoid obligations. The Law against wage and social dumping (Lohn- und Sozialdumping-Bekämpfungsgesetz, LSD-BG in force since 1.1.2017; former LSDB-G), aims to ensure equal pay conditions for everyone employed in Austria and to ensure fair competition between Austrian and foreign companies. Penalties to companies are imposed if wages and salaries (as provided for in the collective agreements) fall short. The previously mentioned laws are the essential common framework for several institutions involved in combating undeclared work.

#### 2.1.2 Characteristics of undeclared work

In Austria, several types of undeclared work exist. Any ranking of the importance of different types suffers from a lack of data and limited comparability. Furthermore data reporting is irregular or undertaken in a compromised form, so that further distinctions cannot be provided.

- **Undeclared work** (e.g. (partly) envelope wages, bogus part-time work, underpayment – where wages and salaries are less than what is provided for in the collective agreements).

Underpayment is controlled under the LSD-BG including all forms of wages and salaries that fall short of collective agreements. Between 2011 (start of the implementation of the LSDB-G) and end of November 2016, nearly 1,950 reports relating to underpayment are documented (affecting 7,308 workers). More than 1,100 final decisions relating to underpayment exist which affect around 2,300 workers, of whom nearly 64% are from abroad.

Information on other types of activity, especially quantitative information, are highly limited (for results based on qualitative methods see footnote<sup>1</sup>). For the gastronomy sector, the Chamber of Labour<sup>2</sup> analysed the situation of part-time workers, finding more than half (58%) of the analysed cases reported to the social security authorities as being part-time or marginal employed workers had actually worked longer hours.

- **Bogus self-employment** (incl. undocumented (illegal immigrant) work)

Despite bogus self-employment being continually discussed as a problem, quantitative data are also limited. The union estimates that up to two-thirds of people working on the basis of a service contract (one-person-enterprises and ‘new self-employed’) or free service contract (Freie Dienstnehmer) are not employed correctly (cf. [www.watchlist-prekaer.at](http://www.watchlist-prekaer.at)).

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<sup>1</sup> Schmatz, Susanne / Wetzel, Petra, ‘*Developments in the field of wage dumping*’ (‘Entwicklungen im Bereich Lohndumping’), on behalf of the Chamber of Labour, Vienna, 2014.

<sup>2</sup> Chamber of Labour, ‘*Evaluation of 371 questionnaires in the gastronomy*’ (‘Auswertung von 371 Fragebögen Gastgewerbe’), unpublished report, Vienna, 2012.

Some information on bogus self-employment exists for the construction sector. Inspections of the Construction Workers Leave and Severance Pay Fund (Bauarbeiter-Urlaubs- und Abfertigungskasse - BUAK) in 2012, which controls the correct declaration of employment status, show indications of possible falsely declared self-employment in 69% of analysed cases.<sup>3</sup>

A specific contextual issue is the posting of workers. Austria is one of the main receiving Member States of posted workers. In 2014 Austria received more than 100,000 PDs A1 (portable documents A1), which is a 70 % increase compared to 2010.<sup>4</sup> It can be assumed that despite several improvements in recent years not all postings are reported to the authorities. Other important issue in this context is the bogus posting of workers and the prevention of forgery and falsification of PD A1. Inspection results repeatedly show cases of violations of the reporting requirements as well as several forms of incorrect payments.<sup>5</sup>

The number of illegally employed persons detected quantified by the Financial Policy was 11,961 in 2015,<sup>6</sup> corresponding to 20.6% of all controlled employed by the Financial Policy.

While undeclared work occurs in several economic sectors, it seems to be particularly widespread in the construction sector. Based on the LSDB-G statistics, previous experience shows that more than half of the final decisions relating to underpayment affect the construction sector (cf. calculations of Schneider (2016) for the shadow economy<sup>7</sup>). Other frequently mentioned sectors include agriculture, transportation, accommodation and food service activities or cleaning activities.

Undeclared work is more likely to be found in SMEs than in larger enterprises, where the possibility of work councils is higher. A report from 2012, based on expert interviews, showed that experts see works councils as an important control body to combat undeclared work.<sup>8</sup>

Main motivators for undeclared work include the possibility to earn more or some 'extra' money, or to find a paid job opportunity, which could be true for the unemployed as well as migrants with no or very restricted labour market access. Results from the Eurobarometer survey for 2013<sup>9</sup> show that problems in finding work is clearly less

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<sup>3</sup> Riesenfelder, Andreas/Wetzel, Petra, 'New forms of working at the interface between independence / dependence. Analysis of the situation in the construction industry' (Neue Arbeitsformen im Grenzbereich Selbständigkeit/Unselbständigkeit. Analyse der Situation in der Bauwirtschaft), Study on behalf of the Chamber of Labour, Vienna, 2013.

<sup>4</sup> Pacolet, Jozef / Wispelaere De, Frederic, 'Posting of workers. Report on A1 portable documents issued in 2014', report prepared in the framework of Contract No VC/2013/0301 'Network of Experts on intra-EU mobility – social security coordination and free movement of workers / Lot 2: Statistics and compilation of national data', on behalf of the European Commission, 2015.

<sup>5</sup> Schmatz, Susanne / Wetzel, Petra, 'Developments in the field of wage dumping' ('Entwicklungen im Bereich Lohndumping'), on behalf of the Chamber of Labour, Vienna, 2014 and, Riesenfelder, Andreas/ Schelepa, Susanne/ Wetzel, Petra, 'Monitoring of the opening of the labour market - Effects on forms of employment and wage dumping' (Monitoring der Arbeitsmarktöffnung - Auswirkungen auf Beschäftigungsformen und auf Lohndumping'), Study on behalf of the Chamber of Labour, Vienna, 2012.

<sup>6</sup> Federal Ministry of Finance (BMF), 'The Austrian tax and customs administration, Annual Report 2015' (Die österreichische Steuer- und Zollverwaltung, Geschäftsbericht 2015'), Vienna, 2016

<sup>7</sup> Schneider, Friedrich, 'Despite opposing tendencies (increase in unemployment and refugees) a reduction in the shadow economy in Austria in 2016' ('Trotz gegenläufiger Tendenzen (Anstieg der Arbeitslosigkeit und Flüchtlinge) ein Rückgang der Schattenwirtschaft (des Pfusches) in Österreich in 2016'), Linz, 2016.

<sup>8</sup> Riesenfelder, Schelepa, Wetzel, 2012.

<sup>9</sup> European Commission, 'Undeclared work in the European Union', Special Eurobarometer 402, 2014.

significant in Austria than the EU 27-average (12% vs. 21%). For Austrians, who had undertaken undeclared paid activities in the past year, the main reason was that “both parties benefited from it” (80% vs. 50% EU-27). Another factor mentioned that places Austria above the EU-average concerns the explanation that “working undeclared is common practice in the region or sector of activity so there is no real alternative” (23% vs. 14%).<sup>10</sup>

In representative surveys carried out several times since the mid-1990s almost two thirds (62 %) of people interviewed (January/February 2015) see the hiring of an illegal worker as a mere peccadillo.<sup>11</sup> Key reasons cited for hiring illegal workers included not being able to afford regular workers (70%) and taxes being too high (65%). The time dimension in the data shows that over the past number of years there has been no relevant change concerning the reasons for undeclared work.

### 2.1.3 Estimated scale of undeclared work<sup>12</sup>

For 2015 the shadow economy is estimated at around EUR 21.4 billion which corresponds to 8% of GDP<sup>13</sup>, a slight increase compared to the period 2011-2014. The comparably high unemployment rate and the high tax burden are seen as the main factors contributing to the increase. For 2016 a reduction is expected because of the tax reform which has come into effect in 2016 and reducing the tax burden on labour.

Tax (and social security contribution) losses due to the shadow economy, in 2013 amount to 2% of GDP. Another report for the construction sector calculated tax and social security losses due to bogus companies amounting to EUR 508 million annually.<sup>14</sup>

#### The development of the shadow economy in Austria from 1990 to 2015

	EUR billion	% of official GDP
1990	6.1	5.5
1995	12.3	7.3
2000	19.7	10.1

<sup>10</sup> Other reasons are more or less in line with the EU average. In total, 5 % of Austrian respondents said, that they had undertaken undeclared work in the last year. The most important activities are ‘repairs or renovations’ (34 % vs. 19 % EU-27) and helping moving house’ (30 % vs. 7 % EU-27) (cf. European Commission 2014).

<sup>11</sup> Schneider, Friedrich ‘A renewed increase of the shadow economy in Austria in 2015 and the adjustment of the Austrians’ (‘Ein erneuter Anstieg der Schattenwirtschaft (Pfus) in Österreich in 2015 sowie die Einstellung der ÖsterreicherInnen dazu’) Linz, 2015.

<sup>12</sup> In Austria two main methods are used. Schneider calculates the size of UDW on the basis of a combination of the MIMIC method and the currency demand method and is using parallel direct methods. (cf. also COM(2014) 221 final} {SWD (2014) 137 final). The second approach is used by Statistics Austria, based on the discrepancy method. The main purpose of the adaptation of National Accounts is not the estimation of certain aspects of UDW, but to receive a sound revision of nation accounts according to the EU regulations. According to press reports, the estimate for the value of the black economy and illegal production in 2013 was around EUR 11.4 billion (of which “illegal production”: 460 million), which means an extra amount of 3.7 % of GDP (cf. e.g. www.finanzen.at/nachrichten/aktien/Stichwort-Das-Bruttoinlandsprodukt-inklusive-Schattenwirtschaft-1000298232).

While results of the National Accounts are not published regularly, results calculated by Schneider are available annually.

<sup>13</sup> Schneider, 2016.

<sup>14</sup> Hye, Raphaela et. al., ‘Social fraud by bogus companies in the construction sector. An assessment of the economic damage’ (Sozialbetrug durch Scheinfirmer im Bauwesen. Eine Einschätzung des volkswirtschaftlichen Schadens’), Report of the Institute for Advanced Studies on behalf of the Federal Ministry of Labour, Social Affairs and Consumer Protection, Vienna, 2015.



2005	22.0	10.3
2010	20.3	8.1
2015*	21.4	8.1

Source: Schneider 2016; \*estimated

Further information, like a breakdown along different types of UDW, is not available.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing undeclared work & Characteristics of the responsible organisations

Several ministries and institutions are involved. The most central ones are: the **Financial Police**, which is the national anti-fraud unit in the **Federal Ministry of Finance** (BMF) and, aside from ensuring tax supervision, is responsible for several regulatory policy measures, in particular labour market tasks (e.g. illegal employment of foreign workers) as well as controls under the Social Welfare Fraud Act and LSD-BG (cf. for more details: <https://english.bmf.gv.at/combating-fraud/Financial-Police.html>). The number of controls and the number of staff number in the Financial Police is repeatedly discussed in the political debate. Several actors request an extension of the staff in order to carry out more inspections. Currently, the Financial Police employs around 500 persons.<sup>15</sup>

The **Federal Ministry of Labour, Social Affairs and Consumer Protection** (BMAK) is responsible for labour market immigration issues, the general social insurance law (ASVG) and the LSD-BG, where the Centre of excellence (LSDB) at the **Vienna Regional Health Insurance Fund** was established as a main authority in the context of controlling underpayments. It cooperates closely with the Financial Police (in the case of foreign cases) and the other regional Health Insurance Funds (in the case of domestic cases). Furthermore cooperation exists with the **Construction Workers Leave and Severance Pay Fund (BUAK)**, which is mainly responsible for identifying and preventing UDW in the construction sector.

The **Austrian Health Insurance Institutions** are responsible for collecting contributions for all branches of Austrian social security as well as a wide array of other wage-dependent levies. In this respect, the health insurance institutions not only act as a "payment hub" by forwarding the respective contributions or levies to the corresponding institutions; they also legally represent those other institutions in all collection-related matters, e.g. recovery or liability-proceedings, bankruptcy proceedings or even criminal proceedings. In order to ensure compliance with contribution obligations they audit employers together with the fiscal authorities in the framework of a joint audit of wage-dependent levies (GPLA – Gemeinsame Prüfung lohnabhängiger Abgaben) and have the power to initiate inspections on an ad-hoc basis, where they are frequently confronted with different types of undeclared work.

The **Public Employment Service (PES)**, responsible for inspections under the AuslBG in the context of issuing employment permits, checks to ensure that the employer complies with the given payment and working conditions including social security rules (Act Governing the Employment of Foreign Nationals - AuslBG §4 (1) Z 2) and similarly, that they comply with the given rules in the context of issuing posting permits (cf. <https://english.bmf.gv.at/combating-fraud/Cross-border-posting-of-workers-in-the-EU.html>).

<sup>15</sup> Cf. several press information's, e.g.

<http://diepresse.com/home/politik/innenpolitik/4927258/Mehr-Personal-gegen-Finanzbetrug-aber-nicht-bei-Finanzpolizei>

**Social partners** play an important role in the legislative process as well as in providing counselling for employees and employers, like in the help-desk 'UNDOK' recently set up for un(der)documented workers, founded by trade unions.

### **2.2.2 Cooperation and collaboration between authorities and cross-border authorities**

As mentioned before, several institutions are involved and the issue of cooperation and collaboration is repeatedly discussed with the aim of strengthening the interfaces and establishing enhanced information flows. Under the law of combating social security fraud (Sozialbetrugsbekämpfungsgesetz – SBBG; taking effect by 2016) cooperation between the relevant institutions will be intensified, especially through the establishment of a 'social fraud database' for the purpose of detecting and easier identification of fraud cases under §§ 153ff of the Criminal Code.

Collaboration between the finance administration and the social security institutions has been happening since 2003 in the joint audit of all wage-dependent levies (GPLA). This process also includes the inspection of underpayment in the case of national employers according to the LSD-BG.

Other forms of cooperation are for example the establishment of a construction-site database. In 2012, BUAK in cooperation with the Labour Inspection and the Labour Inspectorate for Transport started a web application for the announcement of construction-sites which, among others things, facilitates targeted inspection activities.

In support of un(der)documented workers the counselling centre "undok" was established in 2014 by several trade unions, the Chamber of Labour and several NGOs (see, [www.undok.at](http://www.undok.at)).

Besides the cooperation of national authorities, the cooperation between the Member States of the European Union is frequently discussed as problematic. One problem is for example that a company with a legal violation detected in Austria or bogus companies can still operate in other EU countries. In general cooperation between Member States is described by experts as not guaranteed and is extremely resource-intensive (concerning time and costs) (cf. for example in the context of LSDB-G: Schmatz/Wetzel 2014).

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

In Austria, several measures exist to tackle UDW and discussions about further improvements and reforms are ongoing. These existing measures are varying in their scope, beside regulations addressing all economic sectors also sector-specific measures (in particular for construction sector, which is comparable highly affected by UDW) exist. It is a mix of measures aiming to deter and to enable compliance.

### **2.3.2 Measures to tackle UDW**

The table below provides a summary overview of measure to tackle UDW in Austria.

#### **Overview of measures to tackle UDW**

<b>Deterrence approaches</b>	Law against wage und social dumping (Lohn- und Sozialdumping-Bekämpfungsgesetz, LSD-BG)
	Law combating social security fraud (Sozialbetrugsbekämpfungsgesetz – SBBG)
	Customer Liability Act

	Reporting obligations (e.g. BUAK: reporting of the extent and the location of the working time of part-time workers)
	Prohibition of envelope wages in the construction sector
	Mandatory cash register rule
<b>Enabling approaches</b>	Reform of the Federal Procurement Act 2015
	Tax Reform 2015 - Easing the income tax burden
	Funding of craftsmen service provision
	Construction site Database
	Service Voucher
	Counselling for workers concerned – UNDOK

The **Law against wage und social dumping** (LSD-BG) introduced penalties, particularly if the employer does not pay the employee's remuneration as stipulated in collective bargaining agreements. Penalties are also imposed if relevant employment contracts do not exist. With the new LSD-BG customer liability rules were tightened, e.g. by establishing a contractor liability for the building sector to hedge wage claims of cross-border posted or temporary workers. If foreign construction workers are underpaid by their company, they can make their claims to the Austrian contractor. Customer liability rules are also defined in the **law combating social security fraud** (SBBG). Contracting companies are liable as a guarantor and payer from the date of the final determination that a company is a bogus company. The liability rules apply to all claims paid for services of employees. This was an important extension, as so far liability rules (**Customer Liability Act**, AuftraggeberInnen-Haftungsgesetz<sup>16</sup>) had focussed on the construction sector only. In general, the law aims to reduce social fraud by several measures, like new and intensified cooperation structures between relevant institutions (cf. above), easier mechanisms to identify bogus companies and by reducing misuse of e-cards, mainly through increased monitoring. To combat bogus self-employment legal certainty concerning the delimitation of self-employed persons and employees was created with the **Social Insurance Allocation Act** (Sozialversicherungs-Zuordnungsgesetz, SV-ZG: partly in force since 1<sup>st</sup> of July 2017). In the future, the type of employment, i.e. "new self-employed persons" and certain groups of operators of a free trade, will be determined with binding effect by the Social Security Institutions in advance.

**Reporting obligations** exist in different ways. One measure addressing a specific form of UDW - bogus part-time work – was introduced in the construction sector. The BUAK observed a rising number of part-time workers.<sup>17</sup> Since 2014 the extent and the location of the working time of part-time workers, including any changes, has to be reported to the BUAK. Also in the construction sector, a **prohibition** of envelope wages, **wages paid cash-in-hand**, was introduced within the framework of the tax reform by 2016 to reduce the possibility of paying fictitious wages and undeclared wages.

<sup>16</sup> Bartos, Beatrix, 'The new contractor liability in the fight against social fraud' (,Die neue Auftraggeberhaftung im Kampf gegen Sozialbetrug'), Internet; [www.hauptverband.at/mediaDB/MMDB136509\\_Bartos\\_Auftraggeberhaftung1.pdf](http://www.hauptverband.at/mediaDB/MMDB136509_Bartos_Auftraggeberhaftung1.pdf), Vienna.

<sup>17</sup> In the 2nd quarter of 2011 (start of high season in the construction sector) the part-time quota for 'Building and related trades workers, excluding electricians' stood at around 3 % and climbed to over 6 % in 2014. In 2015 a reduction to 5 % was observed.

Furthermore the tax reform 2015 brought the introduction of a **mandatory cash register** as of 2016. All businesses must record their cash sales electronically when they exceed the threshold of EUR 15 000 revenues and EUR 7 000 cash revenues per year. For such cases, electronic cash register systems must be in use and should reduce the possibility of undeclared money transactions.

**Enabling approaches** also exist. **Easing the tax burden on labour** in the framework of the tax reform 2015 can be seen as a preventive measure in the context (cf. EEPO Annual Policy Update, September 2015).

The reform of the **Federal Procurement Act** 2015 brought some relevant changes with the aim to combat more effectively wage and social dumping in public procurement. The use of subcontractors gets more regulated and controlled. For certain services (e.g. construction contracts from a value of EUR 1 million) the award must be given to the bid which is most economically advantageous instead of the bid with the lowest price.

In 2014 and 2015 **funding of craftsmen service provision** existed. The costs for refurbishment and modernisation of flats and houses of private persons were subsidised, if the work was carried out by licensed craftsmen. Only labour costs were eligible but no costs for materials. The subsidy amounted to 20% of the labour costs up to a maximum of EUR 600. Currently a re-introduction of the provision is being discussed. The measure showed a high take-up rate, but also according to an evaluation, deadweight-effects. At the same time another study indicated it led to rising tax revenues.<sup>18</sup>

In 2012 a **construction site database** was implemented (as already stated above). Beside the BUAK and Labour Inspection, also the finance police and the health insurance providers have access to the data, so that in sum targeted and planned checks and controls can be more easily carried out.

**Service Vouchers** introduced in 2006 aim to legalise work in private households. Private employers can purchase service cheques at post offices and tobacconist shops and use them to remunerate housekeepers, who are so-called marginal part-time employees. Employees remunerated via the service voucher are covered by work accident insurance and have the opportunity to opt-in to health and pension insurance. However service cheques are being used to a much lesser extent than expected, even if the number of purchased vouchers is rising year by year. In 2014 nearly 250,000 cheques were issued, compared to 98,000 cheques in 2006. The number of employees using a voucher in 2014 was 7,650 and therefore increased by more than three times compared to 2006 (2,067 users)<sup>19</sup>.

As already mentioned, UNDOK, is a relatively new initiative to support un(der)documented workers in Austria. Within the first year of activity nearly 150 persons used the offer.<sup>20</sup>

### 2.3.3 Good practice

Austria has established a distinct regime of control with regard to wages, connected tax and social security contributions. The cornerstone is the **LSDB-G**, which is seen by experts of different sectors as an essential foundation against dumping practices and UDW, with preventive and universally beneficial effects.<sup>21</sup> Ongoing analysis and improvements are essential to ensure effectiveness. Since the law came into force

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<sup>18</sup> Reports are not published. Internet: <http://derstandard.at/2000029006842/Kraeftiges-Lobbying-fuer-einen-Handwerkerbonus-neu>.

<sup>19</sup> BMASK, 'Active labour market policy in Austria, 1994-2013' ('Aktive Arbeitsmarktpolitik in Österreich 1994-2013, Vienna, 2013, and BMASK, 'Active labour market policy in Austria' ('Aktive Arbeitsmarktpolitik in Österreich 2015, Documentation, Vienna, 2015.

<sup>20</sup> UNDOK, 'Summary – 1 year UNDOK' ('BILANZ – 1 JAHR UNDOK-ANLAUFSTELLE'), Vienna, 2015. Internet: <http://undok.at/wp-content/uploads/2014/06/Bilanz-1-Jahr-UNDOK-Anlaufstelle.pdf>

<sup>21</sup> Riesenfelder/Schelepa/Wetzel 2013, Schmatz/Wetzel 2014

(2011), thousands of reports relating to underpayment have been documented, affecting more than 7,000 workers<sup>22</sup>. Final decisions relating to underpayment affect around 2,300 workers, the sum of penalties amounts to EUR 7,318,190. Additional EUR 6,049,698 was imposed due to non-cooperation with control authorities or missing employment documents.

In 2013 the Main Association of Austrian Social Security Institutions (Hauptverband der österreichischen Sozialversicherungsträger) established a monitoring system called **DBENTS**, to offer institutions more effective assistance in relation to conducting checks and combating abuse concerning the posting of workers. Key features are the fully electronic recording of all incoming PD A1 and storage and archiving in a central database, which can be accessed only by authorised individuals and a search function for the competent Austrian social security institutions.

### **2.3.4 Challenges and barriers**

Several challenges to tackling UDW exist. Amongst other reasons, it is often argued that a too high tax burden on labour leads to UDW, and it is too early to say whether the tax reforms will lead to a reduction of UDW. Schneider estimates for 2016 a reduction of UDW by around EUR 2 billion.<sup>23</sup>

Other main challenges are:

- Effective enforcement through better cooperation between authorities.
- Cross-border cooperation, especially for inspection services, allowing them to establish the authenticity of a particular PD A1 but also concerning, for example, joint activities.
- Improved cooperation and collaboration between MS in detecting undeclared work and enforcing workers' rights.
- On the employee-side, a lack of knowledge about their rights, the fear of losing their jobs (e.g. an underpaid job in Austria will be better than having no job in the home country), or even the knowledge of their unlawful employment situation can discourage workers from demanding their right. Low-threshold (multilingual) information and counselling offers e.g. 'UNDOK' help desk, are important in this context.

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<sup>22</sup> Latest available data for the period: 01.05.2011 - 30.11.2016

<sup>23</sup> Schneider, 2016

## Factsheet on Undeclared Work – BELGIUM (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

Belgian legislation does not provide a precise definition of undeclared work. However, a general definition of undeclared work may be found in the Belgian Social Criminal Code. The latter defines undeclared work as “*all work done in contravention to social legislation under the competence of federal authorities*”<sup>24</sup>.

In order to develop a sectoral policy, the Federal Public Service Employment, Labour and Social Dialogue has established partnership agreements with social partners in specific sectors. These sectors are: the construction sector, the metal construction sector, the cleaning sector, the transport sector, the security sector, electro technical sector, garages, the green sector (agriculture, horticulture), funeral sector and removal sector. These partnership agreements allow social partners to negotiate the implementation of specific measures at the three different steps in the fight against undeclared work (prevention, detection, repression). If the legal definition does not fit the operational environment of these sectors, the social partners are allowed to adjust the definition.

#### 2.1.2 Characteristics of undeclared work

The main types of undeclared work in Belgium are:

- Undeclared work performed by foreign workers in an irregular situation;
- Undeclared work performed by Belgian workers or legal residents;
- Undeclared work performed by Belgian workers or legal residents who benefit from social allowances as integration allowance and social assistance;
- Partially undeclared work performed by Belgian workers or legal residents;
- Undeclared work performed by Belgian workers or legal residents with a false status (bogus self-employment, volunteers or trainees); and
- Work of a self-employed person who does not declare all his income to the tax administration.

The main broad sectors where undeclared work is found in Belgium are the **construction sector** and the **HORECA sector** (Hotels, Restaurants and Catering). The **meat processing sector** is also an important contributor to undeclared work. The government pays particular attention to construction, **cleaning, passenger transport** and **security sectors** by concluding sectoral agreements with the social partners.

There are no recent data about undeclared work distributed by employer size, or about the motivators for undeclared work.

#### 2.1.3 Estimated scale of undeclared work

Currently, Belgium does not have any available data on the scale of undeclared work and no recent estimations have been conducted. Nevertheless, there is a project of the Federal Public Service (Social Security) to create an observatory “OBSOE” on the underground economy<sup>25</sup>. On the other hand a country report for Belgium made for the ILO provides more detail<sup>26</sup>.

Nevertheless the data collected by the judicial district cells provide the number of infractions and positive controlled cases. These figures only give an estimate of the different types of undeclared work among the controlled population by the different bodies involved in the control process, and since these controls are not random no statistical inference is possible. But some figures are noteworthy: out of 15,001 controls in 2014, 7,060 infractions considered as undeclared work have been registered, mainly

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<sup>24</sup> Social Penal Code, Article 1, § 1

<sup>25</sup> Internet : <http://socialsecurity.belgium.be/fr/ampleur-de-la-fraude-sociale-et-fiscale-sublec>

<sup>26</sup> [http://www.ilo.org/labadmin/info/WCMS\\_224578/lang--en/index.htm](http://www.ilo.org/labadmin/info/WCMS_224578/lang--en/index.htm)

in the HORECA, building, auto garages and cleaning sectors of activity, for which the rate of positive controls was over 40%.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing Undeclared Work

At the federal level, two bodies were established by the Royal Decree of 29 April 2008 to tackle undeclared work, namely the Ministerial Committee and the College. On the one hand, the Ministerial Committee for the fight against fiscal and social fraud is chaired by the Prime Minister and features members of the government. On the other, the College for the fight against fiscal and social fraud is chaired by the Secretary of State.

Each year, the College establishes an action plan<sup>27</sup> which is submitted to the Ministerial Committee for approval, which defines the overall policy and the priorities of the inspection services. The Committee also ensures the uniform application of law in the country.

The Social information and Investigation Service<sup>28</sup> (SIRS) was established in law on 27 December 2006 and in 2010 consolidated in the Social Criminal Code. As a coordinating body, this service supports federal social inspection services to address UDW, and can be considered as "a single point of contact". It prepares protocols for collaboration between the Federal Authority and the Regions to organise the fight against illegal work and social fraud. It makes proposals to the relevant ministers to develop the legislation applicable in the context of the fight against undeclared work.

In Belgium, the fight against undeclared work and social fraud is primarily the responsibility of the federal social inspection authorities:

- Federal Public Service Social Security (i.e. FPS Social Security) acts to ensure correct reporting of remuneration of employees to social security. This service is organised territorially into nine "regions". This inspection service has been integrated in the inspection service of the National Social Security Office from 1<sup>st</sup> July 2017 onwards.
- Federal Public Service Employment (i.e. FPS employment) is involved in relationships between an employer and its workers. This service is organised territorially into 22 divisions.
- National Social Security Office responsible for the administration of social security, and checks whether employers correctly report the remuneration of their employees.
- National Employment Office checks the compliance of statements relating to unemployment insurance, career disruptions and early retirement. There is an inspection service by regional unemployment office.

There are also other social security public institutions which are involved in the fight against undeclared work, specifically in relation to fraud in social benefits such as the National Institute for Health and Disability Insurance<sup>29</sup> and the National Institute for the Social Security of self-employed for contribution fraud.

At the regional level, the regional inspectorates of the Walloon Region, the Brussels-Capital Region, and the Flemish and German-speaking community are responsible for regionalised social legislation, such as the granting and monitoring of work permits to foreign workers employed in Belgium. Except for the control of foreign workers, these regional services have no specific competence regarding undeclared work and social fraud, which remains at the federal level.

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<sup>27</sup> Internet: <http://www.sirs.belgique.be/siodsirs/publicationDefault.aspx?id=43619>

<sup>28</sup> In French : Service d'Information et de Recherche Sociale (SIRS).

<sup>29</sup> In French: Institut National d'Assurance Madaldie-Invalidité (INAMI).

Finally, there are the 21 local cells<sup>30</sup> which conduct inspections against fraud concerning social contributions and social benefits. Each cell is composed of a representative of the various federal inspection and regional services, a representative of the FPS Finance, a magistrate of the King's public prosecutor, and a member of the Federal Police. It may also have representatives of other public institutions of social security and regional inspection services. Each year, targets are set for the cells in the national action plan adopted by the College and approved by the Ministerial Committee. The results were very positive in 2016, with minimum targets for the overall total frequency of checks being exceeded (i.e. 11,000 against the 9,000 requested).

### **2.2.2 Characteristics of responsible organisations**

This information is included in Section 1.2.1 above.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The SIRS has participated in the establishment of international collaboration between inspection services. For example, the Declaration Benelux against cross-border social fraud<sup>31</sup> was signed on 23 September 2015. Under this, Belgium, the Netherlands and Luxembourg will work together (via data exchange and joint inspections) against social dumping, undeclared work and other social fraud.

As mentioned above, the FPS employment has developed a sectoral policy to deal effectively with undeclared work. Partnership agreements have been concluded with representatives of specific sectors (i.e. the construction sector, the meat sector, the cleaning sector, the transport sector, childcare services). New partnership agreements are being prepared particularly in the HORECA sector. These partnership agreements received legal and structural framework with the creation of the Partnership Commission (i.e. federal agency). The latter prepares the partnership agreements between the relevant ministers and professional organisations. In this way, the social partners are involved in the three stages of the fight against undeclared work: prevention, detection, targeted repression. The SIRS is responsible for monitoring the implementation of partnership agreements concluded by the ministers.

There is also a special collaboration between the Inspectorate of the Social Security Office and the Control of Social Law of FPS Employment in order to implement structured and coordinated checks in each local district. Similarly, some initiatives have been developed to ensure more effective cooperation with the police, the judicial authorities, etc.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The general policy against undeclared work, and more extensively the fight against social fraud and social dumping is defined each year in an Action Plan for the fight against social fraud and social dumping that covers the actions of the cells judicial district, the SIRS and the different inspection bodies. The strategic plan foresees a programming of the controls based on the risks. The analysis of these risks and their evolution shows that the risks needing a multidisciplinary approach are increasing. Social dumping and transnational social fraud is considered in the action plan as the biggest challenge for the inspection services. It concerns mainly the irregular use of posted workers.

As explained above the Social information and Investigation Service <sup>32</sup> (SIRS) can be considered as "the single point of contact". It is composed by representatives of the different bodies involved ( Social security administration, federal police, social partners ( trade-unions and employers' association), public federal services of employment, social

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<sup>30</sup> Program law of 27 December 2006.

<sup>31</sup> Internet : [http://www.benelux.int/files/8914/4308/2200/M20157\\_FR.pdf](http://www.benelux.int/files/8914/4308/2200/M20157_FR.pdf)

<sup>32</sup> In French : Service d'Information et de Recherche Sociale (SIRS).



security and finance, justice court). The SIRS in itself does not have any role in controlling. It acts mainly as a coordinating body of all the different control bodies of the different administrations concerned with social fraud. The role of the SIRS is to execute the policy defined by the Council of Ministers.

### **2.3.2 Measures to tackle UDW**

As stated in the 2016 Action Plan, this plan also constitutes the integrated action plan "social fraud" included in the government's agreement. The 2016 Action Plan defines 90 measures covering not only the different forms of undeclared work but also everything that may be considered as social fraud in relation to different social security or social assistance benefits. It also concerns the application of some aspects of the labour law (bogus self-employed status, false employment contracts).

The fight against undeclared work remains organized around targeted sectors: Horeca, building and cleaning. These three sectors represent about 60 % of the controls operated. But other sectors have been identified: meat sector, transport, garage, manufacturing, taxis, horticulture, retail trade, craft bakeries.

Concerning the HORECA, the introduction of the so-called BlackBox that is compulsory in the sector should have a direct effect on the use of undeclared work. The control in this sector will have a deterrent dimension, as usual, but also a training dimension. The daily control and registration of the workers will be extended in the critical sectors like the meat sector. Specific controls and measures will be also introduced for the transport of goods, the taxi and private transport of persons.

Besides the usual undeclared work, a growing attention is devoted to the misuse of posted workers. Among the 90 "actions" of the Action plan 2016 and 2015 about one third are related with the misuse of posted workers. A committee against social dumping has been created and has to develop new strategies against fraud. The measures may be organized following the following directions:

- Optimization of the use of existing databases, extension of these databases and intensive use of datamining and data matching with the objective of a better targeting of the controls;
- Conclusion of partnership agreements and organization of roundtables with the social partners in the critical sectors;
- Intensification of European collaboration and trans-border collaboration, participation to the European Platform for Undeclared Work; and
- Creation of the Social Dumping Committee with the objective of elaborate new strategies and instruments against social dumping.

The only performance or efficiency indicators available are the results of the controls operated in the different sectors: 37 % of the controls ended with a positive control, meaning that a repressive or administrative sanction or action has been taken. (Cellules d'arrondissement-statistiques 2016 –SIRS).

### **2.3.3 Good practice**

Examples of good practice in addressing undeclared work in Belgium are provided below.

#### *The BlackBox in the HORECA sector*

Since 2016 a new system has been introduced in the restaurants of the HORECA sector. This requires all restaurants to be registered by the use of a so-called Black Box, which registers customer orders as soon as the bill is paid, whatever payment mechanism is used. The objective is to avoid fiscal evasion. The content of the Black Box is directly transferred to the employers' accountants and may be controlled by the administration. The Black Box also registers the amount of worked hours of the staff who serve clients.

### *Extensive use of datamining for identifying the risk sectors and firms*

The use of datamining allows the improved identification of specific sectors and/or firms where the risk of social, fiscal fraud or undeclared work is high. The use of datamining has been associated with an increase of the number of controls and inspections.

### *Sectoral roundtables, action plans for fair competition and partnership agreements*

The pressure of social dumping is rising with the use of posted workers. The use of roundtables and partnership agreements can lead to restricted social dumping, since employers' and employees' organisations have common interests in this field.

### *Flash inspections*

On a regular basis the local cells carry out so called national 'flash inspections' in different economic sectors (such as construction, catering, transport, etc.). These sectors are at particular risk of undeclared work, and employers should be made aware that this behavior is unacceptable.

Therefore these announced inspections (on the SIRS-website and in the press) on compliance with social legislation have a particularly adverse effect on the perpetrators to realize that the risk of being caught in breaches is real. This awareness must eventually lead to a mentality and behavioral change in order to better comply with social legislation. The usual unannounced controls will of course continue unabated and severe social fraud will be tackled rigorously.

### *E-GOV network*

A very strong e-GOV network (Crossroad bank for social Security, crossroad bank for enterprises, etc.) with big data are available as well as a strong online collaboration platform. Enforcement bodies have secured access to all of them for daily use.

### *Social Criminal Code<sup>33</sup>*

All infringements on labour law, safety and health and social security law are described in a uniform and logic way, kept up to date with the corresponding sanctions, administrative and criminal proceedings, competences and investigation powers of social and labour inspectors. To complement this, a system of online electronic penal reports has been put in place ("e\_PV"). All relevant services, inspectors, public prosecutors, service of administrative fines, have access. A database "Ginaa" (with detailed follow-up regarding prosecution and conviction up to the final payment of fines) is also available.

### *Prohibition of payment in cash for wages and salaries*

At the end of 2016 payment in cash became prohibited as a general rule. Only few exceptions are still allowed.

## **2.3.4 Challenges and barriers**

The strategy of a targeted approach limits the efficiency of the fight against UDW, even if the use of datamining will help to concentrate on the most risky sectors or firms. As quoted at the beginning of the Action Plan the measures and actions will depend on the budgetary decisions and constraints. One of the barriers is certainly the size of the human resources implied in the controlling operations: 900. This number must be compared to the number of potential 'at risk' population of employees, self-employed, posted workers, posted self-employed.

One should also keep in mind that the Action Plans are not only concerned with undeclared work of different types, but also with social fraud in a broad sense: misuse of social security or social assistance allowances.

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[http://www.ejustice.just.fgov.be/cgi\\_loi/change\\_lg.pl?language=fr&la=F&cn=2010060607&table\\_name=loi](http://www.ejustice.just.fgov.be/cgi_loi/change_lg.pl?language=fr&la=F&cn=2010060607&table_name=loi)

The most important challenge is the social dumping often implied by the use of posted workers.

## **Factsheet on Undeclared Work – BULGARIA (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

In Bulgaria there is no common definition of undeclared work (UDW) adopted and applied nationally – with no single definition in law and with different responsible authorities having different understandings what encompasses UDW (as illustrated in 1.1.2 below). Undeclared work is broadly considered as a significant part of the informal (shadow) economy, which comprises lawful economic activities for the production and exchange of goods and services, but which avoids state regulation, taxation, social security contributions and control.

#### **2.1.2 Characteristics of undeclared work**

The main types of undeclared work in Bulgaria, are, according to the annual reports of:

- The *National Revenue Agency (NRA)* at the Ministry of Finance (MF): working without a labour contract, with a contract with a lower official wage than the real wage; recruitment under, or at the minimum insurance threshold for the respective job; or declaring labour contracts as part-time work instead of the real full-time employment; and
- The *General Labour Inspectorate Executive Agency (GLI EA)* at the Ministry of Labour and Social Policy (MLSP): an employment relationship without a written labour contract; labour contracts not registered in the NRA; undeclared work based on false calculation of working time that does not account for night, holiday and extra hours work; 'envelope wages'.

The main broad sectors where undeclared work is found are: wholesale trade and retail (food, garments, textiles); agriculture, food processing; services (repairs, advertising, accounting, waterproofing of buildings, funerals, taxi, security); trade in food commodities (grain, sugar, etc.); production and distribution of excise goods (cigarettes, fuels, alcohol); construction, real estate sales; tourism, hotels and restaurants and transport.

In terms of employer size, undeclared work is mostly found in micro-, small- and medium-size enterprises, sole traders and self-employed, mostly located in small/medium towns and in rural areas (Dzekova, R. (2014); Nonchev, A. (2011)<sup>34</sup>).

The relatively high unemployment and poverty rates, and insufficient disposable incomes, are key motivators for undeclared work, and while reforms of the pension and health systems are ongoing their progress is delayed. As far as the 10% tax flat rate was introduced, there are no specific incentives or alleviations for low-income groups of the population or for micro- and small enterprises.

#### **2.1.3 Estimated scale of undeclared work**

The NRA provides information on taxes and social insurance contributions that are incorrectly declared and the impact on the budget resulting from their non-payment. In 2014 GLI EA reports about violations such as regulations governing formation, modification, implementation and termination of employment contracts; distribution of working time and labour remuneration. After 2013, the key performance indicators are improving. This general trend results from improvements in the organisation of the work of the NRA and GLI EA and the cooperation between the tax, labour and social security public authorities.

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<sup>34</sup> Nonchev, A. (2011) Dynamics of the Hidden Economy in the period of Crisis. Internet: [www.csd.bg/fileSrc.php?id=20590](http://www.csd.bg/fileSrc.php?id=20590)

- The National Statistical Institute (NSI) applies the tabular approach for the purpose of exhaustive adjustments of the GDP and GVA. According to Eurostat methodology applied in 2012<sup>35</sup> and further, the initial corrections of the GDP produced in 2011 was by 13.02 % (GDP = EUR 41 693.3 million); and by 15.02 % of the GVA (Kolev, M. 2014<sup>36</sup>). The distribution of this 13.02 % of GDP was as follows: additional income, unincorporated activities and national accounts adjustments – 6.74 %; adjustment for self-employed persons - 1.46 %; adjustment for working without a contract (Labour Force Survey) - 1.39 %; income in kind, private use of business cars, tips - 1.79 %. Some pieces of that information as the adjustments for the self-employed and incomes in kind and tips could be used for UDW quantifications.
- The 2016 annual research on the hidden economy performed by the Centre for Study of Democracy shows that the index of the hidden economy has decreased (Hidden economy in Bulgaria, 2016), and at the lowest level between 2002 and 2016.

The Risk Management Directorate of the NRA has carried out a risk analysis related to the concealment of employee wages. The mechanism used for concealment comprises the conclusion of employment contracts with lower salaries than those actually paid and / or with fewer than the actual working hours (usually labour contracts for 4 hours or less), which result in the declaration and submission of lower social security contributions and income tax. A peculiarity in this case is the participation of both parties (employer and worker) in the process of concealing real wages. According to the analysed data, the average annual loss amounted to approximately BGN 440 million, and involved on average approximately 35,000 employers, representing about 47% of the risky employers.

Risk characterization data for 2010-2015 is shown below:

<b>Year</b>	<b>Relative share of risky employees</b>	<b>Relative share of risky employers</b>	<b>Total potential damage (taxes + social contributions) (in thousands of BGN)</b>
2010	53.79%	47.50%	441,054
2012	59.33%	48.04%	375,539
2013	58.79%	47.60%	363,685
2014	58.71%	47.64%	469,173
2015	58.50%	47.49%	426,976

The NRA has not investigated the risk of tax evasion and social security contributions from total undeclared work.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing Undeclared Work**

The key national authorities with responsibilities for identifying, tackling and/or preventing UDW are the NRA at the MF and the GLI EA at the MLSP.

Social partners' organisations are interested in UDW, mainly through participating in working groups with state bodies and implementing projects to tackle the informal economy and UDW.

<sup>35</sup> The methodology was changed in 2016 and new information about the revised GDP and GVA will be published. It will take into account the illegal activities and the black economy.

<sup>36</sup> Kolev, M. (2014). Measuring and Tackling the Undeclared Economy in Bulgaria, Sofia, Power point presentation at a conference on Informal economy and undeclared work in Europe, in States and States of Informality in Europe: Current and Future Perspectives, Marie Curie International Conference Sofia, 4 September, 2014. Internet: [www.csd.bg/artShow.php?id=17041](http://www.csd.bg/artShow.php?id=17041)

There are a few national NGOs which carry out research activities on the informal economy, including undeclared work as a significant part of it. For example, starting from 2002 the Centre for Study of Democracy carries out regular studies on the hidden economy.

The NRA investigates (mainly) on partially or fully undeclared taxes and social insurance contributions. GLI EA controls the implementation of labour legislation and imposes sanctions related to undeclared work. In addition to the work of these agencies the National Social Security Institute (NSSI) deals with social security payments and collects information about them; the NSI collects information on undeclared work for statistical purposes, including that on its impact on gross domestic product (GDP) and gross value added (GVA).

### **2.2.2 Characteristics of the responsible organisations**

The NRA is a specialized body subordinated to the Ministry of Finance for ascertaining, securing and collecting public receivables and determined by the legislation private state receivables. The governing bodies of the Agency are a Board of directors and an executive director. The structure of the Agency includes the Central management and six territorial directorates (TD), namely the TD of NRA Sofia, TD of NRA Plovdiv, TD of NRA Varna, TD of NRA Burgas, TD of NRA Veliko Tarnovo and TD of NRA "Big taxpayers and insurers". There are 28 regional service offices that cover the entire territory of the state. The organisation had 7,686 employees at the end of 2016.

The GLI EA is a subordinate administrator of budgetary funds with responsibilities to control the observance of labour law and legislation in the field of occupational health and safety, promotion of employment, labour migration and labour mobility, in all economic sectors. The GLI EA is managed by an executive director and comprises a general administration, structured in four directorates, and a specialised administration, divided into two directorates and one general directorate. The GLI EA operates 28 regional offices (one in every district town), subordinate to the general directorate. The organisation has 495 employees, including the core staff of 350 persons with the powers to make inspections.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The institutions with functions to deal with UDW cooperate in applying deterrence and enabling measures. The rules and procedures of cooperation are laid down mainly in legislation and in signed cooperation agreements.

In 2009 a Labour Inspection Act was adopted to regulate the functioning of the national labour inspection system (before the Act, the coordination was based on multi- and bilateral agreements). A tripartite Cooperation Agreement No85/29.09.2010 was signed between the NRA, GLI EA and NSSI. Working groups of experts from the three institutions define criteria for the selection of inspection objects/work premises; develop a strategy for joint inspections and rules for the exchange of information. Specific measures are designed and applied for cooperation between the three institutions in the work with employers, employed and self-employed.

In addition to the control activities and exchange of data, public authorities with functions relating to UDW cooperate in applying enabling measures. Examples are a joint campaign carried out by the NRA and GLI EA for the observation of labour, tax and social security legislation among companies located in Black Sea towns, resorts and holiday villages; design and publication of brochures and promotion flyers ('Money in envelope', 'Take a purchase receipt' and others).

The NRA, GLI EA and NSSI work actively with social partners, particularly for carrying out specific inspections in enterprises.

The institutions adopt internal rules and procedures for organising the exchange of data. Based on signed agreements, regular exchange of data of mutual interest and need is

carried out. Operational data are exchanged in the case of joint inspections and other activities. The GLI EA and NSSI organisations have mutual real time access to databases and registers of labour contracts maintained by the NRA.

GLI EA is the country liaison office and participates in the exchange of information and control under Directive 96/71/EC concerning the posting of workers in the framework of the provision of services, including information on abuses, through the Internal Market Information System (IMI). The Agency is the competent authority under a signed trilateral agreement between Bulgaria, Romania and Greece, as well as under bilateral agreements with other EU member states.

Both NRA and GLI EA participate in international working groups, projects and events at EU level on various issues regarding undeclared work.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The Bulgarian Government applies a unified policy approach for tackling the shadow economy and UDW as a significant part of it. In 2015, the Government adopted a National Strategy on increasing the collection of revenues, tackling the shadow economy and reducing expenditures for the enforcement of legislation 2015-2017. The review of measures in the Action Plan to the Strategy shows that although deterrence oriented measures are prevailing, preventive, curative and promotion approaches are considered in the policy on tackling the informal economy.

### **2.3.2 Measures to tackle UDW**

An amendment to the Labour Code laid down the obligation for employers to register signed labour contracts in the NRA within three days and to register termination and any change in the position or term of the labour contract within seven days. The penalties for violation of this obligation are very stringent, for example in the case of a second violation by an employer, with an established person working without a labour contract, the GLI EA is entitled to suspend operations at the work premises. On the initiative of the GLI EA, in July 2015, by amending the Labour Code, a daily labour contract was regulated for seasonal work in the agriculture sector. The measure became popular among farmers.

Other measures introduced: minimum social insurance thresholds by economic activities; reduction of all payments in cash to a maximum threshold; introduction of the opportunity through the website of the NRA for the electronic declaration of taxes and social security contributions; and compulsory connection of all fiscal devices of economic actors with the NRA system. Electronic services are provided through which individuals and employers receive information about: the employment contracts declared by the respective employer in the NRA, and about the social insurance data provided to the NRA. In 2014 the NRA introduced an integrated information system 'Control' and the GLI EA introduced a quality management system for the control activity and an information security system, in accordance with standards ISO 9001:2008 and ISO 27001:2013.

The annual reports are prepared for the implemented measures based on the National Strategy on increasing the collection of revenue, reducing the costs of the shadow economy and reducing expenditures for the enforcement of legislation. On the basis of these reports, an annual implementation plan is drawn up every year.

From the beginning of 2015 employers that hide social security contributions in large sizes for state social insurance or for health insurance for their employees are considered as subjects to crime according to the Criminal Code of the Republic of Bulgaria.

### **2.3.3 Good practice**

As a result of the introduction of daily labour employment contracts for short term seasonal farm workers, NSI data shows a significant increase in the number of employed persons in the agricultural sector in the first half of 2016 compared to the first half of

2015 (before the contracts were introduced). In April 2016, for the first time since 2004, the number of employees in the agricultural sector exceeded 80,000, and throughout 2016 more than 100,000 single employment contracts of this kind were used.

Analysis by the Risk management Directorate in the NRA, related to the concealment of part of the wages of employees, was checked in 2012, 2013 and 2014 through inspections and audits (including over 2,500 inspections over these three years, around 1,850 inspections of natural persons to ascertain facts and circumstances and, approximately 200 audits of risky employers).

The assessments of the risk treatment have shown that the overall control measures were not particularly effective and have resulted in a negligible reduction in social insurance contributions lost over the entire treatment period. Applying statistical analysis found that the effect of the control actions was short term and gradually decreased. It was also found that the overall effect of all measures taken (including providing access to the social security account for all natural persons, raising awareness campaigns among non-controlled persons, media campaigns and the impact of any other control action under which an examination of the facts and circumstances relating to that risk is carried out in accordance with the instructions given for its treatment) was low – around a 3% reduction mainly as a result of measures against traders and builders. In addition, treatment does not reduce the proportion of at risk persons. Some increase of declared wages and/or duration of working daily time was registered, but they were still significantly lower compared than their actual values.

For 2014, the damage increased compared to 2013, which was opposite to the trend in previous years for a gradual reduction in damage. The main reasons for this increase were the changes in the external conditions: there was an increase in the number of employees in risk sectors, an increase of real amount of wages, and also change of legislation leading to the rise of the risk behaviors. From 1<sup>th</sup> of January 2014 in the Personal Income Tax Act has been stipulated the right to refund taxes for a certain number of natural persons who have received only income under employment relationships, not exceeding the amount of the annual minimum wage. This provision negatively affected the behavior of the persons in risk, who have started to declare even lower wages, flattened to the minimum wage for the state. Although the provision was abolished in 2015, it was the main cause of the higher damage to the budget in 2014.

The NRA cooperates and interacts with the other state authorities, applying the administrative principle of the official beginning for the electronic exchange of information, control and assistance in order to reduce the administrative burdens, and optimization of the terms and actions.

The NRA provides technical and information support to the other administrations / authorities regarding the exchange of information and guidelines developed by the NRA e-services - reference for current status of labor contracts, etc. The new electronic services aim to significantly facilitate the exchange of information between the administrative authorities in the country, with the expected end result being a faster and better service to citizens and companies. The increase in the number and usability of these electronic services means fewer visits and the reduced use of paper documents in the local NRA offices.

#### **2.3.4 Challenges and barriers**

Challenges: to improve the awareness of employed persons about labour and social insurance legislation and legal protection of workers' labour and social insurance rights, as well as the confidence in public institutions.

Barriers: lack of confidence in public institutions: procedural fairness and justice, and public trust, have to be restored.



Also the barriers include the overall difficult situation of the economy, unemployment, legislative shortcomings and subsequent deficiencies in the control activities in case of bankruptcy of enterprises.

In order to address these challenges and barriers, initiatives of social partners and other stakeholders are being implemented: Fostering a culture of commitment are the 'Come Into the Light' campaign (2007); and 'Work Legally' campaign (2008). The proactive role of social partners involves research, offering advice, public awareness, education services; services of the National Centre 'Rules for Business' (BICA and CITUB); Virtual Social Academy (BCCI, 2014), etc.

The NRA organizes regular information campaigns on undeclared work. These comprise the "Wages in the Envelope" campaign and the "Get Your Cash Receipt" campaign, which includes a lottery (clients can register their cash receipts to participate in the lottery).

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## **Factsheet on Undeclared Work – CROATIA (July 2016)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

Definition of undeclared work in Croatia follows the definition set at the EU level (any paid activities that are lawful as regards their nature but not declared to public authorities<sup>37</sup>), and is used by all institutions engaged in the design and implementation of activities working towards combating undeclared work.

#### **2.1.2 Characteristics of undeclared work**

Publicly available data on the scope and specificities on undeclared work in Croatia are quite limited and based on different estimates and assumptions. Based on the results of different inspections (please see Section 1.1.3), it can be concluded, however, that most common forms of undeclared work in Croatia include performing business activities without registration, envelope wages and illegal immigrants working. The highest number of violations of the Labour Act in 2014<sup>38</sup> have been recorded in the areas of catering, trade and construction sectors, but no data is available on the distribution of undeclared work by employer size. According to Bejaković (2015)<sup>39</sup>, it can be assumed that the non-payment of taxes and contributions is less common in large companies, primarily because the extent of their operations and the need to run complete accounts and non-cash payments.

Empirical researchers in most cases find the tax burden as the most important determinant of the unofficial economy, followed by the motivation of taxpayers to paying taxes (sometimes referred to as 'tax morale') and quality of state institutions<sup>40</sup>. Bejaković (2015)<sup>41</sup> concluded that the official and underground economy in Croatia are substitutes, working in opposite directions, with the shadow economy increasing as a result of the recession in the period 2009-2010. In that period, the most important factors influencing the shadow economy in Croatia (such as tax moral, tax burden and labour market conditions), according to Bejaković (2015)<sup>42</sup>, worked in the same direction, increasing the share of the shadow economy in the period 2008-2010, opposite to the period 2002-2008, when these were stable. Therefore, it can be concluded that main motivators for undeclared work in Croatia include a low employment rate and lack of work opportunities, as well as relatively high taxes and obligatory contributions on wages.

#### **2.1.3 Estimated scale of undeclared work**

There are different estimations on the scale of undeclared work in Croatia, which range from less than 10 % to more than 30 % of GDP. Schneider (2011)<sup>43</sup> estimated that the

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<sup>37</sup> There is no formal national definition.

<sup>38</sup> Commission for combat against undeclared work (2014). Consolidated report on the measures taken for combating undeclared work.

<sup>39</sup> Predrag Bejaković (2015) A revision of the shadow economy in Croatia: causes and effects, *Economic Research-Ekonomska Istraživanja*, 28:1, 422-440, DOI: 10.1080/1331677X.2015.1059104

<sup>40</sup> Lovrinčević, Z., Mikulić, D., & Galić Nagyszombat, A. (2011). Unofficial economy in Croatia and the impact of the economic recession on the unofficial economy. In Z. Reić & V. Šimić (Eds.), *Conference proceedings challenges of Europe: Growth and competitiveness reversing the trends* (pp. 479–908). Split: University of Split, Faculty of Economics.

<sup>41</sup> Op. cit.

<sup>42</sup> Op. cit.

<sup>43</sup> Schneider, F. (2011), 'Shadow economies all over the world: new estimates for 162 countries from 1999 to 2007', in

shadow economy in Croatia amounted to 30.4 % of GDP; analysis conducted by A.T. Kearney (2013)<sup>44</sup> evaluated that the shadow economy amounted to 28 % of GDP; while the CBS estimate (unofficial data) indicates that it is more realistic that the shadow economy reached 7.4 % of GDP in 2014.

Despite the evident lack of data on the shadow economy and its size in relation to GDP, reports on conducted labour inspections indicate a gradual decrease of cases of undeclared work in Croatia, which can primarily be attributed to the wide scope of different measures designed and implemented to combat undeclared work and the shadow economy in general (please see Section 1.3).

According to the data of the Croatian Labour Inspectorate for 2014, cases of undeclared work have been identified in almost all industries, especially in the hospitality industry, trade and construction. Most common violations detected by the labour inspectors have included:

- employment of workers without an employment contract or delivery of the written confirmation on the concluded contract, in cases where the contract has not been concluded in written form;
- concealing of working relation through conclusion of different forms of contracts (e.g. service contract) for jobs with characteristics which require conclusion of work contracts;
- failure to register workers for mandatory pension or health insurance;
- employment or work of foreigners contrary to the relevant legislation or without application to the competent authorities of pension or health insurance, where required; and
- hiring seasonal workers for temporary of part-time seasonal jobs in agriculture.

In 2014, there was total of 6 853 potential violations of labour regulation reported by the Inspectorate, which resulted in 2 957 misdemeanour charges at competent courts against employers, 258 mandatory misdemeanour warrants and 118 misdemeanour warrants issued, and 55 penalties imposed on the scene. In addition, inspectors have issued 495 decisions on penalties related to an identified 774 workers which were not registered for pension insurance upon commencement of work or were registered with incorrect working hours, and 93 foreign workers who were working illegally. About EUR 292 000 has been paid to the State Budget based on these fines. This data indicate a decrease of detected violations in the area of labour regulation in comparison to the period 2011-2013, when an annual average of 1 321 workers were identified as unregistered for compulsory insurance, and 388 as illegal immigrants.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing Undeclared Work:**

There is no single public organisation responsible for tackling undeclared work in Croatia. Instead of that, responsibility is shared between different ministries and government departments, including:

- Ministry of Labour and Pension System, especially Labour Inspectorate's department;
- Ministry of Finance, especially Tax Administration and Customs Administration;
- Ministry of Interior;
- Ministry of Tourism;
- Ministry of Agriculture; and

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Schneider, F. (ed.), Handbook on the shadow economy, Cheltenham, Edward Elgar.

<sup>44</sup> A.T. Kearney (2013). The Shadow Economy in Europe, 2013. Available at: <https://www.atkearney.com/documents/10192/1743816/The+Shadow+Economy+in+Europe+2013.pdf>

- Croatian Employment Service.

Departments which carry the highest responsibilities in the area of preventing and combating undeclared work in Croatia are predominantly the Labour Inspectorate within the Ministry of Labour and Pension System, as well as the Tax Administration and Customs Administration within the Ministry of Finance in cooperation with Ministry of Interior. Somewhat lower level responsibilities in combating undeclared work are situated within the Ministry of Tourism, Ministry of Agriculture and Croatian Employment Service

### **2.2.2 Characteristics of the responsible organisations**

The Labour Inspectorate carries out inspections and other professional activities in the field of labour and safety at work, performing inspections of the implementation of laws and regulations governing: labour relations and occupational health and safety, obligatory notification, check-out and changes over insurance of workers on the mandatory pension and compulsory health insurance, relations with the employer, preparation of answers and statements to the requirements of the state attorney in civil and criminal proceedings conducted by the applications or proposals for labour inspectors, preparation of reports on inspections conducted and the measures taken, performance of representation before magistrates' courts in misdemeanour proceedings and before the administrative courts concerning actions in administrative proceedings. It also conducted joint actions with the Ministry of Interior in combating the illegal employment of foreigners, and collaborated with Ministry of Finance in surveillance regarding compliance with the minimum wage act and legislation in the field of taxes and social contributions.

The Tax Administration department is responsible for collecting tax revenues. The Tax Administration inside its' organisational structure has a tax inspectorate which controls payment of taxes and unreported income. The Tax Inspectorate also has responsibility to prepare proposals for initiating criminal proceedings and the submission of applications for criminal acts in cases of economic offences such as attempted tax evasion.

The Customs Administration is in charge of inspections and enforcement activities in the fight against the grey economy, with particular emphasis on the supervision of the implementation of regulations governing the trade and the provision of services, and supervision of all forms of unregistered and illegal trade activities. By taking control of affairs in the field of aforementioned unregistered activities, the Customs Administration is also in charge of detecting possible regulations that violate labour regulations. In addition, the Customs Administration is in charge of surveillance of compliance regarding sojourn tax.

The Ministry of Interior in cooperation with the Labour Inspectorate is mainly in charge of combating the illegal employment of foreigners. The Ministry of Agriculture inspects the observance of special regulations in the field of Agriculture, Forestry and Water Management. However, inspectors cannot take concrete measures in combating illegal employment in the agriculture sector except in specified cases where information is forwarded to the Labour Inspectorate.

The Ministry of Science, Education and Sports controls implementation of regulations on job placement for regular students. This should be realised through actions of student centres, which formally are organisational units of public universities / polytechnics in Croatia but with their own legal personality. The Ministry of Tourism is authorised for the inspection of activities by registered entities and individuals engaged in providing services in tourism, but not for detection and prosecution of undeclared businesses in this field, which is a responsibility of the Customs Administration. The role of the Croatian Employment Service in combating the illegal employment is that if an unemployed person from the Croatian Employment Service unemployment register was detected in

undeclared work activity, then penalties in the form of deletion from unemployment register will follow.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

Despite the fact that there are examples of cooperation in data sharing and joint actions, generally there is a lack of coordination among these ministries and departments. That was the main reason why the Croatian Government in August of 2014 has formed one committee in charge of coordinating actions for tackling undeclared work in Croatia. The composition of this committee represented different Ministries which were involved with their responsibilities and measures in tackling undeclared work in Croatia. The following ministries delegated their representatives in this committee: Ministry of Economy, Ministry of Labour and Pension System, Ministry of Finance, Ministry for Crafts and Entrepreneurships, Ministry of Tourism, Ministry of Agriculture, Ministry of Interior, Ministry for Social Policy and Youth, Ministry for Health, Ministry for Science, Education and Sports, Croatian Employment Service and Croatian Pension Insurance Fund. On the other hand it seems that results in terms of creating effective mechanisms for tackling undeclared work in Croatia was not achieved through the work of this 'committee'.

There is no publicly available information regarding any cross-border co-operation of Croatian public bodies in combating undeclared work, so it is quite difficult to deliver any judgment in that direction.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Country Specific Recommendations 2014 identified a high proportion of undeclared paid activity in Croatia and emphasised the need to address undeclared work, recommending to outline plans to tackle the issues of undeclared work by the end of 2014. The Ministry of Labour and Pension System has pronounced 2014 as the year of combating informal employment, which was emphasised through different planned activities, including preventive, curative and repressive ones.

The Commission for Prevention of Undeclared Work was established in 2014 by the Croatian Government. The Commission consists of representatives of thirteen ministries, the Croatian Employment Service and the Croatian Institute for Pension Insurance. A report on the measures taken for combating undeclared work was drafted in 2014, which identified different areas of activity which regulate the measures against undeclared work, including employment in the fisheries sector, student work, combating undeclared work in the field of unregistered business activities etc.

Initiation of more active involvement of the Tax Administration in development and implementation of instruments for combating undeclared work has been planned in 2015, primarily through the adoption of the Action Plan which should have defined the areas of implementation and guidelines for combating all types of earning income by 'moonlighting', without payment of taxes. Implementation of the measures has been envisaged through efficient and close cooperation of the Tax Administration and other institutions in collecting and analysing data essential for identification of correct tax liabilities, which also includes the identification of areas exposed to risk of undeclared employment, measures for combating this form of employment, as well as awareness-raising measures.

Most of the measures tackling undeclared work and the shadow economy in general are based on a deterrence approach, as described in more detail in the following sections. Awareness raising campaigns have been initiated relatively recently, while other measures based on an enabling approach mostly include active labour market policy measures incentivising self-employment and employment in Croatia.

### **2.3.2 Measures to tackle undeclared work**

The Ministry of Finance and Tax Administration implement most of the measures tackling undeclared work, which are based on the deterrence approach. Fiscalisation of cash payments has been introduced in 2013, to ensure efficient oversight over transactions done in cash. These transactions are immediately (via internet) reported to the Tax Administration. Results have been achieved almost immediately, since the reported revenues have increased significantly with the introduction of fiscalisation, especially in catering and other tourism-related business activities. The Act on nannies regulates the mostly informal personal child-care service provision by setting up basic standards allowing persons and firms to register such an activity, and permitting local government to subsidise such services. Since 2014, employers have the obligation to submit a unified form with wage calculations (JOPPD form) to the Tax Administration. The JOPPD form substituted six different forms used before 2014 and enabled the Tax Administration to monitor the payments of contributions, taxes and income of individual workers.

The Ministry of Labour and Pension System is in charge of design and implementation of measures which are primarily based on the enabling approach. These primarily include awareness-raising campaigns on the harmful effects of undeclared work on the economy, as well as design and implementation of the active labour market policies and measures, whose budget and scope increased significantly in 2015, with the support of funding from ESIF. The Act on Employment Encouragement, adopted in 2012, has introduced several new measures aiming to decrease undeclared work. Vouchers have been introduced for temporary and seasonal employment in agriculture, employment procedures have been facilitated for employers, incentives for self-employment have been introduced, as well as different incentives for employment being introduced to facilitate employment and decrease the share of undeclared work in Croatia. The Act on Mediation in Employment and Rights during unemployment stipulates that persons who perform work without a contract or other receipt enabling work activities will be deleted from the registry of unemployed administered by the Croatian Employment Service, and will be able to apply again after six months.

New measures have also been introduced in the area of pension insurance. The Pension Insurance Act, adopted in 2013, has significantly widened the scope of persons with obligatory insurance and introduced shorter deadlines for registration of the commencement, changes, and end of pension insurance, which is now due within 24 hours from the occurrence of the change in pension insurance status. Deadline for registration of the commencement with obligatory insurance is before starting work. Registration procedures have also been simplified with the introduction of obligatory electronic forms and decreasing the number of documents which need to be attached to the insurance registration.

It should also be mentioned that the social care centres and local and regional administration have the obligation to regularly exchange data on the social welfare receivers who are capable to work and who have participated in community services without payment, which is their obligation in line with the Social Welfare Act. Furthermore, the Act on Crafts from 2013 introduced the status of 'secondary profession', which enabled persons who have worked without registration to legalise their business activities.

In the area of tourism-related activities, the Ministry of Tourism has amended the Hospitality and Catering Industry Act and the Act on the Provision of Tourism Services, with the aim of facilitation and simplification of starting a business and combating undeclared business activities and employment in the industry.

The Labour Act reform, completed in 2014, resulted with the adoption of the new Labour Act and several accompanying implementing regulations, which entered into force in August and December 2014, respectively. The main objectives of the new Labour Act include facilitating employment and internal mobility of workers, enabling more flexible business operations and reduction of labour costs, encouragement of more effective and

faster restructuring of employers, as well as facilitating measures against undeclared work.

When it comes to effectiveness of different measures, available data is quite limited. The effects and efficiency of active labour market policies is currently under comprehensive analysis, results of which should indicate the actual effects of all ALMPs implemented in Croatia, as well as the need for their re-design. It seems that largest effects have been achieved with the fiscalisation of cash payments, which significantly increased the reported revenues of the catering industry, as well as the introduction of the JOPPD forms for reporting of paid personal income, taxes and contributions, which enabled a more efficient and comprehensive monitoring and control by the Tax Administration.

### **2.3.3 Good practice**

Probably the best practice in tackling undeclared work in Croatia has been the introduction of cooperation of all relevant ministries in the area, under the Commission for Prevention of Undeclared work. It has proven to be especially important since different ministries and government bodies are responsible for different aspects of combating undeclared work and the shadow economy in general. Since 2014, the Commission has published annual reports on conducted measures combating undeclared work, which provides an overview of activities conducted by all relevant bodies and institutions, and facilitates monitoring of their effect on decreasing undeclared work in Croatia. When it comes to individual measures, two measures should be highlighted in terms of their efficiency – fiscalisation of cash payments and introduction of a single electronic form for reporting of paid personal income, taxes and contributions. Both of the measures have enabled the Tax Administration to more efficiently monitor and control obligations and payment of taxes. In the first year of fiscalisation implementation, a significant increase of reported turnovers and income was recorded in activities that fall under obligation of fiscalisation, with an emphasis on trade and catering activities.

### **2.3.4 Challenges and barriers**

The main challenges in tackling undeclared work in Croatia include a low level of utilisation of labour, which further deteriorated under the financial crisis and long-term recession. Tax and administrative burdens in Croatia are still high, which significantly contributes to the development of the shadow economy, including undeclared work. Over the last several years, significant developments in the area of combating undeclared work have been achieved, primarily through the adoption of relevant legislation, simplification of procedures and centralisation of all activities under the supervision of the Commission for Combating Undeclared work. Significant improvements have also been achieved within the comprehensive labour law reform, which was oriented towards flexibilisation of the labour market, decreasing labour costs and simplification of different employment procedures. However, total labour costs have still remained high for employers, as well as general tax and administrative burdens related to doing business in Croatia. In addition, some of the recently introduced regulations (e.g. working time recording) and their application in practice have been unclear to both employers and relevant institutions, which also contributes to the number of labour regulation violations. Additional simplification of relevant regulations, as well as decrease of labour contributions and taxes could positively influence the decrease of undeclared work. Putting a larger focus on prevention of causes, rather than negative effects of the undeclared work could save on costs of inspections and court procedures.

## **Factsheet on Undeclared Work - CYPRUS (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

The Commission's definition of undeclared work (UDW) is paid, legal, work that is not declared and not reported. In Cyprus, there is a grey area surrounding the term 'legal' in the Commission's definition which should be brought out. An activity could be publicly legal but may violate individual contractual commitments in the terms of employment. For example, publicly employed teachers are not allowed to tutor their own students under a private account, yet private schools employing their own teachers and providing tutoring are perfectly legal. We will refer to this situation as an individually illegal activity. The basic problem is not whether such an activity is reported, but rather that it is not allowed under an individual contract. In the case of public servants, a second employment is prohibited by law.

In Cyprus, there is no official and immutable definition of UDW. Officials from the Ministry of Labour, Welfare, and Social Insurance (MLSI) tend to favour a pragmatic definition which revolves around whether "contributions (to) the Social Insurance Fund are not paid or are paid (for) a lower wage"<sup>45</sup> Some of the discussions that have recently taken place have clearly referred to privately illegal activities, and several widely publicised raids on private homes where tutoring was taking place by publicly employed teachers have occurred over the years. Other examples of privately illegal and undeclared activities include those by publicly employed doctors who may work on their own account, and illegal immigrants and refugee claimants who engage in paid legal activities when they are not supposed to (refugee claimants are not allowed to work in the first six months of presence in Cyprus; after six months, they may work legally in certain pre-specified areas of work).

Most official concern has been about the employment of workers such as illegal immigrants, refugee claimants who engage in paid legal activities when they should not, and the non-declaration of legal work carried out by Cypriot or other legal workers in a paid or self-employed capacity. Abuses of the terms of employment (e.g. requiring workers to work for longer hours than they should) are, in principle, monitored by officials from the MLSI.

Since there is no universal definition of UDW, different organisations with diverse remits will have a different focus. The dominant player involved in monitoring UDW is MLSI; this occurs through the regular supervision of the workplace – see below. Other organisations are also involved and will have a different focus. The Ministry of the Interior deals with work permits, nationality issues, identity cards etc. The Ministry of Finance may shape tax and other policy which may impact on the incidence of UDW, but its focus will be a macroeconomic one. The newly unified tax authorities will be interested in the collection of income and indirect taxes, and their focus will be primarily on the collection of assessed but as yet unpaid tax liabilities by individuals and companies.

#### **2.1.2 Characteristics of undeclared work**

The main types of workers engaged in UDW include: Illegal immigrants who are employed in legal work, such as construction, and receive envelope wages; the self-employed (including a wide range of professions and vocations) whose work is not reported or is underreported, some of which may be in second jobs that are individually illegal; legal paid workers who hold jobs that are not declared and for which no social security contributions are made; and those receiving unemployment benefit and social security who hold jobs that are not declared. The first three groups are likely to account

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<sup>45</sup> This quote was contained in the validation review of the draft sent to the 'nominated representatives of Cyprus'.



for most of the UDW in Cyprus, but no real evidence is available on the total or their relative ranking in importance.

The main sectors where UDW is likely to be found include home services, construction, the food and restaurant sectors, the hospitality business, agriculture, retail trade and across a diverse range of vocational and professional services.

The Commission's (2014) *Undeclared work in the EU, Special Eurobarometer* reports (QE6) that home renovations (25% of respondents), car repairs (22%), home cleaning (35%), farm products (11%), other services (24%), and other goods (20%), are the areas where much of UDW is believed by respondents (according to the percentages shown in brackets) to be found.

There is no hard evidence available on how UDW is distributed by employer size. It is possible that large companies are more professionally run and careful about UDW. To the extent that some abuses occur (e.g. reducing the effective wage rate by requiring longer hours of work or flexible forms of employment), these may be engineered by 'consensus' between the employer and the employees. Abuses may be more likely in the case of individual employers or very small companies where the two parties can come to a mutually acceptable arrangement which reduces costs for the employer but also preserves the worker's job. It should be noted that some of the penalties for UDW (e.g. the exclusion from bidding on government contracts) will concern large firms, so there is an additional incentive for compliance in their case.

There are motives for UDW from both sides of the market. For employers, UDW 'pays' because, until the crisis, there was a shortage of unskilled labour; now, it pays because the decline in demand has necessitated a decrease in costs. Illegal workers offer flexibility in terms of when and for how long they are employed, are paid less than unionized labour, and their social security and other contributions are not made. From the point of view of the worker involved in UDW, the motives include securing work and tax-free income at terms which are preferable to unemployment or legal work elsewhere. In the case of Cypriot workers engaged in UDW, the motives may include adding to their income through flexible forms of employment which are not widely available and are generally not sanctioned by unions. Thus, each category of UDW carries its own special context and forces at work.

The Commission's (2014) *Undeclared work in the EU, Special Eurobarometer* reports ((QE4T) as reasons for UDW that 26% of respondents believe that regular salaries are too low, 15% say that there are no regular jobs and 14% assert that social security contributions are too high.

### **2.1.3 Estimated scale of undeclared work**

Any estimate of the scale of UDW is fraught with difficulties, both definitional and conceptual. The discussion below should, therefore, be read with this caveat in mind.

As noted in section 1.1.2, there are three large sources of UDW. Illegal immigrants are thought to be of the order of 25-35,000, or between 7-9% of the gainfully employed in Cyprus (currently approximately 370,000 persons). So a very rough estimate of the share of GDP (meaningful only under special assumptions about the production function and likely an overstatement) due to this particular type of UDW might be of the same order, namely around 7%.

A second large source of UDW concerns underreporting by the self-employed. The rate of self-employment has been declining over time and is now of the order of 12% (for 2015 Q3, CYPSTAT report 43,410 self-employed individuals out of a total of 370,203 persons employed). Self-employment includes not only tradesmen (electricians, plumbers, mechanics painters, construction and repair people and others), some of whom may employ the illegal immigrants referred to above, but also professionals such as lawyers, doctors, private tutors and other service providers. Some of the self-employment may occur in dual job holding by employees in the public sector who

generally work only until 3pm. The size of the tutoring and medical services activities was estimated by AKEL (2003)<sup>46</sup> to be approximately CYP 27 million in 2000, most of this being due to tutoring rather than medical services. This equates to about 0.5% of GDP.

Using data drawn from the Family Expenditure Survey (FES, 2004), Pashardes and Polycarpou (2008)<sup>47</sup> investigated the extent to which households underreport self-employment income, capital income, and income from agriculture. They concluded that a conservative estimate of the size of the black economy in this particular context is of the order of 6.7% to 8.1% of GDP, with this range including capital income underreporting. Note that their estimate includes the AKEL effects (below).

Some of the UDW by legal workers may be in paid work, the third category mentioned in section 1.1.2. A variety of payment schemes may be in force, including envelope wages; and by definition such work does not involve the payment of social security contributions. This UDW would result in increased household income that would not be reported but would be captured by the Pashardes and Polycarpou (2008)<sup>48</sup> study.

Abuses of unemployment insurance and welfare schemes may also exist. However, the scale of these abuses is thought to be limited relative to the work carried out by illegal workers, the self-employed and paid workers.

The AKEL (2003) study estimates the total size of the 'para-economy' (defined to include some unpaid and some illegal work) as 9.2% of GDP in 2000. This figure is broadly in line with the estimate of 8.8% of GNP during the 1980s by Georgiou and Syrighas (1994)<sup>49</sup>; they rely on the Tanzi method which uses the demand for currency as a proxy for 'underground' activity, and their methodology is broadly consistent with the definitions in AKEL (2003). Adding the rough estimate of UDW of 7% of GDP due to illegal workers (category 1 above) and the Pashardes and Polycarpou (2008) estimate of about 8% for underreporting (categories 2 and 3 above) would produce an overall estimate of the order of 15% of GDP. Williams and Renooy (2013)<sup>50</sup> note that the scale of UDW in the EU has been decreasing recently, and this is probably also true in Cyprus. For Cyprus, they report a figure from Schneider (2012)<sup>51</sup> of 25.6% of GDP in 2012 (down from 29% in 2003). This, however, appears implausibly high.

One issue worth noting relates to possible UDW differences between the government controlled area in the south and the occupied north. Besim and Jenkins (2006)<sup>52</sup> examined the situation in the north and estimated the number of unregistered workers by (i) comparing the work force with those registered in various insurance funds, and by (ii) counting the number of unregistered immigrants. They concluded that the number of workers in the informal sector was in the region of 35-40% of the total labour force, whose contribution to GNP was of the order of 12-17% of GNP. They also noted (p. 3) that the official statistics for income considerably understate this and that '... the gap in

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<sup>46</sup> AKEL (2003) E Paraoikonomia sten Kypro: Melete (Nicosia, Grafeio Oikonomikon kai Koinonikon Meleton, AKEL).

<sup>47</sup> Pashardes, P. and A. Polycarpou, (2008), 'Income tax evasion, inequality and poverty', Cyprus Economic Policy Review, Vol. 2, No. 2, pp. 37-49.

<sup>48</sup> Ibid

<sup>49</sup> Georgiou G. M. and G. L. Syrighas (1994) 'The "Underground Economy": An Overview and Estimates for Cyprus', Cyprus Journal of Economics, Vol 7. No. 2, December, pp. 125-143.

<sup>50</sup> Williams C.C. and P. Renooy (2013) Tackling undeclared work in 27 European Union Member States and Norway: Approaches and measures since 2008, Eurofound, Dublin.

<http://www.eurofound.europa.eu/publications/report/2013/labour-market/tackling-undeclared-work-in-27-eu-member-states-and-norway-approaches-and-measures-since-2008>

<sup>51</sup> Schneider, F. (2012), Size and development of the shadow economy of 31 European and 5 other OECD countries from 2003 to 2012: some new facts, available at [http://www.econ.jku.at/members/Schneider/files/publications/2012/ShadEcEurope31\\_March%202012.pdf](http://www.econ.jku.at/members/Schneider/files/publications/2012/ShadEcEurope31_March%202012.pdf).

<sup>52</sup> Besim, M. and G. P. Jenkins (2006), 'Informal but not Insignificant: Unregistered Workers in North Cyprus', unpublished mimeograph.

the incomes of permanent residents of north and south Cyprus could be significantly smaller than what was reported in the official statistics for north Cyprus’.

All this work suggests that UDW in the government-controlled areas, where UDW is less prevalent than in the north, is probably of the order of 15% and may have declined during the crisis as illegal workers departed.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

The main governmental organisation with an interest in UDW is MLSI. Other organisations with an interest in UDW include the Ministry of the Interior, tax collection authorities, the Ministry of Finance, and the Police Force. In a Presidential System, the Executive Branch and the House of Representatives also have a major role to play. Social partner organisations, such as trade unions and employer organisations, also play a role in monitoring and dealing with UDW.

The MLSI is responsible for monitoring all labour market and employment developments, supervising the collective bargaining process, facilitating the resolution of industrial relations disputes, monitoring the implementation of labour legislation, administering the social insurance programme as well as the new Guaranteed Minimum Income (GMI) programme, running the Public Employment Offices, and interacting with social partners through the Tripartite Process.

During the last 10 years, tackling UDW has been a priority for Governments in Cyprus. In 2009 Joint Inspection Units (JIUs) commenced fighting UDW. Four JIUs operate on a daily basis, mainly inspecting construction sites, hotels, restaurants and manufacturing enterprises. Inspectors from the Department of Labour Relations, the Department of Labour and the Social Insurance Services take part in these units. The coordination of the JIUs is done by the Department of Labour Relations in MLSI.

Recently, the Council of Ministers decided to reorganise the Joint Inspection Units into a centralised inspections inspectorate. The inspectorate, among other mechanisms, will use advanced information systems and risk assessment methods in its work. Draft law will be forwarded to the Parliament in Summer 2017.

The Ministry of the Interior is responsible for issues relating to migration, issuing identity cards and work permits, citizenship applications, refugee/asylum claims, and the implementation of all legislation covering this broad set of issues. The legality of the work status of an individual would come under its remit, and so it has a direct role in the determination of UDW.

Tax collection authorities are now integrated and responsible for issues relating to both direct and indirect taxation, and are involved in the monitoring of social insurance payments along with MLSI and the Ministry of the Interior.

The Police Force, under the Ministry of the Interior, is responsible for executing court orders and resolving cases of illegal entry. They also have a special unit dealing with human trafficking, some of which is for illegal work purposes.

The Ministry of Finance is responsible for the broad macroeconomic and fiscal policy that shapes the environment within which UDW exists.

The Executive Branch (President and Council of Ministers) sets policy in the context of advice received from the relevant Ministries. When legislation is required, it must work with the House of Representatives to secure sufficient political consensus to implement new measures.

The Tripartite System involves the government (executive and legislative parts), unions and employer organisations. It manifests itself in a number of institutionally defined bodies and helps shape social consensus.

## **2.2.2 Characteristics of the responsible organisations**

The MLSI, the Ministry of the Interior and the Ministry of Finance are large, highly professional bodies employing many well-qualified specialists who, among many other responsibilities, monitor UDW and try to deal with it in the context of the policy environment and the available resources.

## **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The nature of cooperation and data exchange, and their effectiveness, are described collectively: Most of the organisations involved in monitoring UDW are ministries which come under the political supervision of the Executive Branch and so must operate within the parameters set by the legal system. A lot of co-operation occurs informally or as a result of ministerial committees appointed by the Council of Ministers. The exchange of information has been improved considerably during the years (2012-2016) when Cyprus was under the programme of financial support by the Commission, the European Central Bank and the International Monetary Fund. Many administrative data sets have been integrated, and the new GMI programme will involve individualised counselling and activation, thus limiting the ability of individuals to collect benefits beyond the allowable amounts while they work.

As a result of measures taken during the recent crisis, much higher monitoring of financial transactions is now carried out by banks. These efforts have required increased co-operation between Member States, the ECB and the Commission. In consequence, it has become more difficult to process transactions involving UDW through the banking system. This may, of course, just increase the demand for currency in circulation.

MLSI, in cooperation with the Support Group and the EU Commission, has proceeded to a study in order to evaluate the existing information system and the existing procedures regarding UDW. The final report will be ready at the end of 2016.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The recent initiatives by the EU with regard to UDW have come in the middle of a deep crisis, and policies in the Memorandum of Understanding do not give UDW centre-stage. As a result, the issue has received relatively modest attention and no major policy initiatives have been undertaken. Nevertheless, efforts are being made on both the deterrence and compliance fronts; however, the resources available to deal with UDW are modest. MLSI and the Minister in charge are spearheading a campaign of public awareness of the problems involved.

Interestingly, the Commission's (2014) *Undeclared work in the EU, Special Eurobarometer* reports that Cypriots disapprove of UDW and have not made or received such payments to any noticeable extent. Yet, 16% reported (QE5) that, when buying goods or services, UDW may have been involved because there was no invoice or VAT receipt. Also, 39% reported (QE1) that they personally know someone whom they suspect of not declaring all their income. They attribute this to a low risk of apprehension (QE3); 56% of the respondents believed that there was 'lack of control' by the authorities ((QE4).

### **2.3.2 Measures to tackle UDW**

Legislation prohibiting UDW is in place. Inspections of workplaces are carried out by officials from MLSI. Government contracts may not be awarded to firms convicted of employing workers illegally and this may provide incentives to avoid UDW and possible apprehension. Public information campaigns have been carried out and the Minister of Labour makes repeated reference to efforts to combat UDW.

Information from the JIUs suggests that, in 2016, 6,469 inspections took place (1,173 for self-employed persons). During these inspections, 14,434 employees were checked

and 15.4% of them found to be undeclared. The main problem seems to be concentrated in the restaurant/café area (with the percentage of undeclared work reaching 22.4%) and in construction (where this percentage was 16.65%). Among EU citizens inspected, 19.4% were undeclared, while this percentage for Cypriot employees was 10.32%.

There is very little information available on the effectiveness of measures to tackle UDW, or on the apprehensions, convictions and the effects of measures to combat UDW. Some rudimentary information is contained in Pashardes (2010)<sup>53</sup>. He reports that, in 2009, 1,208 employers were accused of illegally employing aliens and 1,617 aliens were found to work without a licence. No information is provided on the outcomes of these cases.

A relatively new law now requires employers to issue a Certificate of Commencement of Employment upon hiring a new employee (copies are issued for the employer, the employee and the Social Insurance Service). An extra-judicial fine of EUR 200 per undeclared employee is imposed if this is not done. In 2015, 1593 such fines were imposed.

### **2.3.3 Good practice**

Impressionistic evidence suggests that inspections and convictions appear to be powerful tools, but there is very little publicly available information on these matters.

### **2.3.4 Challenges and barriers**

Several problems make it difficult to deal with UDW. First, Cyprus is in the midst of an unprecedented crisis with high levels of unemployment. In this context, UDW may provide an option for employers whose businesses would not otherwise survive and employees who would not otherwise be employed. Second, the political problem continues to absorb mental and other resources which might have been devoted to other important issues, including UDW. Third, a number of government services are not being provided to a sufficiently high standard; as a result, private schooling and private health care are thriving. Individuals feel that their taxes are not well-spent, corroding the moral and efficiency foundation of the fight against UDW. Efforts are, of course, being made to remove all these obstacles.

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<sup>53</sup> Pashardes, P. (2010) In-work poverty and labour market segmentation A Study of National Policies European Commission DG Employment, Social Affairs and Equal Opportunities. (Assisted by S. Andreou)

## **Factsheet on Undeclared Work – CZECH REPUBLIC (September 2017)**

### **2.4 Nature and Estimated Scale of Undeclared Work**

#### **2.4.1 Definition of undeclared work**

In the Czech Republic, there is no local legal definition of undeclared work (UDW). The Employment Act (§5.e) defines illegal work as dependent work<sup>54</sup> performed outside of an employment contract or performed by a foreigner without a valid work or residence permit. (A pervasive form of illegal work, referred to as “Švarcsystém” (eponymously named after the entrepreneur Miroslav Švarc, its “inventor”) consists of using self-employment contracts in place of employer-employee contracts in work relations that fundamentally constitute an employer-employee relationship and ought to be covered by an employment contract.) The Czech Republic therefore formally adopted the UDW definition from the Decision of the European Parliament and Council of 9 March 2016 as any paid work that is legal, but is not reported to public administration. The implementation of this recent adoption remains to be developed and we thus focus in most of this factsheet on the closely related agenda of dealing with illegal work.

The State Labour Inspection Office (SLIO), the Foreign Police, the District Labour Offices (DLO), as well as members of the tripartite all apply the current state of the legislation when considering illegal work and UDW. There has been a gradual clarification of how and when to best apply the specifics of the Employment Act outlined in the preceding paragraph. The different positions of the trade unions and of the employer associations on what constitutes a useful definition of illegal work play out in the legislative process as either party attempts to affect one of the frequent updates of the Labour Code or the Employment Act.

#### **2.4.2 Characteristics of undeclared work**

According to SLIO, the main types of practices targeted by the Labour Inspection authorities are the presence of effective employer-employee relations without written employment contracts (also including those working illegally while registered unemployed), the absence of appropriate permits for the employment of foreign workers, and the “Švarcsystém” disguising salaried employment as self-employment. In 2016, Švarcsystém cases represented about 20%<sup>55</sup> of uncovered instances of illegal employment, whereas its share in 2010 was 10%. Foreign workers also frequently work based on a trade licence, as independent contractors, when their employment relations at least border on regular long-term employer-employee relations.

According to ad hoc surveys<sup>56</sup> the highest incidence of UDW and illegal work in the Czech Republic is among workers holding multiple jobs and among self-employed. The most

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<sup>54</sup> Dependent work is performed in a relationship of a supervisor-employer with a supervisee-employee, work that deserves a salary, and is performed within specified work hours.

<sup>55</sup> There were 247 SLIO inspections that uncovered Švarcsystém, with the total of 256 persons involved in this type of arrangements: 122 citizens of the Czech Republic, 29 citizens of EU Member States, and 105 Third-Country nationals.

<sup>56</sup> See the following studies:

Kux, J., Kroupa, A. (2006): Undeclared Labour in the Construction Industry. CLR, European Institute for Construction Labour Research. Country Report – CR, RILSA. Internet: <http://www.rilsa.cz/an205.html> World Bank (2015); Horáková, M., Kux, J. (2003): Country Study on Informal Economy in the CR. Prague, Research Institute of Labour and Social Affairs. Internet: [http://www.vupsv.cz/INFORMAL\\_ECONOMY.pdf](http://www.vupsv.cz/INFORMAL_ECONOMY.pdf); Fassmann, M. (2006): Shadow economy – III, Undeclared Work (Stínová ekonomika – III, Práce na černo. Pohledy č. 3), Praha, Českomoravská konfederace odborových svazů.; Drbohlav, D. et al. (2009): Illegal economic activities of immigrants: Czech Republic in broader European context. (Nelegální ekonomické aktivity migrant: Česko v evropském kontextu) Čermák Zdeněk - Lachmanová Lenka - Fassmann Martin - Drbohlav Dušan, Karolinum, Praguem, ISBN 9788024615523.

common practices consists of tax evasion in small companies (paying the minimum wage and the rest in an envelope), undeclared earnings from secondary jobs or overtime hours, and undeclared work activities of the registered unemployed. During the economic boom preceding the great recession, many foreign workers had at least one UDW activity since their arrival in the country and the highest incidence of UDW appeared at the time of arrival. About a half of those involved in UDW are low skilled workers. There is also an indication of an intensive overlap of declared and undeclared work with about two thirds of the self-employed who engage in UDW generating significant benefits from tax evasion.

According to evidence and the experience of SLIO, supported by a recent study<sup>57</sup>, UDW is most prevalent in construction (accounting for 20% of the total number of identified illegally employed persons), processing/manufacturing (14%), wholesale/retail and motor vehicles repairs/maintenance sector (11%) in particular. In 2016, consistent with this evidence, SLIO inspections targeted the following sectors: wholesale/retail trade and repairs/maintenance of motor vehicles (24%), construction (17.7%), the HORECA<sup>58</sup> sector (16.7%), and the processing/manufacturing sector (15.9%).

There is no systematic evidence on the distribution of UDW by employer size, although both existing ad hoc surveys<sup>59</sup> and SLIO inspection practice are consistent with the majority of illegal employment and UDW cases being concentrated among small (under 10 workers) or medium sized companies (10-49 workers), and the self-employed. However, it is possible that some large employers under-report actual hours worked (in the services sector in particular). This trend is more or less stable over time. In 2016 approximately 52% of SLIO inspections targetted employers with 0-9 employees, 16% with employers with 10-49 employees, and employers without any registered employees.

One of the two main incentives which may motivate the existence of UDW is the high tax wedge on low-wage earners through social security contributions. Equally importantly, the Czech tax wedge gap between self-employed and employees continues to be one of the largest in the EU. Correspondingly, an unusually high proportion of workers in the Czech Republic are self-employed, i.e., work in job types more prone towards UDW. The administrative burden imposed on employers by the three systems of tax collection (income tax, social security, health insurance) could represent another contributing factor (Doing Business, The World Bank<sup>60</sup> reports high workload in terms of hours related to this agenda in an average Czech company).

A less discussed issue is that the bureaucracy of the Czech system of work and residency permits for foreign workers may have pushed law-abiding immigrants into illegal work. However, since June 2014, administrative costs may have declined thanks to the 'dual card' approach where one card (based on one application) contains both the residence and work permit.<sup>61</sup> In the same spirit, inefficient business regulation may force workers

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<sup>57</sup> CETA (2015): Shadow economy in the Czech Republic: A study [Studie: Stínová ekonomika v České republice] Internet: <http://eceta.cz/studie-stinova-ekonomika-v-ceske-republice/>  
[http://eceta.cz/wp-content/uploads/2015/11/SE\\_01\\_2015\\_web.pdf](http://eceta.cz/wp-content/uploads/2015/11/SE_01_2015_web.pdf)

<sup>58</sup> Hotels, restaurants, and catering sector

<sup>59</sup> Filipec, P. 2011. "The Shadow Economy Analysis in the Czech Republic". Charles University in Prague, Faculty of Social Sciences. Internet: <https://is.cuni.cz/webapps/zzp/detail/95977>  
Also, CETA (2015).

<sup>60</sup> World Bank Group. 2014. *Doing Business Economy Profile 2015 : Czech Republic*. Washington, DC. © World Bank. Internet: <https://openknowledge.worldbank.org/handle/10986/21267>  
License: CC BY 3.0 IGO.

<sup>61</sup> Asylum seekers are effectively not allowed to work for extended periods of time. However, this issue affects only a small number (under 1000) of individuals.

into self-employment arrangements. There is little empirical evidence evaluating the success in terms of UDW reduction of recent reforms in this area.

### **2.4.3 Estimated scale of undeclared work**

In 2016, SLIO performed about 9,300<sup>62</sup> inspections that targeted illegal employment practices. These inspections of employers uncovered 5,815 violations of labour legislation (in terms of the following areas: undeclared/illegal work, but also labour relations/conditions and occupational safety and health which are also identified by legality of employment inspectors), in which 2,290<sup>63</sup> workers were illegally employed. A large proportion of the foreign workers involved in some form of violation did not have a valid work permit, and the second largest group of foreigners had all the necessary permits but worked without proper contractual arrangements. Within the foreign-worker group, Ukrainian and Vietnamese workers continue to represent the largest groups. Similar results are reported for earlier years. In 2016, inspections involved both legal entities and physical persons as employers, with 30% of the inspected workplaces being subject to some form of formal employment or work safety issues. It is difficult to generalise these numbers into an estimate of the country-wide extent of UDW, as SLIO inspections target workplaces that are the most likely to be in breach of employment legislation. It is clear that in a country of 5 million employees and 450,000 foreigners with a long-term presence, 2,290 illegally employed workers constitute a very small group.

On the other hand, a qualitative difficulty with these numbers is that even careful inspections are unable to deal with certain forms of UDW. When both parties to an employment relationship claim to be collaborating based on a verbal agreement or a short-term under-EUR 350-per-month contract (under the arrangement known as Agreement to Complete a Job, "Dohoda o provedení práce"), such relations are not subject to reporting to the sickness insurance system and effectively prevent the examination of actual hours worked. In the Czech Republic small employers are avoiding long-term contracts (allowing for less flexibility) and favouring short-term contracts (for definite period) to such an extent that regular employer-employee long-term contracts are becoming the exception with small employers.

According to 2015 studies by A.T. Kearney and VISA and by the CETA<sup>64</sup> think tank, the shadow economy adds up to about 15 % of the Czech GDP. For the purposes of cross-country comparisons of such estimates, it is crucial to account for the qualitative differences in methodologies involved in generating such estimates. According to the CETA study, the Czech Republic features a relatively high share in an EU comparison of purchases of services and products from friends, colleagues, and acquaintances (esp. in home improvement and car maintenance activities) in small municipalities. The CETA study also cites estimates that almost 200 000 workers (i.e., over 3 % of the labour force) was involved in illegal work activities in 2013.

## **2.5 Institutional Framework**

### **2.5.1 Responsibilities for addressing Undeclared Work**

SLIO, which is supervised by the Ministry of Labour and Social Affairs (MoLSA), is entitled to perform inspections with all employers and self-employed with regard to workplace safety and the formal aspects of employment, including illegal employment. A key issue is that employers must have available written employee contracts on site, until they register their employees for the purpose of pension insurance. Following a legislative change, the obligation to have the contracts available in the place of work also applies

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<sup>62</sup> The annual target for 2016 was set to 7,000 inspections; SLIO inspected 3,518 physical persons and 4,538 legal entities.

<sup>63</sup> 1,367 Third-Country nationals, 760 Czech citizens, and 163 citizens of EU Member States.

<sup>64</sup> Ceta, 2015



for posted workers (from 1<sup>st</sup> April 2017). In addition to a regular programme of annual inspections<sup>65</sup>, SLIO occasionally organises unexpected nation-wide actions focused on specific issues (e.g. Christmas markets). It is also worth noting that between 2012 and 2015, much of SLIO activity was covered by ESF funding (OP LZZ<sup>66</sup>).

In 2000, the Czech government established an 'Inter-ministry coordination board for curbing illegal employment of foreigners', which also features representatives of the tripartite bodies, the Czech Statistical Office, SLIO, etc. (the bylaws of the board were updated in 2014). A corresponding Action Plan for fighting illegal migration was approved in 2004 and involves actions by the Ministry of Interior, MoLSA, Ministry of Foreign Affairs, Ministry of Finance and other public administration bodies. The board participates on annual reports that compile policy information in this area from all involved ministries.<sup>67</sup> The board clearly improves information flows between ministries; it is less clear (given the absence of corresponding recent documents) that it plays an important role in coordinating legislative work or targeting inspections.

### **2.5.2 Characteristics of the responsible organisations**

SLIO is divided into a Head Office and 8 Regional Labour Inspectorates, with about 190 labour inspectors focusing on employment issues and following a centralised inspection methodology. Some of the inspectors received special training for detecting illegal employment of foreign workers and human trafficking practices. Some 45 company cars, laptop computers and mobile internet routers were provided to the employment inspectors several years ago to speed up the performance of accounting checks at the inspected workplace.

### **2.5.3 Cooperation and collaboration between authorities within the Czech Republic and cross-border authorities**

When inspecting a workplace, SLIO naturally cooperates with the Czech Social Security Administration and Trade Licencing Offices when checking formal aspects of inspected documents. A key collaboration is between SLIO and DLOs, as some of the illegally employed workers are registered as unemployed. The labour inspectorates also frequently coordinate with the state, municipal and/or foreign police, as needed.<sup>68</sup>

Since October 2014, SLIO uses an integrated information system with access to the so called Common Database of the MoLSA department, through which inspectors may verify, for example, whether a certain employee was duly registered for the purpose of social insurance. We suspect, however, that progress is slow in the area of integration of various databases employed by the tax, social security, and health insurance authorities and by welfare and labour offices, and by the foreign police. However it is clear that, in specific individual inspection cases, SLIO receives information from other state organisations, as outlined above, and that cooperation with respect to UDW is on the increase – including national and regional cooperation between the Police, Foreign Police and Customs Offices. Furthermore, the 'Inter-ministry coordination board for curbing illegal employment of foreigners', which meets bi-annually, also sets up ad hoc sub-committees and supports information flows, at least at the aggregate level.

In terms of UDW, the closest cooperation has traditionally been between DLOs and SLIO authorities. In 2015 and 2016, SLIO reacted to extensive suggestions from the LO when targeting inspections to employment agencies. SLIO also regularly receives support from the Police of the Czech Republic, Foreign Police and the Customs Administration. Other

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<sup>65</sup> Target for 2016: 7000 inspections; 2017: 8500 inspections

<sup>66</sup> OP LZZ stands for Operation Program for Human resources and Employment [Operační program Lidské zdroje a zaměstnanost].

<sup>67</sup> The 2012 report can be found here: <http://www.psp.cz/sqw/text/orig2.sqw?idd=65146>

<sup>68</sup> Inspectors are not armed, unlike members of the Police of the Czech Republic. The Foreign Police has specialists trained to identify falsified documents and other specialists trained in the regulation of employment relations for foreign workers.

than support provided for inspections, we know of no direct active cooperation between authorities in this policy area.

The Czech Republic collaborates with other Member States within the IMI<sup>69</sup> system on the posting of workers, which enables any individual Member State to share and request information from authorities in a different Member State. Since April 2017, following the implementation of the Enforcement Directive 2014/67/EU, the scope of administrative cooperation through the IMI system has been widened. Apart from requests for information on specific posting arrangements, both the system and the Czech legislative framework allows for the exchange of administrative data and decisions to service providers, as well as cross-border enforcement of financial administrative penalties imposed in the context of the posting of workers.

## **2.6 Policy Focus and Measures**

### **2.6.1 Policy approach**

The recommendations featured in the Czech policy debate as of the writing of our 2007 UDW report (and well represented in Fassmann, 2006, for example) included (i) strengthening the analytical capacity at the Ministry of Finance, (ii) simplifying tax legislation and collection, (iii) introducing measures to eliminate room for disguising regular employee-employer relationships as self-employment, (iv) strengthening monitoring, enforcement, and sanctions of UDW, (v) launching a public media campaign against UDW. The actual policy course focused on approaches (iii) and (iv).

Repression is the main tool of UDW policy as Czech policymakers focus on parameters of the relevant legislation. The continuous updates of the Employment Act and of the Labour Code introduced since 2004 with an eye towards reducing illegal employment practices include more stringent conditions for unemployment registration, stricter conditions on temporary employment agencies and on the type of jobs to be performed by self-employed instead of regular employee-employer contracts, and extended powers of DLOs as an inspection authority together with increased penalties for UDW of an increasing variety.<sup>70</sup> In recent years, SLIO has become the main authority addressing UDW and its inspection efforts (and penalties) were magnified.

### **2.6.2 Measures to tackle UDW**

The chief measure used in the Czech Republic is Labour Inspection. During 2016, SLIO imposed penalties of approximately EUR 2 million in connection with illegal employment practices.

The stricter regulation of temporary employment agencies, which increased the price of labour they offer, led to a partial replacement of the flexible labour they supplied by equally flexible quasi-legal arrangements.

For several years now the government has been increasing the statutory minimum wage from very low levels. The effect of this policy on the share of self-employed in the total employment and on UDW has not yet been analysed.

It is not clear how effective labour inspections are. First, many of the inspection cases transform into legal proceedings that tend to be extended and involve several instances of appeals. Second, there are no studies attempting to estimate the causal effect of changes in maximum penalties, number of inspections, etc.

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<sup>69</sup> The Internal Market Information system of the European Commission.

<sup>70</sup> The very high level of penalties was recently decreased: the *minimum* penalty for employers enabling illegal employment declined from under EUR 10,000 to under EUR 2,000 as of January 2016. The practices leading to employer being penalised when uncovered include employers not having proper employment documentation on site and exceeding the annual limit for Agreements to Complete a Job.

### **2.6.3 Good practice**

Good practice examples identified in recent years have been included in the unified methodology for inspecting the legality of employment.

### **2.6.4 Challenges and barriers**

We believe that the lack of data management across various state authorities is a major obstacle to identifying targets for labour or financial (tax authority) inspections.

Most of the discussion in the country focuses on updating the Labour Code and the Employment Act to foster the practice of labour inspections in the field. Looking forward, further data sharing (mainly within the practice of SLIO) will take a key role.

The country could benefit from a transfer of good practices from other MSs. An important incentivising factor is the high tax wedge on low-wage earners through social security contributions. Equally importantly seems to be the notable tax wedge gap between self-employed and employees.

### **Additional References**

Annual Summary Report on Work Inspections [Roční souhrnné zprávy o výsledcích kontrolních akcí provedených inspekcí práce za rok 2014] Internet:  
<http://www.suip.cz/rocní-zpravy/>

Paying Taxes 2016: The Global Picture, Internet:  
<http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Special-Reports/Paying-Taxes-2016.pdf>

## Factsheet on Undeclared Work – DENMARK (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

The Danish tax authorities define *undeclared work* as legal productive activities that are not reported and taxed according to existing legislation. This definition is generally accepted.

If the unreported activities are performed by foreigners without a work-permit, they will also fall into the category of *illegal work*.

Exempted from undeclared work are unpaid activities performed to assist friends and family members. In addition young people aged 15 years and under may work in private households without reporting their income. Pensioners can do the same, if their income is below EUR 1,410 (DKK 10,500) per year (2016).

#### 2.1.2 Characteristics of undeclared work<sup>71</sup>

According to a recent survey, around 40% of the population had in 2014 bought services through undeclared work. The majority of the services were paid in cash (26%) followed by bipartisan favours (19%). The survey does not contain detailed data about the various form of UDW by sector, but in surveys from 2008-09<sup>72</sup>, 29% of the persons who had carried out undeclared work against payment in cash stated that the most important activity was construction work, hotels and restaurants (17%), public and personal services (13%), cleaning (11%) and agriculture (incl. gardening), fishing and quarrying (11%). Exchange of services, most important sectors: Construction (33%), public and personal services (13%), agriculture (incl. gardening), fishing and quarrying (13%), transport and telecommunications (10%). Data from 2014 reports that the major forms of services bought through UDW in 2014 are: Hairdressers (7%), repair of electrical systems in private homes (6%), auto repair (5%), assistance from a carpenter (4%), cleaning (4%) and care of pets (4%).

Typically undeclared work is performed for friends and relatives and the vast majority of services are bought from private individuals, not firms.

The majority of those doing unreported work are men. Thus among the men, 28% had performed undeclared work in 2014, while the share among women was 16%. Among those demanding undeclared work, there was no significant gender bias.

Age plays an important role, when it comes to performing undeclared work. Thus approximately one in three aged 18-39 years performed undeclared work in 2014, while the same was true of only one in five in the forties and one in eight in the over fifty age bracket. Among the buyers of undeclared work, the age distribution was more even.

Also income is an important determinant for supplying and demanding undeclared work. The suppliers of undeclared work are more often low-income earners. Thus, every third person in the lowest income decile carried out unreported work in 2014. Among those in the highest decile only about 1 in 10 carried out undeclared work during the same period. Looking at education, it is not surprising that people with craft training are more frequently found among the suppliers of undeclared work.

The main motivators for undeclared work are the wish to save money and a personal relation to somebody, who supplies undeclared work.

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<sup>71</sup> The majority of this and the following section is based on a recent publication from the Rockwool Foundation (Nyt fra RFF, Marts 2016. Internet: <http://www.rockwoolfonden.dk/publikationer/markant-fald-i-efterspoergslen-paa-sort-arbejde/>)

<sup>72</sup> Rockwool Foundation (2010): Danes and undeclared work [Danskerne og det sorte arbejde], New from the Rockwool Foundation 2010:77. Internet: <http://www.rockwoolfonden.dk/publikationer/danskerne-og-det-sort-arbejde/>

An interesting feature from the recent studies of undeclared work is a decline in the share of the adult population, who state that they would be willing to perform undeclared work, if they had the opportunity. One reason for this change is probably that an increasing share of the population is stating that they see the risk of being detected, when performing undeclared work, to be higher in 2014 than in previous years. This increase is however solely observed among those not doing unreported work themselves.

### **2.1.3 Estimated scale of undeclared work**

Based on information about the share of the adult population performing undeclared work (24%) and the average number of undeclared hours they report (1.7 hours per week), the share of undeclared work as a share of all declared work amounted to 1.6% in 2014. This can also be taken as a rough estimate of the contribution of undeclared work to GDP, if one assumes that the productivity and the distribution by sectors is the same for undeclared and for declared work.

The share of undeclared work relative to all declared work has declined significantly in recent years from around 3.0% in 2009 and 2010. The decline is solely due to a decline in the average number of unreported hours worked, while the share of the population performing undeclared work has been stable.

Since 2012 a number of policy changes have been introduced. They could explain the observed decline in the estimated scale of undeclared work and are described in detail below.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing Undeclared Work**

The responsibility for addressing undeclared work is divided among several authorities.

The major actor is the Central Customs and Tax Administration (under the Danish Ministry of Taxation), which is responsible for implementing the legislation on income taxation and controlling tax returns. Based on existing legislation, the authority thus defines the border line between income from work, which has to be declared, and income, which is exempt from reporting. The authority has also taken initiatives to a number of campaigns directed at increasing the awareness of the damaging effects of undeclared work and of the risks of being detected, when supplying or demanding undeclared work.

The Danish Working Environment Authority (also under the Ministry of Employment) focuses on the issue of health and safety at work for people performing undeclared work (including illegal workers). The assumption is that working in the "grey segment" of the labour market also carries an increased risk of dangerous working conditions.

Furthermore the Danish Immigration Service (under the Ministry for Foreigners and Integration) is responsible for granting work and residence permits to non-EU-citizens. The issue of illegal work is therefore the main focus of this authority.

During inspections these authorities are assisted by the Police.

Finally the social partners (especially the trade unions) have taken a strong interest in undeclared work among migrants and posted workers (including illegal immigrants.). Their main perspective is thus the fear of 'social dumping' due to migrants and posted workers, who accept inferior work and pay conditions relative to the norms on the Danish labour market. One element in relation hereto is of course, whether the incomes of the migrants and posted workers are fully reported to the Danish tax authorities or whether the lower pay is combined with tax fraud.

### **2.2.2 Characteristics of the responsible organisations**

The Central Customs and Tax Administration is a national body based in Copenhagen with regional branches. It has around 6 300 employees (2015).

The Danish Working Environment Authority (also under the Ministry of Employment) is a national body with three regional branches, each of which is responsible for workplace inspections at the local level. The total number of employees is around 550.

The Danish Immigration Service (under the Ministry for Foreigners and Integration) is a national authority based in Copenhagen with a total of about 500 employees (full-time).

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

Since the opening of the Danish labour market for workers from the New Member States, the issue of social dumping has been high on the Danish political agenda. One aspect hereof has been the risk of undeclared work and underreporting of income in the sectors employing a high share of migrants and posted workers. Therefore resources have been allocated for increased control of social dumping in the form of inspections. Such regular inspections have been taking place since 2004. In the Budget Law for 2015, further EUR 3.7 million (DKK 27.7 million) were allocated for joint inspections by the tax authorities, the Working Environment Authority and the police. This meant that a total of EUR 9.6 million (DKK 72.0 million) were allocated for the joint inspections in 2015. The joint inspections are regulated by a written agreement, which defines the forms of cooperation and the planning of the inspections including the exchange of information between the participants. The Working Environment Authority is responsible for coordinating the collaboration.

The cooperation between the abovementioned authorities resulted in inspections of 773 firms in 2015 during eight national-wide inspections. The number has been rather stable in recent years. In 2015 the inspections led to 26 charges to foreign firms for not having registered their activities in Denmark and around 500 improvement notices for non-compliance with regulations concerning work and health safety. The main sectors targeted by the national inspections were construction, cleaning and catering, agriculture and the manufacturing industry, with the greatest emphasis on the first two. In addition to the national inspections just described, the authorities also cooperate on inspections at the regional level. A total of 38 such inspections were conducted in 2015.

An important tool for monitoring the activities of foreign employers in Denmark is the Register for Foreign Service Providers (RUT). This register is the Danish official registry to report foreign services. Foreign service providers, who do business in Denmark, must report this to RUT. The Working Environment Authority oversees that foreign companies adhere to the Danish working environment legislation. It also checks that foreign companies are reported to RUT, and that the notification is complete and correct in relation to rules.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

It is generally believed that the volume of undeclared work in Denmark amounts to only a minor part of the market economy. Furthermore undeclared work mainly takes the form of extra hours performed by workers who already have a full-time job, for instance in the construction sector.

Due to the rather high level of income taxes and a VAT rate of 25%, the economic incentives to perform undeclared work are considerable in the case of Denmark. In general however the widespread use of administrative registers and controls involving the use of personal identification numbers and a strict registration of private firms makes it difficult to develop a large-scale black economy.

In recent years there has however been an increased focus on combating undeclared work, probably also stimulated by the opening of the Danish labour market to migrants and posted workers. The major elements have been:

- Intensified and targeted controls and inspections by the authorities;

- More legal instruments to be applied in the control and prosecution of undeclared work; and
- Campaigns aimed at changing the attitude towards undeclared work both among the population in general and within specific target groups such as young people.

Thus the policy approach can mainly be characterised by deterrence although there are also examples of attempts to enable compliance through information and campaigns. Compliance has also been supported by allowing young people and retired persons to conduct undeclared work without being criminalised.

### **2.3.2 Measures to tackle UDW**

#### *Stronger control measures*

As described above, since 2004 regular intensive control actions have been carried out against unreported and illegal work. The control actions have taken place under strong media attention and this has strengthened the preventive effects of the actions. Also, the outcomes of the individual inspections have in recent years been made public on the website of the Ministry of Taxation and the Working Environment Authority. The intensified control measures have had their main focus on sectors and businesses which have turned out to have problems in this field. One purpose of the controls has also been to get hold of persons, who work undeclared while receiving unemployment benefits or cash benefits for unemployed. Follow-up on individual cases regarding unemployment benefit is carried out by 24 private Unemployment Funds under the auspice of The Danish Agency for Labour Market and Recruitment. Follow-up on individual cases regarding cash benefits for the unemployed is carried out by Udbetaling Danmark, the authority responsible for the collection, disbursement and control of a number of public benefits.

In addition, tax authorities have in 2015 announced a new project, which is targeted at persons who declare a very low taxable income, while at the same time having a high standard of living exemplified by an expensive house, ownership of luxury cars etc. Thus by combining various administrative registers the tax authorities hope to better target individuals who get their income from undeclared work or criminal activities.

#### *Information campaign*

Also in 2004, an information campaign against undeclared and illegal work was launched in co-operation with the social partners. The campaign focused on the concept of "Fair play". It described undeclared work as not only tax evasion leading to a reduction in public revenues – but also unfair competition in relation to other competing enterprises and to the great majority of people who pay their taxes. This first campaign has been followed by several others, some of which have been targeted at specific groups like young people or public procurers. Another important target group has been entrepreneurs of a non-Danish ethnic background, who have been informed about the Danish tax-legislation and employment regulations.

#### *Legislative initiatives*

In April 2005 the Danish Parliament (Folketinget) approved a law, which gave the tax authorities better instruments to combat undeclared work. They were thus given authority to obtain access to construction sites to control the information given by the employer concerning sub-contractors and employees. Also they were allowed to instruct employers to have an updated file of all employees from their first day of work.

In 2012 new legislation was introduced, which further allowed for tighter monitoring in the form of:

- Private consumers who pay bills amounting to more than EUR 1 343 (DKK 10 000) must pay using digital means of payment and not in cash. This allows for monitoring of the payment. The same rule applies to firms. If cash payments are used, the buyer can be made responsible for unreported income tax and VAT by the seller.

- At all construction sites there must be signs indicating the names and VAT registration number of the firms working there. Foreign firms must show their number in the Register for Foreign Service Providers (cf. above). Also all vans must carry the name of the firm which owns them and the VAT registration number.
- As part of the fight against major organised undeclared work, the tax authorities were given the right to enter private property, but only in the case where there is visible outdoor work of a professional nature taking place. The tax authorities are able to enter the land itself, e.g. the garden, and not into private homes.
- All workers became obliged to carry a valid piece of ID and show it to the tax authorities if required.

After a change of Government in 2015, the last two items have been taken out of the legislation based on the argument that they were in conflict with basic citizen's rights.

#### *Lower taxation on work*

Over recent decades, taxes on work have been reduced. The effects hereof are documented in a series of tables published on the home page of the Ministry of Taxation. For a low-income earner, the marginal tax rate has fallen from 45.5 % in 1999 to 40.3 % in 2016. For high-income earners the reduction is 6.9 percentage points, from 63.3 % in 1999 to 56.4 % in 2016. There has thus been a reduction in the incentive for UDW driven by the income tax system.

#### *Subsidies for services bought by private households*

The law on subsidies to home improvements was in effect in the years 1991-1995. In the beginning, the subsidy covered 40 % of wage costs and profits. The subsidy was only paid for wage costs and profits – materials were not subsidised. There was a maximum of EUR 940 (DKK 7 000) per household – in a period the maximum was EUR 1 343 (DKK 10 000). In 1994 the subsidy stopped but with payments running into 1995. All in all expenses to this the subsidy had an amount of EUR 706 million (DKK 5.3 billion).

Since 1994 various schemes have existed, which imply that a wage subsidy or a tax deduction is given to households that buy household and craftsmen services (cleaning, gardening, repair work etc.) from private firms. The purpose of the schemes is both to stimulate the demand for labour and to reduce the amount of undeclared paid household work. The exact services eligible for support and the size of the subsidy have varied over time. In its present form, in 2016 and 2017, the scheme supports household services like cleaning, childcare and gardening and various sorts of repair work and renovations, mainly with the aim of saving energy. For household services the tax deduction is EUR 807 (DKK 6 000) per adult living in the household. For repair work and renovation the deduction is EUR 1 613 (DKK 12 000). Given the marginal tax rates above, the cash value of the deduction is around half of the figures just mentioned.

### **2.3.3 Good practice**

Given the decreasing amount of undeclared work in recent years reported above, it is tempting to point to the effects of the new legislation introduced in 2012. In particular, there seems to have been an effect on the average number of hours of undeclared work for persons who supply it. Also there is an increasing awareness of the risks of being detected, when buying services from undeclared work. Based on the available evidence one cannot point to a specific cause for this, but one candidate could be the limit of EUR 1 343 (DKK 10 000) set to paying for services in cash, which is also mentioned above is the main form of compensation, when it comes to undeclared work.

### **2.3.4 Challenges and barriers**

As already mentioned, undeclared work plays a rather limited role on the Danish labour market. Also it seems that the amount of undeclared work as a share of GDP is actually declining. A plausible explanation is the intensified and targeted controls and inspections



by the authorities and the increase in the number of legal instruments applied in the control and prosecution of undeclared work

At present a major challenge takes the form of 'social dumping' by migrants and posted workers and foreign firms working in Denmark. In a Danish context the term social dumping refers to situations where work and pay conditions are below the usual level on the Danish labour market, but also to employers and employees not reporting income that is subject to VAT or income tax payment.

Therefore significant resources have been allocated to address the various forms of social dumping including undeclared work by migrants and posted workers. There is no doubt that the joint efforts by a number of public agencies have resulted in putting a downward pressure on the extent of undeclared work in this area. An exact assessment of the degree of success is however not possible based on the available evidence.

## **Factsheet on Undeclared Work – ESTONIA (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

In principle, there is no official (positive) definition of undeclared work. The legislation stipulates rights and obligations regarding work and services and indirectly designates practices whereby workers, employees, service providers, employers avoid employment law, labour market regulations, tax and social security regulations and contributions.

In principle the same latent definition is followed by different institutions. However, while the labour law enforcement institution, i.e. Estonian Labour Inspectorate, focuses on regulation of labour market; tax and social security contribution collection and administration institutions, Estonian Tax and Customs Board focus on tax law.

#### **2.1.2 Characteristics of undeclared work**

The main features that link to undeclared work are working without a formal binding employment contract, envelope wages, and partially undeclared work in the form of replacing employment contracts with providing services via self-employment or a company. The last category points to dependent or false self-employment; 'para-subordinate workers' in contrast to genuine, real self-employment or entrepreneurship. It is motivated by differences in taxation of labour and services in Estonia. It results in undeclared work where a portion of the employee's salary from a formal employer (usually the minimum salary) is paid officially while the remaining salary is paid as business income to benefit from significantly lower tax contribution.

Following the poll of Estonian Chamber of Commerce in 2016 (336 respondents) the three main incentives for undeclared work within employers were<sup>73</sup>:

- a) High taxation rate (57.3%), personal income tax is 20%; social tax is 33% of gross earnings; unemployment insurance premium is 1.6% of gross earnings<sup>74</sup> and corporate income (only distribution of profits are subject to income tax at the rate of 20 % of the amount of taxable payment.
- b) Cost saving and competitive advantage (42.7%), in sectors with very tight competition, like construction and food sector, envelope wages are more common. This might be enforced by institutional settings. For instance, public procurement procedures give advantage to the lowest price, which leads construction companies to make public offers under the market price, i.e. already assuming that part of the payroll will be left undeclared. Envelope wages and labour tax avoidance are seen as significant competitive advantage, because it allows them to offer the cheapest price and therefore create win-win situations for buyers and sellers.

From employees perspective the reasoning of undeclared work is as following:

- a) Income concealment (37.5%), individuals are motivated to hide their real income to take up benefits and tax credits for people in employment, or might be interested in undeclared income in case they are obliged to pay for child support and they intend to avoid these obligations;
- b) Higher salary (9.5%), non-payment of taxes is seen as an easy way to increase personal or business income;
- c) Loss of unemployment benefits (4.5%).

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<sup>73</sup> [https://www.emta.ee/sites/default/files/kontaktid-ja-ametist/uudised-pressiinfo/pressimaterjalid/30\\_11\\_2016\\_umbrikupalkade\\_tulemused\\_koda\\_mta\\_v.pdf](https://www.emta.ee/sites/default/files/kontaktid-ja-ametist/uudised-pressiinfo/pressimaterjalid/30_11_2016_umbrikupalkade_tulemused_koda_mta_v.pdf)

<sup>74</sup> <https://www.emta.ee/eng/private-client/declaration-income/tax-rates>

According to the Estonian Chamber of Commerce 2017 poll, the sectors where 'envelope wages' are most prevalent are construction, transport, HORECA, retailing, and industry. Also, most of the incidences are reported in small enterprises with up to 19 employees<sup>75</sup>.

Meriküll and Staehr (2010)<sup>76</sup> have estimated that firm-related characteristics, such as sectoral activity, firm size and employment changes, are important determinants of unreported employment in Estonia as well as in other Baltic states. According to the authors, many of the recipients of envelope wages may have few alternatives to accepting unreported employment. This indicates that individuals are often forced to accept fully or partly undeclared work, i.e. the situation is involuntary. Regular analysis of the undeclared economy by the Estonian Institute of Economic Research has indicated that about a half (37% in 2016) of people receiving undeclared salaries are not satisfied with this while just below half (47%) are satisfied with it<sup>77</sup>. In comparison with 2015 unsatisfied rate grew significantly, most of them (66%) are younger generations (aged 18-29). The same research indicates that the share of people satisfied with undeclared work is unequally divided in the society, i.e. geared towards older generations (aged 72), in rural areas and towards lower educated. However, the general attitudes among the working population are rather unsupportive of undeclared salaries as 62% of all working people do not favour payment of undeclared salaries in 2016. About 42% of undeclared wage receivers are afraid of losing their job in case they refuse undeclared work. However, the share is 49% among those who are not satisfied with receiving undeclared salaries, indicating that it is a forced choice for a considerable share of people receiving undeclared salaries.

### 2.1.3 Estimated scale of undeclared work

The Estonian Tax and Customs Board have estimated based on administrative data that in first quarter of 2017 the share of undeclared work was under 4.59% of workers<sup>78</sup>. Also, the Estonian Institute of Economic Research has estimated based on cross-sectional survey that the share of 'envelope wages' in 2016 has remained at between 7% and 10%. In 2016 the estimated tax loss from envelope wages was round EUR 109 million, which in comparison with 2015 was 32.7% (50 million) less. Compared to the last year the number of employees that received envelope wages decreased by 1,821 to 34,297.

Williams and Horodnic (2015)<sup>79</sup> have estimated (using Eurobarometer 2013 survey data) that 5% of employees are paid envelope wages, that the median percentage of gross salary paid as envelope wages is 40% and the tax morality index<sup>80</sup> is 2.82, which is the

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<sup>75</sup> [http://www.emta.ee/sites/default/files/kontaktid-ja-ametist/uudised-pressiinfo/pressimaterjalid/22.05.2017\\_pressikonverents.pdf](http://www.emta.ee/sites/default/files/kontaktid-ja-ametist/uudised-pressiinfo/pressimaterjalid/22.05.2017_pressikonverents.pdf)

<sup>76</sup> Meriküll, Jaanika, and Karsten Staehr. 2010. 'Unreported Employment and Envelope Wages in Mid-Transition: Comparing Developments and Causes in the Baltic Countries', *Comparative Economic Studies* 52 (4): 637–70. doi:10.1057/ces.2010.17.

<sup>77</sup> Estonian Institute of Economic Research 2016. *Varimajandus Eestis 2016* (elanike hinnangute alusel). Tallinn, 2016 (title in English: *Shadow Economy in Estonia 2016*). Internet: [https://www.mkm.ee/sites/default/files/varimajandus\\_eestis\\_2014\\_elanike\\_hinnangute\\_alusel\\_.pdf](https://www.mkm.ee/sites/default/files/varimajandus_eestis_2014_elanike_hinnangute_alusel_.pdf)

<sup>78</sup> [http://www.emta.ee/sites/default/files/kontaktid-ja-ametist/uudised-pressiinfo/pressimaterjalid/22.05.2017\\_pressikonverents.pdf](http://www.emta.ee/sites/default/files/kontaktid-ja-ametist/uudised-pressiinfo/pressimaterjalid/22.05.2017_pressikonverents.pdf)

<sup>79</sup> Williams, C. C., and I. A. Horodnic. 2015. 'Evaluating the Prevalence of the Undeclared Economy in Central and Eastern Europe: An Institutional Asymmetry Perspective', *European Journal of Industrial Relations* 21 (4): 389–406. doi:10.1177/0143831X14568835.

<sup>80</sup> In the analysis, to identify the level of population tax morale, Eurobarometer survey data were analysed, In the survey, six attitudinal questions were asked regarding how people rate the acceptability of various types of shadow work on a 10-point Likert scale (where 1 means absolutely

average for CEE countries and indicates that attitudes towards non-compliance behaviours are generally unaccepting.

Also, Paulus (2015)<sup>81</sup> have estimated (using income survey data linked with tax records at the individual level) that about 12% of wages and salaries in total are under-reported, and that people in the bottom and the top part of the earnings distribution evade much more.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

Addressing undeclared work is the focus of two main institutions in Estonia: the Estonian Labour Inspectorate, and the Estonian Tax and Customs Board. The former focuses on making employment rights effective, including tackling undeclared work; the latter is responsible for collecting tax revenues. Additionally, administrators of social and unemployment insurance could have a role in identifying and tackling undeclared work. The eligibility criteria of these benefits are related to factual declared employment and payment of taxes, thus during the application cases of undeclared work could emerge and information could be used by the Labour Inspectorate or the Tax and Customs Board to enforce the legislation.

### **2.2.2 Characteristics of the responsible organisations**

**The Estonian Labour Inspectorate** is a government agency working under the authority of the Ministry of Social Affairs. The main tasks of the Inspectorate are implementation of work environment policy, national supervision of requirements of legal acts regulating health and safety at work and labour relations in the work environment, notification of the general public, employees and employers about hazards in the work environment, and resolution of individual labour disputes at an extra-judicial labour dispute resolution body. In the Inspectorate, the Supervision Department is responsible for making employment rights effective and supervision of requirements of legal acts regulating labour relations and the working environment. About 52 labour inspectors are working in this department.

The area of activity of the **Estonian Tax and Customs Board** includes administration of state revenues, implementation of national taxation and customs policies and protection of society and legal economic activities. The Board has a directing function and exercises state supervision and applies enforcement powers of the state on the basis and to the extent prescribed by tax legislation. The Board is accountable to the Minister of Finance who directs and coordinates its activities and exercises supervisory control over it. Departments of the Board are: 1) Administration Department; 2) Legal Department; 3) Audit Department; 4) Tax Department; 5) Personnel Department; 6) Internal Control Department; 7) Intelligence Department; 8) Service Department; 9) Customs Department; 10) Revenue Department; 11) Investigation Department. The Board has its central office in the capital Tallinn, and regional offices across Estonia.

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unacceptable and 10 means absolutely acceptable). The index for each nation is calculated using the mean score across these six attitudinal questions. It is important to keep in mind that all scores are closer to 1 (totally unacceptable toward non-compliance behaviours) than 10 (attitudes reflecting total acceptance of non-compliance). Even for those, who receive envelope wages in CEE countries, the median score is 3.83.

<sup>81</sup> Paulus, Alari. 2015. 'Tax Evasion and Measurement Error: An Econometric Analysis of Survey Data Linked with Tax Records', ISER Working Paper Series 2015-10. Institute for Social and Economic Research. <https://ideas.repec.org/p/ese/iserwp/2015-10.html>.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The main cooperation model/tool on undeclared work is the 'Employment register'. Since 1 July 2014, all people who are employed or who are working on a voluntary basis in Estonia must be registered by employers in the new employment register.

On the one hand, the register should reduce undeclared work and increase tax revenue by requiring registration of employees before the actual employment starts, and by making the supervision by taxation officials easier. On the other hand, the purpose of the register is also to increase the amount of electronically gathered data for administrative decisions and to ease the data exchange between different state institutions. The employment register is also the basis for determining the employment related social guarantees (health insurance, pension, and unemployment insurance premiums) and for supervision over the fulfilment of the employment related obligations. The database is used by:

- The Estonian Tax and Customs Board for monitoring the tax liabilities of taxable persons;
- The Labour Inspectorate for making entries into the register on the basis of the decision of the labour dispute committees;
- The Estonian Unemployment Insurance Fund for verification of employment status and registration of persons as unemployed or moving back into work, and for granting unemployment allowances and other unemployment insurance benefits;
- The Estonian Social Insurance Board for verification of employment status and granting different benefits;
- The Estonian Health Insurance Fund for verification of employment status and granting health insurance benefits; and
- The Police and Border Guard Board for exercising supervisory control over the working conditions of foreigners.

Also, every worker can check the system to make sure that the employer has registered them correctly, payments are declared and all taxes are paid. The register data is available for all public bodies requiring employment related information. The objective of the implementation of this system is to avoid multiple submission, collection and processing of the data and to reduce the administrative burden of the employers as well as of the public agencies.

Additionally, the Labour Inspectorate and the Estonian Tax and Customs Board cooperate by sharing case-by-case information on establishments and employers that are suspected of infringing employment and tax law. Also, the Labour Inspectorate and the Police and Border Guard cooperate by carrying out joint inspections based on a cooperation agreement and plan for detection of illegal employment and cases of labour exploitation (e.g. trafficking).

Cooperation with other Member States is mostly based on data sharing. The Estonian Tax and Customs Board shares data with other tax authorities based on the council directive 2011/16/EU and council regulation 904/2010/EC on administrative cooperation in the field of direct taxation. There are also number of bilateral agreements<sup>82</sup> for the avoidance of fiscal evasion with respect to taxes on income and capital. These regulations stipulate both automatic exchange of information and also case by case exchange of information on possible employment relations and tax obligations.

Additionally, the Labour Inspectorate cooperates with other member state authorities in case the undeclared work is related to posting of workers in the framework of the provision of services as stipulated in the Directive 96/71/EC. In these cases, the

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<sup>82</sup> See internet: <http://www.emta.ee/eng/business-client/income-expenses-supply-profits/international-agreements/conventions-avoidance-double>

Inspectorate shares the available administrative data or additionally carries out inspection to gather evidence.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Different policy measures tackle undeclared work, including increasing commitment via awareness-raising and information campaigns to inform workers about the risks, and deterrence approaches that detect and punish non-compliance. Since 2017 a greater effort is being directed to encouraging people and businesses to work legitimately or to help those already participating in undeclared work to legitimise their activities.

### **2.3.2 Measures to tackle undeclared work**

**Enabling compliance - fostering commitment via awareness rising.** The Estonian Tax and Customs Board have launched a campaign website<sup>83</sup> to inform workers and employers about 'envelope wages' and undeclared work. The key message is that these practices are illegal, introduce unhealthy competition and paralyse Estonia's development and the good functioning of society as a whole. In regard to information sharing, the website includes a calculator that estimates loss of income in cases of social risks like unemployment, parental leave, and sickness absence. Also, there are complementary channels of communication, including radio, to raise the awareness.

**Deterrence - improving detection.** Since 1 July 2014, employers are obliged to register their employees in the employment register, which gathers information about employments. All businesses who provide work are required to register the persons employed by them in the register irrespective of the form or the length of the contract. In addition, data on people working on a voluntary basis must also be recorded in the employment register. Hence, all people doing some kind of work must be registered. The employment must be registered at the moment the employee starts working in order to avoid the 'first day of employment' excuses. The termination of employment must be registered within 10 calendar days. Registration is possible via The Board's website, via personnel management programmes of a company or agency or by visiting the bureau of the Estonian Tax and Customs Board in person. It is also possible to use a simplified procedure for first registration by telephone or text message, although it must be supplemented within seven calendar days to be complete. If the employer does not register the start or the end of employment as required, the tax authority may claim penalty payment of maximum EUR 3,200.

Both the Labour Inspectorate and the Tax and Customs Board have carried out targeted control of enterprises for tax avoidance and undeclared work. The activities include inspection visits to company and work sites as well as notification letters. The objective is to prevent the infringement of tax laws and raise law-abiding behaviour among tax payers, thus instead of burdening employers and administrators with offence procedures in the first instance they are given the opportunity to revise their business activities and change them in accordance to the law. In these letters, the companies are asked to revise their accounting and tax related information and give feedback to the tax authority on the results of their business activities. The notification letters give companies a certain time to improve their tax behaviour. In those companies who do not improve their tax behaviour or cannot give satisfactory reasons to the results of their business activities, a control of tax payments and accounting are initiated.

In the competence of the Labour Inspectorate is to find out whether employees have been notified of working conditions in writing (i.e amount of salary, taxes, description of duties, working time etc.) if not, the inspector has a right to make an injunction or start a misdemeanour proceedings. If the inspector suspects that the employer has not paid

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<sup>83</sup> See internet: <http://www2.emta.ee/palk/>

taxes on behalf of the employee or have not registered his/her employees, the inspector provides that information to Tax and Customs Board.

### 1.3.3 Closer cooperation with Social Partners

Estonia's Tax and Customs Board newly adopted strategy for 2017 – 2020 foresees measures for taxpayers awareness raising including deeper cooperation with all social and cross-industry partners on all tax matters.

Bogus Self-Employed

- Counselling, analysis of companies with potential risk, first contact by phone, following subsequent counselling activities including correspondence and meetings with companies;
- Cooperation with Estonian Auditor's Association and formation of a working group;
- Estonian Association of Construction Entrepreneurs

Cooperation for elaborating new provisions to the Public Procurement Act, according to which when submitting a tender, supplier should provide evidence of its six-month wages, if they are not 70% of sectors average, the organizer of tender is obliged to ask for an explanation and can eliminate such supplier from procurement.

Estonian Association of Security Entrepreneurs

In order to combat envelope salaries, undeclared work and underestimated bids in public procurement, the members of the association gave their agreement on disclosure of their detailed tax data, which is used to ensure fair competition and could serve as a starting point for concluding collective agreements in the area of Security services. In cooperation with Tax and Customs Board, members formed a working group, which is dedicated to sectoral analysis, counselling and prevention of possible labour risks.

### 1.3.4 Good practice

There are no policy evaluations on interventions for tackling undeclared work. However, the **Employment Register** would be considered good practice on the grounds that it is a new/innovative measure in the Estonian policy mix that is expected to increase compliance with the labour and taxation regulations. Overall, the employment register has been well accepted by employers and employees (both the Estonian Trade Union Confederation ([EAKL](#)) and the Estonian Employers' Confederation ([ETTK](#)) welcomed the register). It is much easier for employers to register their employees and for the taxation officials to perform supervision, compared to the previous system. State institutions have now more information without the need to require additional documents from persons, hence the register reduces administrative burden.

Since the implementation of the register as of July 2014 up to June 2015, tax revenue has increased around EUR 11.8 million and the number of persons that received declared income increased by 21,000 persons.

However, there are doubts whether the declared wages are correct, as they are mostly around national minimum wage. Hence, it is assumed that full undeclared work and wages is being replaced by partial undeclared wages. Moreover, on construction sites, people have been registered as 'volunteers' who do not seem credible and show that some employers still try to find ways to cheat the system. Although these 'volunteers' account for only around 0.2% of all employees, the taxation officials consider it as a serious problem.

### 1.3.5 Challenges and barriers

According to the study, Shadow Economy in Estonia 2016<sup>84</sup>, 42% of those not satisfied with receiving envelope wages self-reported that they would have lost their job if not doing so. It follows that job and employment security are a crucial push factor of envelope wages and undeclared work. According to the same study, 13% of workers report that they are not against envelope wages and 25% do not have an opinion whether they are in favour of or against these practices. The main reasons for supporting envelope wages are too costly tax burden for employees (67% of those in favour), it is an option for higher income (64% of those in favour) and too costly tax burden for employers (64% of those in favour). These self-reported considerations show that there is a considerable share of undeclared work cases that could be prevented by raising legal awareness and legal certainty.

As discussed above, the institutional factor of partial undeclared work is that the taxation of labour and capital is not proportional, favouring the latter. The incentives in the system motivate to provide services for another company as a juridical person through the person's own private limited company instead of arranging an employment contract. Both parties win from the situation, because if the worker would have an employment contract, then the employer would have to declare and pay social tax (33% of gross wage) and unemployment insurance premiums (0.8% of gross wage) on the remuneration. Since one company provides services to another company, employment taxes need not be paid and the entire remuneration is paid directly to the private limited company. The owner of the private limited company can then decide how much they would pay for themselves as salary and how much they would take out as dividends. In sum, this motivates partially undeclared where a portion of the workers income is received without paying all the taxes.

However, institutional factors could not explain the whole situation as labour market conditions and the economic situation also influence workers' and companies' preferences and behaviour. Prevalence of undeclared work tends to increase during the recession and reduction in labour demand.

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<sup>84</sup> Estonian Institute of Economic Research 2016, op. cit.



## Factsheet on Undeclared Work - FINLAND (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

In Finland undeclared work is defined as work which is paid for but not declared to the tax administration.<sup>85</sup> <sup>86</sup> The 'shadow economy' is a wider concept that consists of 1) undeclared wages, 2) undeclared enterprise income and 3) hidden dividends.<sup>87</sup> Most often undeclared work refers to the activities of SMEs, while in larger companies the problems relate more to different kinds of tax roving advantages for personnel.

Currently the concept of the 'shadow economy' is more frequently used in official contexts than undeclared work, with the shadow economy being defined in different ways, with undeclared work being a rather unambiguous concept according to the authorities. The Law on the Grey Economy Information Unit in the Tax administration states that the shadow economy is an organisational action which neglects statutory payments like taxes, pension, insurance or Custom payments. In the National economy, the definition excludes production that is not accounted for in the National economy. The fiscal definition considers the shadow economy as a legal economic activity that is hidden from the authorities. The illegal economy is defined as criminal activity, and not included in the shadow economy.<sup>88</sup>

#### 2.1.2 Characteristics of undeclared work<sup>89</sup>

The main type of undeclared work is "envelope wages" (hidden employment) in the construction, accommodation and catering sectors. Also entertainment and real estate sectors have been identified as fields of hidden employment. A particular area is household renovation work obtained from the small construction companies or self-employed individuals, which often remains undeclared. Illegal migrant work is not a problem in Finland but related underpaid work amongst migrant workers is, and mostly in connection to the construction and catering sectors.

Shadow wages are most frequently found in the construction sector (7.1 per cent of total wages) and real estate (6.7 per cent). The accommodation and catering industry, as well as the entertainment sector, are also mentioned as an increasing proportion of the shadow economy.

Statistics are not available for the distribution of undeclared work by employer size. Most often undeclared work refers to SMEs, while in larger companies the problems relate more to different kinds of income tax roving advantages for personnel.

Limited evidence is available on the main motivators for undeclared work in Finland. On the basis of authors' contextual knowledge the main motivators relate to heightened profitability risk in different sectors, especially during difficult economic conditions. A relatively high tax rate and high employment expenses also increase the motivation of the employers to use undeclared work. In addition households may have difficulty

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<sup>85</sup> Etelä-Saimaa Magazine (2016). Interview with Heimo Säkkinen, Tax Inspection Chief. <http://www.esaimaa.fi/Online/2015/08/18/Pimeit%C3%A4%20palveluja%20ostaneen%20tunte%20yli%20puolet%20suomalaisista/2015119438441/4>. Accessed 3.4.2016.

<sup>86</sup> Virén, M. (2013).

<sup>87</sup> Hirvonen, M. & Lith, P. & Walden, R. (2010). Finland's internationalizing shadow economy. (Suomen kansainvälistyvä harmaa talous.) Publications of Parliament Audit Committee 1/2010.

<sup>88</sup> [https://www.vero.fi/fi-FI/Tietoa\\_Verohallinnosta/Harmaan\\_talouden\\_torjunta/Harmaan\\_talouden\\_maaritelma\(14464\)](https://www.vero.fi/fi-FI/Tietoa_Verohallinnosta/Harmaan_talouden_torjunta/Harmaan_talouden_maaritelma(14464)).

Accessed 15.4.2016.

<sup>89</sup> Tax Administration (2016). Shadow economy – supervision statistics 2015 (in Finnish).

Release 30.3.2016. [https://www.vero.fi/fi-FI/Tietoa\\_Verohallinnosta/Uutiset/Uutta\\_tietoa\\_harmaasta\\_taloudesta\\_Harmaa\(39511\)](https://www.vero.fi/fi-FI/Tietoa_Verohallinnosta/Uutiset/Uutta_tietoa_harmaasta_taloudesta_Harmaa(39511)).

Accessed 3.4.2016.

affording renovation and other household work due to high expenses. People who receive social assistance, such as unemployment benefit, may be caught in an 'incentive trap', which prevents them from declaring minor assignments so as not to lose benefits.

In the case of restaurants run by migrants, for example, significant benefits of undeclared work are pursued.

### **2.1.3 Estimated scale of undeclared work<sup>90</sup>**

Currently statistics differentiating between the distribution of UDW by type are not available for Finland. Partly, this is due to the focus of research, partly for other reasons like interpretation and use of available data sources. Hirvonen et al. (2010) focus on fiscal tax deficit, legally earned but not properly declared income. This measurement is close to that what is done in Sweden.<sup>91</sup> Nurminen (2008) and Virén (2013, 2014) write about the part of GDP not properly included in official statistics.

In 2011, according to tax inspection authority calculations, the shadow economy accounted for about 5.5–7.5 per cent (EUR 4,000–6,000 mill.) of the total economy.<sup>92</sup> On this basis "shadow wages" were estimated to be 2 per cent of the total payroll (about EUR 1,241 mill.).<sup>93</sup>

However, according to Virén (2014), there were problems in these calculations. According to the tax inspections only about 0.5 per cent of wages were actually undeclared. The problem of estimating was further pronounced due to unrepresentative nature of the inspections.<sup>94</sup> Nurminen (2008) estimates the share of the shadow economy as 1.5 per cent<sup>95</sup> and Virén (2014) considers this more plausible.

According to Hirvonen et al. (2010) shadow wages were most frequent in the construction sector (7.1 per cent of the total wages) and real estate (6.7 per cent). Also accommodation and catering and transport are frequently mentioned, as well as the entertainment sector<sup>96</sup>.

The Government's assessment considering overall shadow economy is based on international sources like Schneider (2011), stating the share of shadow economy about 13.7 per cent, but these estimations are considered well exaggerating from the point of view of Finnish authors.<sup>97</sup>

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

A large number of different ministries and authorities with a broad range of tasks take part in combating the grey economy and economic crime. *The Ministry of the Interior* coordinates the work connected to the grey economy. *The Ministry of Finance* is responsible for taxation.

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<sup>90</sup> Ministry of the Interior (2016). Economic crime and shadow economy. [https://www.intermin.fi/en/security/combating\\_crime/economic\\_crime\\_and\\_the\\_shadow\\_economy](https://www.intermin.fi/en/security/combating_crime/economic_crime_and_the_shadow_economy). Accessed 3.4.2016.

<sup>91</sup> Skatteverket (2014). Skattefelets utveckling i Sverige 2007-2012. Rapport 1.8.2014. [https://www.skatteverket.se/download/18.5c88598914352927a4215e6/1389176760118/Rapport\\_Skattefelets+utveckling+i+Sverige+2007\\_12.pdf](https://www.skatteverket.se/download/18.5c88598914352927a4215e6/1389176760118/Rapport_Skattefelets+utveckling+i+Sverige+2007_12.pdf)

<sup>92</sup> Hirvonen et al. (2010).

<sup>93</sup> Virén (2014).

<sup>94</sup> Virén (2014).

<sup>95</sup> Nurminen, R. (2008). Shadow economy value low in Finland. (Piilotalous arvo Suomessa vähäinen). *Tieto&Trendit* 2008:8., 12–14.

<sup>96</sup> Hirvonen et al. (2010).

<sup>97</sup> Virén (2014).

*The Ministry of Social Affairs and Health* is in charge of social security and occupational safety and health and *Regional State Administrative Agencies* are in charge of the supervision and direction of standards and practices in workplaces. *The Ministry of Economic Affairs and Employment* is in charge of fair competition between companies and labour law and non-discrimination in working life. In addition, other authorities including the police, Customs Bureau and the Finnish Centre for Pensions, as well as authorities dealing with debt recovery and bankruptcies, combat the grey economy.

When combating the issue of UDW the role of the Tax administration and Regional State Administrative Agencies (AVIs) (through their work protection function and contractor's liability function) is crucial. The labour administration's role relates to labour intensive sectors, and there is cooperation between agencies, e.g. with different Ministries, Police, Customs, Pensions' Centre and professional organisations. This takes place in the wider framework of battling the shadow economy, not only UDW. The shadow economy, as stated above, refers also to retail control, insurance payment control and different forms of crime tackling.<sup>9899</sup>

The Tax administration is responsible for tax inspections and AVIs, e.g. to supervise the implementation of Contractor's liability Act, which is designed to decrease the level of undeclared work in the construction sector, as well as in other branches of the economy.<sup>100</sup> AVIs are also responsible for supervising foreign workers.

### **2.2.2 Characteristics of the responsible organisations**

Information on the specific structure of the organisations responsible for UDW related issues is not available. The mentioned organisations operate on a national level and engage in cooperation. The special Grey Economy Information Unit was established in 2011 as part of the Government programme against shadow economy. The Grey Economy Information Unit in Tax administration forms 0.5 per cent of its total personnel (about 5,000 persons in 2014). In 2016, the number of tax inspectors in operational activities was between 500 and 600. The unit informs public, publishes expert reports which enhance the cooperation between different authorities.<sup>101</sup> There are also six AVIs in different regions.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

Little information is available on the nature and models of cooperation between organisations with an interest in UDW in Finland.

However information exchange between them has been strengthened in the context of the Government programme against shadow economy 2011–2015. The new strategy for tackling the shadow economy and economic crime 2016-2020 was agreed on 12 April 2016. In May the strategy was accompanied with the action plan on concrete measures. In line with the requirements of the Parliamentary Audit Committee, the strategy includes internationalisation, a holistic approach to the formulation of the Strategy, consistency in efforts to tackle the shadow economy and its anticipated progress in the long term. The government wants to tackle the shadow economy and economic crime especially by means of preventive action. To be successful in tackling the shadow

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<sup>98</sup> Valtiontalouden tarkastusvirasto (2015). (Tuloksellisuustarkastuskertomus. Harmaan talouden torjuntaohjelmat ja torjuntatyön koordinaatio.) Valtiontalouden tarkastusviraston tarkastuskertomukset 14/2015.

[https://www.vtv.fi/files/4842/14\\_2015\\_Harmaan\\_talouden\\_torjuntaohjelmat\\_ja\\_torjuntatyon\\_koordinaatio.pdf](https://www.vtv.fi/files/4842/14_2015_Harmaan_talouden_torjuntaohjelmat_ja_torjuntatyon_koordinaatio.pdf)

<sup>99</sup> MEE (2011). (Talousrikollisuuden ja harmaan talouden torjuminen rakennus- sekä majoitus- ja ravitsemisalalla -työryhmän mietintö.) Ministry of Employment and Economy Publications. Competitiveness 17/2011. [http://www.tem.fi/files/29563/TEM\\_17\\_2011\\_netti.pdf](http://www.tem.fi/files/29563/TEM_17_2011_netti.pdf)

<sup>100</sup> Pesonen, R. (2011). Contractor's liability Act and combatting shadow economy.

<https://www.rakennustieto.fi/Downloads/RK/RK110202.pdf>

<sup>101</sup> TA (2015). Tax administration action report 2014.

economy and economic crime, authorities need to collaborate and have a common view of the situation. UDW is addressed in this respect. The new operations are concentrated on the Grey Economy Information Unit at the Tax administration, but some new obligations were set on Labour administration also concerning supervision.

Limited information is available on the effectiveness of cooperation between authorities in Finland, with the exception of the Government audit described at 1.3.4. While cooperation between other Member States does take place around the shadow economy, no information is available on cooperation relating specifically to UDW.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The Finnish approach to fighting the grey economy, economic crime and undeclared work main elements are the political commitment in the form of special action programmes since 1996 which have been ratified by the government and co-operation both between different authorities and between authorities and representatives of the private sector, in particular with business and trade unions.

Main measures are proposals for legislation, resources for economic crime investigation, training of authorities, and research and information campaigns. These include:

- Legislative amendments to reduce the potential for co-operation between the black economy and criminal businesses;
- Modernising the powers of the authorities to increase efficiency;
- Enhancing the processing of economic crime to better enforce criminal liability; and
- Making currently confidential official information public to increase transparency in business and to enable self-monitoring by enterprises.

The Finnish approach is multi-method ranging from preventative, awareness rising to increasing ex-post control and strengthening the investigation of economic crime. The effective cooperation and exchange of information between public authorities is a key factor when detecting, combating and investigating financial crimes or undeclared work. A special unit undertaking analysis of the shadow economy was established in 2011 under the auspices of Tax administration, and additional funding was provided to authorities.

Several policy initiatives have been introduced in recent years. While several Governments since the 1990s have sought to tackle the shadow economy, efforts have been increased during the Katainen's Government (2010–2014). This shadow economy programme consisted of Ministerial cooperation with the aim of strengthening coordination, and providing continuity and resources to the authorities including a EUR 300–400 million increase in funding (but not only to target UDW).

### **2.3.2 Measures to tackle UDW<sup>102</sup>**

The fact that no thorough research exists on the policies engaging measures to tackle shadow economy<sup>103104</sup>, was regarded problematic. In 2014 an assessment was made for the Parliament on measures to combat the shadow economy and white-collar crime in 2010–2014 (Katainen's Government). The programme was accompanied by EUR 20

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<sup>102</sup> TA (2015). Tax administration action report 2014.

<sup>103</sup> Virén (2014).

<sup>104</sup> Hirvonen, M. & Määttä, K. (2014). Report to the (eduskunta) Parliament audit committee on measures to combat the shadow economy and white-collar crime in 2010–2014; summary.

Parliamentary Audit Committee Publications 1/2014.  
[https://www.eduskunta.fi/FI/tietoeduskunnasta/julkaisut/Documents/trvj\\_1+2014.pdf](https://www.eduskunta.fi/FI/tietoeduskunnasta/julkaisut/Documents/trvj_1+2014.pdf).

Accessed 3.4.2016.

million additional funding for authorities each year to help combat the shadow economy. The programme was also supported by other projects e.g. to combat white-collar crime.<sup>105</sup> The share of resources specifically directed to UDW measures is however unknown.

Disclosure obligations for the construction sector were introduced in 2014 and managed by the Tax administration, and included monthly lists of workers on site.

One of the main measures to address UDW are awareness rising campaigns, e.g. "Black future" net pages <http://www.mustatulevaisuus.fi/>, and undertaken through cooperation between the Tax administration, Police and Customs.

Public procurement and public subsidies have been identified as important target areas in the combat against the shadow economy.<sup>106</sup>

The labour administration was responsible for clarifying different measures and the Ministry of Employment and the Economy for preparing legislation relating to e.g. constructor's liability act and obligation to deliver receipt in the cash trade. Paying wages in cash was forbidden in 2013 and accountant became obliged to report their suspicions. Also payments that pass the accounting and cash registered became under surveillance.

The Grey Economy Information Unit has studied the impact on the construction sector of the legislative changes concerning the Information Reporting Requirement measure. The evaluation included a study of legislation introduced since 2011 affecting construction companies' independent notifications, i.e. 1) Tax number register/Independent tax numbers, 2) Reverse charge mechanism for VAT, 3) Extended duty to notify contractors and employees in the construction sector based on the Tax Administration report<sup>107</sup> including statistical and qualitative data. The new measure appears quite successful in terms of increasing declared businesses and work. The legislative changes concerning the construction sector have boosted tax revenue and increased companies' independent notifications given for tax purposes. This increase in notifications is seen in the higher payroll figures, mainly arising from new companies. The extent to which the pay of foreign nationals is included within the tax system has improved, although deficiencies in taxation coverage were also found. Overall it seems that the culture has become healthier in terms of transparency and adequate payrolls. However, on the downside is the increased administrative burden both on the side of the contractors and the tax administration. Further development is called for on the level of concrete practices, information exchange and especially in the use of electronic systems to foster the technical processing of information. Cuts in the public authorities' resources may threaten the implementation of the new system in long term.

In addition, some indicators exist on the level of the economic crimes and police investigations but not on UDW due its hidden nature. The number of crime reports made by the Tax administration remained the same in 2013 and 2014 (about 500) and the Tax administration has statistics on identified hidden wages.

Positive feedback has been received concerning the media campaign.

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<sup>105</sup> Hirvonen, M. & Määttä, K. (2014). Report to the eduskunta audit committee on measures to combat the shadow economy and white-collar crime in 2010–2014; summary. Parliamentary Audit Committee Publications 1/2014. [https://www.eduskunta.fi/FI/tietoaeduskunnasta/julkaisut/Documents/trvj\\_1+2014.pdf](https://www.eduskunta.fi/FI/tietoaeduskunnasta/julkaisut/Documents/trvj_1+2014.pdf). Accessed 3.4.2016.

<sup>106</sup> Tax Administration (2015). Grey Economy 2015 reports grey economy in Finland and how it is fought against. Tax Administration Bulletin 11/17/2015. [https://www.vero.fi/en-US/Tax\\_Administration/News/Grey\\_Economy\\_2015\\_reports\\_grey\\_economy\\_i\(38729\)](https://www.vero.fi/en-US/Tax_Administration/News/Grey_Economy_2015_reports_grey_economy_i(38729))

<sup>107</sup> Rakentamisen tiedonantovelvollisuus urakka- ja työntekijätiedoista - lainsäädännön vaikuttavuus 7/2017

### 2.3.3 Good practice

Measures directed towards the construction sector like reverse value added tax and the Contractor's Liability Act have had positive results. Reverse value added tax means that the client pays VAT to the state instead of contractor in the construction sector. The liability act means that all contractors have an obligation to check contracting partners' ability to discharge their statutory obligations by checking certain information and registers before making an agreement on temporary agency work or subcontracted labour.<sup>108</sup> Efforts to raise awareness have been important in combatting the increasing shadow economy. Finland has embraced an overall shadow economy tackling policy.

The household deduction model is one long term initiative which encourages households to use declared work in renovations and other household tasks. This has had financial effects and also increases public awareness of the negative aspects of the shadow economy. In 2016, the household deduction is EUR 2,400 for a person (and EUR 4,800 for a household) for a renovation or other household work obtained from contractor and paid against receipt. Deduction is made from the households' income taxes (EUR 100 own-risk share).

### 2.3.4 Challenges and barriers

A key challenge in Finland is the increasing size of the total shadow economy, although estimations are controversial and inaccurate. UDW is especially prevalent in the construction sector but is also spreading to the other sectors. The economic crisis, high tax rate and inflexible labour market, and incentive traps also create the conditions for UDW to increase.

According to the Government audit, the programme to tackle the shadow economy is not yet sufficient, is poorly defined, is fixed term, and has projects within it which are poorly coordinated - although no evaluation studies currently exist.<sup>109</sup>

The shadow economy has been less of a concern while more general economic issues have been under political debate. Still, committees are continuously discussing further measures to improve measures.

In conclusion, while the shadow economy has become a focus for attention in Finland, this is less the case for UDW. However, UDW activities have now spread to new sectors, and the main challenge is now collaboration also cross the borders, having a common strategy and promoting joint activities between different authorities also in practical level. There seems to be a chronic under resourcing of the controlling authorities, and challenges in developing effective policies.

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<sup>108</sup> Laki tilaajan selvitysvastuusta ja vastuusta ulkopuolista työvoimaa käytettäessä (22.12.2006/1233) <https://www.finlex.fi/fi/laki/ajantasa/2006/20061233>

<sup>109</sup> Valtiontalouden tarkastusvirasto (2015). (Tuloksellisuustarkastuskertomus. Harmaan talouden torjuntaohjelmat ja torjuntatyön koordinaatio.) Valtiontalouden tarkastusviraston tarkastuskertomukset 14/2015. [https://www.vtv.fi/files/4842/14\\_2015\\_Harmaan\\_talouden\\_torjuntaohjelmat\\_ja\\_torjuntatyon\\_koordinaatio.pdf](https://www.vtv.fi/files/4842/14_2015_Harmaan_talouden_torjuntaohjelmat_ja_torjuntatyon_koordinaatio.pdf)

## **Factsheet on Undeclared Work – FRANCE (September 2017)**

### **2.4 Nature and Estimated Scale of Undeclared Work**

#### **2.4.1 Definition of undeclared work**

In the French legal context, undeclared work refers to illegal work defined in the labour code by the SME Law of 2 August 2005.

Illegal work involves a number of different types of major fraud, which contravene or abuse elementary rules linked to independent vocational activity, in the name of an enterprise, as well as rules linked to the hiring or employment of employees.

Those frauds are:

- Dissimulated [hidden] work (travail dissimulé);
- Bargaining;
- Illicit workforce loans;
- Employment of a foreigner without a work permit;
- Accumulation of irregular jobs; and
- Replacement income fraud.

The definition of dissimulated work refers to: "a person undertaking activity without having declared it as an enterprise, and an employer dissimulating part or all of its employees for part or all of their working hours". This definition has replaced the one formulated in the Law of 11 March 1997 relating to clandestine work, particularly to avoid confusion between undeclared work by employers and foreigners in an illegal position (without a residence permit). In other words, the legal definition of dissimulated work refers to two kinds of fraud: undeclared activity and undeclared employees.

If an enterprise is not registered in the Trade Register (Registre du commerce) and Professions Register (Registre des métiers) when this is compulsory, or if it does not declare its activity to social protection bodies or the tax administration, this is classed as dissimulated activity. If an employer does not make a declaration to the official bodies for the recruitment of its employees, does not present a pay slip for each employee, and/or does not give the correct number of working hours, this is classed as dissimulated employment.

The four main administrations or agencies in charge of fighting against illegal work – the Labour inspection, Police, social welfare agency (URSSAF) and other state departments like tax and customs, all follow the same definition.

In France, dissimulated work is penalised in the Labour Code with a maximum of three years imprisonment and a EUR 45,000 fine for individuals, EUR 225,000 for enterprises; by the Trade code with an additional penalty: interdiction of managing companies for five years; and by the Social Security Code requiring extra social contributions and penalties to be paid.

Tougher penal sanctions and special investigation techniques for UDW have been introduced (Dissimulated [hidden] work; Bargaining; Illicit workforce loan): with new aggravating circumstance punishable up to ten years' imprisonment and a fine of €100,000. This allows for investigative powers of judicial police officers (wiretaps, spinning) (art. 13 de la loi 2014-790 du 10 juillet 2014).

New penal sanctions have been created:

- Prohibition from collecting for a maximum period of 5 years "any public aid awarded by the State, local authorities, their establishments or groups, and any financial assistance paid by a private with public service mission (art. 12 de la loi 2014-790 du 10 juillet 2014, art. 131-39 du code pénal - Décret n° 2015-364 du 30 mars 2015).

- A new additional penal sanction in the case of conviction for illegal work: the dissemination of the decision on a dedicated Ministry of Labor website, with a sentence of up to a maximum of two years.

#### **2.4.2 Characteristics of undeclared work**

The fight against illegal labour has become more effective in recent years, with fewer controls but being better targeted and more efficient.

In 2014 – the last year with available data: 57,300 companies were inspected, including 38% in the construction sector, 25% in hotels and food/catering and 18% in agriculture sector. Some 15,300 offenses of illegal work were identified, of which 75% were for hidden work and 13% were for employing a foreigner without a work permit. In the priority sectors, one third of inspections are joints inspection between different control bodies.

There was also a sharp rise in social security adjustments within the priority sectors, rising to EUR 339 million in 2015 from EUR 253 million in 2014 and EUR 139 million in 2013. In agriculture this rose to EUR 10 million in 2014 from EUR 8.7 million in 2013.

Control services are professionalised and specialised, with an important education campaign and the creation of services dedicated to the national and regional level.

In 2016, 6,800 reported offenses for illegal work have been recorded, compared to 6,750 in 2015.

In practice, dissimulated work mainly concerns cases of the under-declaration of employees or under-declaration of working hours. In two thirds of cases, the offence concerns the deliberate failure to complete the official hiring declaration, while dissimulation of working hours represents 5% of offences (but under-estimated according to the inspection bodies). Failure to provide pay slips represents 14% of offences. Bogus status (bogus interns, bogus volunteers, bogus self-employed) represents only 3% of sanctions, a drop on the 2012 figure (7%). The French administration underlined a global increase in the number of sanctions linked to illicit workforce loans and bargaining (18% against 11% in 2012) while the number of sanctions linked to the use of foreign workers without a work permit is stable (11% in 2015). Moreover, over the past seven years, we can identify two main trends across administrative data: 1) the increasing number of sanctions due to dissimulated work (66% to 72%); and 2) the decreasing number of sanctions for using foreigners without a work permit (14% to 7%). By sector:

- The construction industry, the transportation sector and seasonal work in farming are the main sectors for all categories of illegal work;
- The hotel and catering services, the food retail sector and the services sector (and notably personal care services) are the main sectors for using bogus status or foreigners without a work permit; and
- The entertainment sector is the most affected by dissimulated work and bogus status.

According to agents from the French administration responsible for inspection, the economic crisis has been a factor leading to the acceleration of undeclared work. Increased competition has led some companies to try to preserve their profits through illegal methods (e.g. false subcontracting, false temporary agency working, under-declaration of the volume of working hours, etc).

The consequences of the crisis, namely levels of unemployment, increased poverty and higher taxation for companies, has reinforced the risk of undeclared work. According to some economists, an increase in the 'black' economy can be observed when respecting rules represents a disproportionate cost for companies. Furthermore, the specific situation of French overseas areas must be highlighted. These overseas areas have a high level of unemployment and poverty, strong clandestine immigration and, more



particularly in Guyana and Mayotte, a low level of education can partly explain a high degree of undeclared work.

More recently, some new trends are developing regarding undeclared work:

- More and more interns are employed by young start-ups into “co-working spaces” or incubators with a certain porosity between legal status and an informal status. So the digital economy could be a factor that stimulated undeclared work, according to a report by CESE<sup>110</sup>.
- Frauds with posted workers: the Ministry of labour (Labor General Department of lab, DGT) has identified nine main countries including Portugal, Poland, Romania and Spain. In 2016, about 354,000 workers were officially registered as posted workers. Main frauds are with illegal work (under declaration of working hours; stable activities in France without establishment, etc). The labour inspectorate organised 14,800 inspections in 2016 (compared to 17,000 inspections for illegal work).

## **Prevention of illegal work**

In the field of prevention, several conventions to combat illegal work involving the State and the professional branches were signed in 2016 concerning private employers (September 9, 2016), agriculture (May 2016) and construction (February 23, 2016).

### **2.4.3 Estimated scale of undeclared work**

According to URSSAF<sup>111</sup>, the French administration in charge of collecting social contributions, 7 in 100 enterprises are using dissimulated work practices. This data is confirmed by recent publications from the European Commission<sup>112</sup> which estimated that, of the 2 million enterprises settled in France, 7.3% were involved in dissimulated work<sup>113</sup>. According to the A.T. Kearney Study on the shadow economy in Europe<sup>114</sup>, the shadow economy represents 10.8% of the GDP in France, while in Europe the scale can vary from 7 to 16%. France (like Germany and the United Kingdom) is identified in the group of European countries where the shadow economy is lower (other countries include Austria, the Netherlands, Ireland and Scandinavian countries).

## **2.5 Institutional Framework**

### **2.5.1 Responsibilities for addressing Undeclared Work**

Preventing and controlling undeclared work is carried out by three national authorities/organisations who are responsible for identifying, tackling and/or preventing UDW:

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<sup>110</sup> Source: Social, financial and economic impacts of undeclared economy, June 2014, Environmental, Social and Economic Council Advices - Bertrand Farriol.

<sup>111</sup> CESE Advise on posted workers, September 2015

<sup>112</sup> “The shadow economy comprises legal business activities that are performed outside the reach of government authorities. These activities typically fall into two categories that remain common across Europe. The first is undeclared work which (...) includes wages that workers and businesses do not declare to the government to avoid taxes and documentation (...). The other (...) comes from underreporting (...) to avoid some of the tax burden.” The Shadow economy in Europe, 2013 – A.T. Kearney, Visa, Friedrich Schneider, 2013.

<sup>113</sup> Social, financial and economic impacts of undeclared economy, June 2014, Environmental, Social and Economic Council Advices - Bertrand Farriol.

<sup>114</sup> “The shadow economy comprises legal business activities that are performed outside the reach of government authorities. These activities typically fall into two categories that remain common across Europe. The first is undeclared work which (...) includes wages that workers and businesses do not declare to the government to avoid taxes and documentation (...). The other (...) comes from underreporting (...) to avoid some of the tax burden.” The Shadow economy in Europe, 2013 – A.T. Kearney, Visa, Friedrich Schneider, 2013.

- Labour inspectors - civil servants belonging to the Labour Administration: these focus on illegal work.
- Social Security Agencies ("URSSAF" et "Caisses de Mutualité Sociale Agricole) - in charge of collecting the social taxes which finance the social security system, and focused on controlling employer declarations based on the calculation of social contributions to be paid, and recovering the tax adjustment in case of violation.
- The agents of the Central agency for the fight against illegal work - OCLTI - which intervene under the responsibility of the Gendarmerie and Police.

Also, civil servants within the tax and customs administration can participate in the fight against illegal work and immigration. Coordination is ensured by the national unit in charge of fighting against fraud, which intervenes under the responsibility of the Ministry of economy and, at local level, by the CODAF.

### **2.5.2 Characteristics of the responsible organisations**

The role of labour inspectors is to control employers at the workplace. The role of URSSAF Agents is to control employer's social contribution declarations and make adjustments in cases of violation. Agents are also able to intervene, at the other organisations' requests, to control and make the tax adjustments when fraud is identified. They are also in charge of recovering the amounts taxed in case of violations. The role of OCLTI agents - police and gendarmerie members - is to intervene in the fight against illegal work in collaboration with the central office on illegal immigration.

In 2012, the French Labour Inspectorate underwent important reforms to improve its efficiency and to strengthen its intervention capacity. In relation to undeclared work, the reforms aimed to improve the detection of new types of fraud, including the most complex ones.

One of the most important measures was the establishment of specialised regional units which were set up specifically to support and monitor the fight against UDW. They act to support the local control units to fight UDW.

The Labour Inspectorate was seen as too generalist and local, which made it difficult for the services to identify complex fraud and intervene when needed. The reform aimed at strengthening the coordination and communication between the different levels of the Labour Inspectorate (local, regional, national), and to better adapt to the evolving context which included, amongst other things, the emergence of more complex types of fraud.

The reform was initiated in 2012 and progressively implemented in 2014. Other aspects are still in the process of being implemented.

The reform of the Labour Inspectorate created local control units which are competent to act on the ground in their delimited area. While the units have a general remit, the fight against undeclared work is one of their main tasks.

These local units are supported by the new regional units. These specialised units act to support the local units which do not always have time and resources to invest in the fight against undeclared work (140 labour inspectors). Also, due to their wide regional dimension, they cover a large part of the territory and can more easily identify cases of undeclared work that would not only concern a single workplace but are organised across several regions and involve several operators based in different regions.

In addition, the reform introduced a national group for monitoring, support and control which supports local services on subjects of national importance (GNVAC). While the group is not dedicated to UDW it has nevertheless been its main focus since its creation. This national group is seen as a very useful central monitoring point to identify new complex fraud and also to respond to requests from other services. The French Liaison Office established by Directive 96/71 / EC of 16 December 1996 on the posting of workers is a component of the GNVAC. In 2016, it was the subject of 734 requests.

### **2.5.3 Cooperation and collaboration between national and cross-border authorities**

Created in April 2008 by order of the French Prime Minister and the French Minister for Finance, Public Funds and State Reform, the national anti-fraud Unit (DNLF) is the main organisation in charge of steering and coordinating the different organisations in charge of fighting against fraud. Its fields of responsibility go beyond illegal work and involve all kinds of fraud (e.g. tax fraud). Nevertheless, two thirds of its work is focused on illegal work. To this end, the DNLF works alongside the major State-run administrations and social welfare organisations, and the Police, Gendarmerie and Customs also assist in furthering its objectives. Its missions are to: improve the knowledge on fraud; ensure effectiveness and coordination of actions implemented to fight against fraud; contribute to the recovery of tax and social contributions in case of sanctions; coordinate all action at international levels; and pilot activities of the 'anti-fraud' operational committee at local level, CODAF<sup>115</sup>.

This organisation, which has a transversal character, is composed of 12 high level executives with an 'anti-fraud' profile. Missions are implemented in partnership with the following different administrations:

- The Treasury and Home Office;
- For tax Issues : Public Revenue Office (DGFiP), Public Customs and Tax Office (DGDDI);
- For Social Welfare Issues: the social Security Agencies composed of the Family Benefits Agency (CNAF), Central Social Security Office (ACOSS and the regional representation with URSSAF), Health Benefits Agency for Employees (CNAMTS), Welfare for the Elderly Agency (CNAV), Independent Social Regimes Agency (CNRSI ) and Agricultural Insurance Agency (CCMSA);
- Social Welfare Agencies: Job Centre (Pôle Emploi), Unemployment Benefits Agency (UNEDIC) and Employee Insurance Agency (AGS); and
- The Labour Ministry (general department of work, DGT).

Professional training programmes are a key tool in the promotion of an anti-fraud culture. The DNLF<sup>116</sup> organises specific training regimes which totalled over 7,700 hours in 2009, 18,000 in 2010 and more than 35,000 in 2012. These regimes provide officers, in particular those responsible for performing checks or in front-facing roles, with dozens of specific training programmes on the use of investigative tools, detection of social fraud and illegal labour, and inter-agency cooperation.

#### **2016: A new national organisation for monitoring and operational coordination**

A new national monitoring organisation, meeting twice annually between DGT, DSS and DNLF, has been introduced to better manage the implementation and monitoring of the national plan to tackle illegal work between the main administrations/bodies involved in this field. The organisation is responsible for:

- Coordinating the monitoring function on illegal labour practices to analyse their evolution and progress in their detection and targeting;
- Defining a small number of operational axes on which several services are mobilized in a coordinated manner throughout the year;
- Acting on the tools and measures to be mobilized to increase the effectiveness of control: interinstitutional training, sharing of experience, meetings of the Regional services, coordination on sanctions, shared use of information systems and communication of information between administrations, etc; and
- Monitoring the implementation of national and European legislation and jurisprudence to combat illegal work for better proposing amendments.

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<sup>115</sup> Comité opérationnel départemental anti-fraud

<sup>116</sup> All information accessible on <http://www.economie.gouv.fr/dnlf>

As a national group for operational coordination between all enforcement bodies, the organisation coordinates these services on significant illegal work cases to exchange information on their activities and to agree on their modalities of intervention. It can also be a place for exchanges on feedback and good practices. The group meets every two or three months. The expert body brings together experts from the administrations and control bodies on the legal side and methodological aspects.

The national unit is also piloting the CODAF at the regional level, which was officially implemented in 2010 after two years of experimentation. It comprises State representatives (police, tax and customs administrations, labour administration, social welfare issues, social welfare agencies) and is presided over locally by the Prefet (representative of the State at local level). The goal is to improve mutual understanding between administrations and agencies and to organise combined operations, mutual learning and share experience to improve the fight against fraud. In recent years, the CODAF has detected more than 25% of dissimulated work violations, next to the operations managed by each organisation. The national unit is piloting the CODAF by giving technical and legal support to the committees, by suggesting actions and by dedicating three officers (one magistrate, two police chiefs) to run the CODAF and answer the questions raised by participants. With the implementation of the national Unit and the CODAF, the volume of detected violations has strongly increased over the past years.

Finally, at the international level, the national anti-fraud unit intervenes in specific types of international fraud such as active businesses non-declared in a tax or social capacity, fraudulent or improper relocation of French businesses, and direct sale to individual clients via trade fair, advertising or home sale.

Administrative cooperation between Member States in the field of posting workers takes place through the liaison office. On the one hand, France has a national liaison office, integrated within the national control unit in Labour DG, and on the other hand, decentralised liaison offices within regional labour inspectorate services, in charge of exchanges with border countries. All services and control bodies responsible for fighting illegal work can ask for the liaison office.

France also wishes to strengthen transnational co-operation in the fight against undeclared work in three areas:

- The development of bilateral cooperation against UDW;
- Active participation in the activities of the European UDW; and
- France is also engaged in the Eurodétachement project

## **2.6 Policy Focus and Measures**

### **2.6.1 Policy approach**

Over the past years, the policy framework was defined under the National Action Plan against illegal work 2016-2018, elaborated by an internal state dialogue. The plan is based on the following main goals:

- Strengthening the fight against unfair social competition at the European level.
- Fighting against posting fraud (targeting complex fraud situations in risk areas, fraud at the establishment, fraudulent use of temporary work, misappropriation of the intra-group).
- Combating the most serious forms of illegal employment: abusive use of certain statutes (such as bogus self-employment); emerging frauds related to the digital transformation of the economy; conditions unfit for accommodation and work, especially those involving vulnerable persons and trafficking in human beings; the struggle against the employment of foreigners without work titles and especially in the organized sectors; and an axis specific to the transport sector.

- More effective controls to implement the levers of action offered by the changes for strengthening the legal arsenal, by strengthening coordination between actors, and training by mobilizing the whole range of fines and penal offenses.
- Prevention and awareness.

### **2.6.2 Measures to tackle UDW**

In this context, the legal framework has been strongly reinforced in recent years with the reform of labour inspections implemented at the beginning of 2015, the Act on the fight against unfair competition of 11 July 2014, the act for growth, activity and equal economic opportunities of 6 August 2015 (known as the Macron Act), and finally the 8 August 2016 Act.

The recent reform of the Labour Inspection system attempted to give a stronger response to increasingly complex frauds with the creation of specific units under the work inspection organisation: implemented at the beginning of 2015, there is now one unit per region. A national group of inspectors oversees the coordination of actions and works on sensitive cases.

The 2014 Act introduced the opportunity for the court to establish a 'black list of companies', accessible on the website of the Ministry of labour for the public including clients and prospects. The decree was published at the end of 2015. Registration under this sanction will strongly impact on the company's brand and their attractiveness.

The 2015 Act introduced some new measures looking at posting workers: a strong increase of financial sanctions from EUR 10,000 to EUR 500,000, the opportunity for the Prefet to more easily stop a building project, a compulsory activity ID card for each employee in the building industry (which has been progressively implemented since 22<sup>nd</sup> March 2017), and the opportunity to immediately stop any governmental aid if evidence of UDW is found.

It is noteworthy that when presenting the draft Macron Act, the Prime Minister announced a systematic inspection of 500 main construction areas with the aim of detecting illegal practices. These inspections must be implemented within a year under the responsibility of the CODAF, managed by the Prefet.

The law of 8 August 2016 supplemented provisions aimed at combating fraud in posting workers, and especially:

- Facilitation of controls (identity card for building sites);
- Administrative fines and enhanced sanctions to halt a situation immediately (e.g. suspending the provision of services in the absence of a prior declaration of posting workers);
- To reinforce the liability of main contractor and user undertakings for all the subcontracting chain (e.g. the main contractor is responsible for declaring work accidents to the labour inspectorate); and
- Access for all control bodies and services involved in tackling illegal work to prior posting workers declaration data, and extending communication rights between them.

### **2.6.3 Good practice**

Examples of good practices include:

- A national group for operational coordination between all enforcement bodies - coordinating services on significant illegal work files to exchange information on activities and agree on modalities of intervention. Providing a place for exchanging feedback and good practices, the group meets every two or three months.
- Rapid and strong ownership of new administrative fines - between July 2015 and December 2016, 1,077 fines (including 917 in 2016) were imposed for an amount of EUR 5.7 million. The strong increase in administrative fines, introduced by law of 10 July 2014, is continuing, and imposes penalties for failing to comply with

the reporting formalities related to the posting of workers in France; sending a prior posting statement to the labour inspectorate and appointing a representative in France. The construction sector accounts for 75% of the fines imposed.

- A significant increase in the number of prefectural decisions of temporary closures of establishments (307 against 233 in 2015) and cases under examination at 31 December 2016 (116 cases compared with 68 cases in 2015). 18 notifications of institutional closures relate to shortcomings in the context of international services. Better organisation is now in place to fight illegal work both at the national level with dedicated units, and at the local level with the involvement of different agents.
- More combined teams (with different backgrounds) for implementing inspections and using and crossing data from different bodies (tax administration, labour inspection, central office for fighting against illegal work) with local coordination.
- The better targeting inspections on some sectors and types of enterprises.

#### **2.6.4 Challenges and barriers**

In recent years, the fight against illegal work and fraud at posting workers has benefited from a considerable strengthening of its legal arsenal by several successive laws, the creation of new levers for sanctioning and empowering fraudsters and main contractors.

It has also transformed the organisation of the labour inspectorate (establishment of the national control group, specialized regional units on the fight against illegal work, etc.) and set up the conditions for the coordination of the inspectorate, and the administrations and services in charge of combating illegal work.

These measures are already producing significant positive effects. If adjustments are sometimes necessary, the challenge is now more in the implementation of this framework and sanctions than in developing a new legislative arsenal.

The effectiveness of the fight against illegal work implies, however, intensifying and operationalising cooperation between European countries against unfair social competition, in order to better analyse, detect and take joint action to prevent and address the various forms of undeclared work, by:

- Ensuring that the requested information is communicated to the liaison office irrespective of the national administrative organisation;
- Allowing the reporting of fraud with a proven transnational dimension to all Member States concerned; and
- Allowing the transmission and exploitation of data from the V.I.E.S. database (established pursuant to Regulation 2010/904 of 7 October 2010) for the purpose of illegal work.

However certain dimensions of the holistic approach need to be strengthened, including information, awareness raising, training of stakeholders and strengthening the role of the social partners. Moreover, there are still significant gaps in control: on the one hand, the investigative powers of the labour inspectorate have not undergone any significant reinforcement to deal with increasingly complex fraud (including in the digital economy), and the compartmentalisation of access to information systems and databases by supervisory authorities in the fight against illegal work and fraud with working workers.

## Factsheet on Undeclared Work – GERMANY (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

In Germany, undeclared work is defined by the 2004 Act to Combat Clandestine Employment (last amendment 2014) (*Schwarzarbeitsbekämpfungsgesetz* SchwarzArbG). The Act applies to services or work performed which the employer, entrepreneur or self-employed has not declared to the social security authority, has not paid contributions and has not met recordkeeping obligations. Second, undeclared work also encompasses services and work for which a taxable person is not meeting his/her tax obligations. Third, the law mentions explicitly social benefit recipients who do not declare their income from services or work to the relevant social security authority. Fourth, the law applies to persons who have not declared their economic activities according to the Trade, Commerce and Industry Regulation Act (§14 and 55 of the *Gewerbeordnung*) or fifth, if applicable, are not registered at the Skilled Trade Register (§ 1 Crafts Code). Services and work provided for family members or for helping neighbours or for self-subsistence according to the Housing Act are excluded, if they are not profit oriented and are performed for low remuneration.

One form of illegal employment is the violation of the Posted Workers Act (*Arbeitnehmer-Entsendegesetz*), of the Act on the Provision of Temporary Workers which regulates temporary agency work, (*Arbeitnehmerüberlassungsgesetz*), of the Minimum Wage Act (*Mindestlohngesetz*) as well as the illegal employment of foreigners.

#### 2.1.2 Characteristics of undeclared work

Depending on the sector and the type of employment, undeclared work can take on several forms:

- Violations of the trade, business and crafts registration obligation include not only cases of non-registration but also of false registration e.g. declaring activities which do not need to meet specific requirements, for example, instead of the eventually performed activities, the declared manager, who formally meets the skills (e.g. Meister level) and other administrative requirements is de facto not the manager as reported by the Länder authorities. In these cases the skills level of the person who is de facto the manager would not allow him or her to set up the business (Federal Finance Ministry, 2013).
- Bogus self-employed workers ("Scheinselbstständigkeit"). In this context both employment of national and foreign workers are often observed, in particular, in the construction sector, the hotel, restaurant and catering industries and the shipping, transportation and related logistics industry.
- Declaration only of part of the income from self-employment to the tax and the social security institutions.
- According to the Eurobarometer report 2014, envelop wages play a minor role in Germany. However, the splitting of pay of an employee across several fictive employees to make use of simplified and reduced tax and social security requirements, in particular in the context of minijobs, is observed. Moreover, a common violation consists in the declaration of a mini job, although in reality more hours are worked and paid. In addition, cases are reported where companies were created or used by the employer of the undeclared worker; bogus companies issue bills as subcontractors for activities which were never carried out and were not paid. The volume of the fictitious invoices is used to pay the wage of the undeclared workers. Thus, the employer can deduce the wages as costs from their taxes (Abdeckrechnungen).
- Violations of the Posted Workers Act, with paid wages below the collective wage agreements on minimum wages in several sectors. Other infringements relate to non-compliance concerning other minimum standards of working conditions (e.g. holiday pay, vacation allowance, working time, safety at the workplace).

Among reported infringements, incorrect recording of worked hours was quite common (Federal Ministry of Finance 2013). Cases of bogus posting of workers were reported.

- Wages paid below the national minimum wage level (since 2015).
- Cases of illegal temporary agency work were reported, where the temporary work agency did not have a valid permit from the PES (Bundesagentur für Arbeit). In some cases temporary agency workers declared themselves as self-employed.
- Illegal employment of foreigners.
- Abuse of social benefits, in particular unemployment benefit II (Arbeitslosengeld II). Undeclared work occurs when the claimant is working more hours and getting more pay than has been explicitly allowed by the PES (in case of unemployment benefit receipt).

According to results of the controlling authorities, a particular focus for undeclared work is placed on the following **sectors**: construction, hotel, restaurant and catering industries, passenger transport services, shipping, transportation and related logistics industry, fun-fair and exhibitor trade, forestry, building cleaning services, constructing and dismantling fairs and exhibitions and the meat industry. These sectors are explicitly named in the Act to Combat Clandestine Employment and §28a(4) of the Fourth Social Code (obligation to declare workers working in these sectors to the social security insurance immediately, at the latest from first day of work). Workers in these sectors need to carry their identity cards or passports with them (§ 2a (1) Act to Combat Clandestine Employment). The incidence of undeclared work is high in the household sector. According to data of the German Socio-economic Panel from 2010, 95 % of the 4.5 million private households who are employing a maid or a housekeeper, do not declare the worker. In contrast to the number of mini jobs in companies, which declined, the number of mini-jobbers in private households increased over the past decade.<sup>117</sup>

There is no information on the **distribution of undeclared work by company size**.

According to the employers' associations and the crafts associations the high labour costs and tax levels are the **main motivating reasons for undeclared work**. The employers' associations also see the restriction in the labour access for immigrants as an important driver for undeclared work and illegal employment. The acceptance of low wages and below average working conditions by some foreign workers and the gains that can be made by some companies as a result of this situation also lead to undeclared work.

Undeclared work in private households is linked to the fact that households cannot deduct costs for employing them from their taxes in contrast to companies<sup>118</sup>. Private households only profit from a limited tax bonus for crafts services in private households, according to § 35a (3) of the Income Tax Act. Also, undeclared workers have an interest in not declaring work if this would lead to a cut or withdrawal of welfare benefits.

### 2.1.3 Estimated scale of undeclared work

Macro-based calculations of the IAW Tübingen estimate the size of the German hidden economy in 2015 to be around EUR 339 billion. That would constitute 12.2 % of the official GDP.<sup>119</sup> The macro-approach uses the econometric estimates in which the size of the black economy is estimated via indicators like tax burden, density of regulations,

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<sup>117</sup> Minijob Zentrale (2012), Heimliche Helfer, 4. Trendreport.

<sup>118</sup> Enste, D. (2012), Undeclared Work and the Shadow Economy (Schwarzarbeit und Schattenwirtschaft), in: Wirtschaftsdienst 2/2012, p. 136-138.

<sup>119</sup> Schneider, F., Bookman, B. (2015), The size of the shadow economy – methods and calculations for 2015 (Die Größe der Schattenwirtschaft – Methodik und Berechnungen für das Jahr 2015), JKU/IAW, Linz, Tübingen.



working times, cash flows etc. Due regard must be given to the fact that undeclared work is only a part of hidden economy.

The Rockwool Foundation used survey results among 18-74 years old to estimate the size of undeclared work in Germany (7.2 % in 2006<sup>120</sup>), although the definition of undeclared work in these surveys goes beyond the terms of undeclared work including e.g. neighbourhood help or do-it-yourself activities. Eurobarometer shows a smaller extent of undeclared work.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing Undeclared Work

In the 2004 Act to Combat Clandestine Employment, the **Federal Customs Administration** and its financial control of undeclared work unit '*Finanzkontrolle Schwarzarbeit*' (FKS) have been given extended authority and an important role to combat undeclared work. Among other rights, they are authorised to conduct unannounced inspections of staff and/or business records. For that purpose they are entitled to enter production sites and other business premises and to check trucks and cars, and they are allowed extensive rights to control tax and social security contributions. If offences are detected, the FKS initiates preliminary proceedings and conducts the investigations. In the preliminary proceedings the FKS has the same rights and duties as the police authorities. In some sense, they can be seen as the controlling and investigative instrument in the fight against undeclared work on the federal level.

In addition other institutions are responsible for tracking undeclared work and for claiming reimbursement of damages: the main institution responsible for detecting social security contributions fraud is **the pension institution** through the *Prüfdienst der Rentenversicherungsträger*; detecting tax fraud is the responsibility of the **fiscal authorities of the Länder**; tracking welfare benefit abuse according to the Second and Third Social Code is the responsibility of **the PES** (*Bundesagentur für Arbeit*). *Länder* authorities are responsible for detecting offences in the area of registration of business, trades and crafts. In March 2017, an amendment to the Act to Combat Clandestine Employment came into force, which gives the *Länder* authorities more competencies to control and audit in the area of the registration of business, trades and crafts. Data are exchanged between the registry of (means-tested) unemployment benefit recipients and declared work periods by employers. In cases where misuse is suspected, the PES informs the FKS, which conducts further investigations.

### 2.2.2 Characteristics of the responsible organisations

The main organisation carrying out controls and on-the-spot visits to employer's premises is the financial control of undeclared work unit (*Finanzkontrolle Schwarzarbeit* FKS) of the Federal Customs Administration. Since January 1, 2016 the FKS is organisationally dependent on the Directorate VII –financial control of undeclared work– of the Central Customs Authority (Generalzolldirektion, Direktion VII, Finanzkontrolle Schwarzarbeit) which superseded the former Federal Finance Administration West (Bundesfinanzdirektion West). In October 2015, there were 6,113 workplaces in the operating part of FKS.<sup>121</sup>

### 2.2.3 Cooperation and collaboration between authorities and cross-border authorities

*Between authorities in Germany:* The FKS makes on-the-spot inspections or on the request of other institutions affected by the consequences of undeclared work. The FKS notifies cases of undeclared work to the institutions that might claim for contributions

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<sup>120</sup> Kirchner et al. (2015), Measuring and Explaining Undeclared Work in Germany – An Empirical Survey with a Special Focus on Social Desirability Bias, *Zeitschrift für Soziologie*, Jg. 42, Heft 4, August 2013, p. 291–314.

<sup>121</sup> Internet: <http://dip21.bundestag.de/dip21/btd/18/064/1806466.pdf>

and taxes (e.g. tax office, social security institutions). Large-scale controls have been organised by the FKS within Germany. These are done within specific sectors (see above). Moreover, the FKS keeps a central database from which customs, tax offices of the *Länder*, the prosecution and police authorities are allowed to receive information on request. Beyond information and file sharing, interpersonal cooperation is fostered between the relevant institutions.

Tackling undeclared work has seen wide cooperation between various agencies and institutions: the Federal Customs Administration and pensions and accident insurances, social assistance and collecting agencies for social security contributions, labour offices, tax offices, *Länder* offices for workplace safety, the police of the *Länder*, the relevant institutions in charge of foreigners and asylum seekers, the Federal agency for electricity, gas and telecommunication, the Federal Office for freight transport, the *Länder* offices in charge of tracking undeclared work as a violation of the trades and crafts laws and other institutions, e.g. the welfare fund (*Sozialkasse*) of the construction industry, the residence registration offices and the business and trade registration offices. Common guidelines and principles are elaborated in collaboration with these institutions. Whenever one of the institutions uncovers instances of undeclared work, all other institutions are informed and thus able to recover contributions and taxes that were withheld through the activity. At the regional and local level personal contacts between staff of the different institutions is an important success factor. Cooperation is fostered by sharing information, common further training, mutual learning, mutual visits, drawing common principles, regular experience-exchange at all levels. At *Länder* and regional levels a multitude of coordination groups between the different institutions have been formed (Federal Ministry of Finance 2013).

The specific issue of illegal migration and the related issues of illegal employment of foreigners have been addressed by cooperation between the Federal Police, the Federal Customs Administration, the Federal Office for Migration and Refugees, the General Intelligence Office, the Domestic Intelligence Service, and the Federal Foreign Office. This cooperation has led to a joint centre, called GASIM ("*Gemeinsames Analyse- und Strategiezentrum illegale Migration*") which was founded in 2006.

A public initiative against undeclared work was started which led to alliances against undeclared work in several sectors (starting in the construction and transport sectors). The memoranda of understanding were signed by the social partners and the Federal Ministry of Finance. They include a general declaration against undeclared work and specific measures to be undertaken by the partners. Alliances are maintained in the construction industry, cleaning trade, transportation and logistics sector, textile cleaning services, electronic crafts, painting, varnishing and decorating crafts, the meat industry, the hairdressers and the scaffold builder craft. 13 regional alliances followed the activities at the federal level.

*With other member states:* Pursuant to Article 4 of the Posted Workers Directive, the Member States designate liaison offices or competent national bodies. The German national liaison office is the Directorate VII –financial control of undeclared work– of the Central Customs Authority (Generalzolldirektion, Direktion VII, Finanzkontrolle Schwarzarbeit).<sup>122</sup>

The Directorate VII –financial control of undeclared work– of the Central Customs Authority (Generalzolldirektion, Direktion VII, Finanzkontrolle Schwarzarbeit) is also the competent authority for operating inbound and outbound requests for legal and administrative assistance based on the regulation (EC) 883/04 and (EC) 987/09.

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<sup>122</sup> Internet: [http://www.zoll.de/EN/Service\\_II/International-cooperation/international-cooperation\\_node.html](http://www.zoll.de/EN/Service_II/International-cooperation/international-cooperation_node.html)). The German Health Insurance liaison office - international service - [Deutsche Verbindungsstelle Krankenversicherung - Ausland (DVKA)] can provide the relevant information for postings from Germany to other Member States

Bilateral cooperation agreements have been concluded so far with France, Bulgaria, the Czech Republic, Austria and the Netherlands. The purpose of these agreements is to intensify cooperation in combating social security contribution and benefit fraud in employment and in unregistered employment, and the illegal transnational supply of workers.

Since 2011, the former Federal Finance Directorate West, now the Directorate VII – financial control of undeclared work– of the Central Customs Authority, as German national liaison office is participating in the European “Internal market Information system” (IMI) in the context of the Posted Workers Directive. The cooperation in IMI with the liaison offices of other Member States is effective.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The main policy approach rests on controlling companies and workers and on setting disincentives through fines, penalties and imprisonment. The severity of the consequences depends on whether there is an administrative offence or a criminal offence, e.g. to withhold the contributions to be paid by the employer for social insurance will be pursued as a criminal offence, while other offences are treated as administrative offences. Administrative fines for offences related to undeclared work can raise up to EUR 500,000 e.g. for illegal employment of foreigners or remuneration below the minimum wage. Other fines are lower e.g. for violation of registration of business, trades and craft rules while performing services or work on a large scale.

The conditions for temporary agency work became stricter in 2011. A wage floor and the right of the FKS to control for it and to issue fines have been taken up in the Act on the Provision of Temporary Workers.

Before the introduction of the national minimum wage, branch minimum wages needed to be fixed in branches particularly affected by posted workers practice, in order to avoid wage dumping and misuse of labour migration. The number of industries for which a minimum wage was requested increased over time. In 2015 a nation-wide minimum wage of EUR 8.50 was introduced. Since January 1, 2017 the federal minimum wage rests at EUR 8.84 per hour.

Preventive measures include easing the access of asylum seekers and refugees to the labour market by shortening considerably the waiting period during which they are not allowed to work. Another preventive measure was to increase the incentive to declare work. This was one of the aims of extending the so-called mini-jobs possibilities in the context of the so-called Hartz reforms. Mini-jobs are employment contracts with an upper wage ceiling of EUR 450 and a lump sum payment by employers of taxes and social security contributions (with an opt-out rule). To promote registered mini-jobs and prevent illegal employment, the household cheque procedure (*Haushaltscheckverfahren*) was established.<sup>123</sup> This procedure is a simplification of registration and social security contributions.<sup>124</sup> Private households pay less social insurance contributions for these “minor employed” persons than commercial employers since April 2003. In addition, the introduction of a tax bonus for crafts services (e.g. repair) in private households according to § 35a (3) of the Income Tax Act is perceived by the crafts association as a successful instrument, as demand for these services increased. Nevertheless, it is estimated that undeclared work in private households is still very high.

### **2.3.2 Main measures to combat undeclared work**

The main measures are the controls and audits carried out by the FKS and other relevant institutions. In 2016, 40,374 companies were controlled by FKS, 107,080 criminal investigation procedures completed, and 45,783 investigations for administrative

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<sup>123</sup> Internet: <http://dip21.bundestag.de/dip21/btd/15/000/1500026.pdf>

<sup>124</sup> Internet: <http://www.minijob-zentrale.de/DE/haushaltscheck/Node.html>;

offences completed. The sum of imposed fines and penalties amounted to EUR 48.7 million administrative fines plus EUR 34.1 million monetary penalties and 1,731 years of imprisonment. According to the *Länder* tax authorities, as a result of the FKS control and audit activities the amount of taxes lost due to undeclared work activities amounted to EUR 62.9 million. The sum of discovered damages amounted to EUR 813 million <sup>125</sup>.

In 2012, common principles were agreed about the common data services at the public pension institution in which data of foreign social security institutions are registered in the context of posting workers. The Federal Ministry of Labour in accordance with the Federal Ministry of Finance is now issuing the necessary permits. Further cooperation agreements and electronic data exchange between the Federal Customs Administration and the public pension institutions were agreed.

Concerning the success of the measures undeclared work has diminished after its peak of estimated 17.2% in 2003. Estimates made by Lars Feld (2012) indicate that the average weekly hours worked in undeclared work decreased from 8 to 5 hours between 2001 and 2008 (corresponding to a decrease of 1.6 million full time jobs) (Federal Ministry of Finance 2013). This can be partly attributed to the favourable economic situation but also to the changes in tackling undeclared work.

There are diverging views and assessments concerning the effectiveness of mini jobs to prevent undeclared work. Based on a study carried out by the IAB, trade unions argue that more undeclared work is induced by the mini jobs, with workers eventually working more hours than agreed in the mini job contracts, as compared to avoided undeclared work (Federal Ministry of Finance 2013). Eichhorst et al. (2012) show that mini jobs have replaced some regular jobs subject to social security contribution.

### **2.3.3 Good practice**

Among good practices the inter-institutional cooperation, the broad consensus among social partners as well as the sectoral and regional alliances to combat undeclared work can be named (see for details above).

According to the Federal Customs Administration the obligation for workers to carry identity cards and for employers to immediately declare the employment of workers with the social security institutions has had positive effects (Federal Ministry of Finance 2013).

### **2.3.4 Challenges and barriers**

While some successes have been logged since the new act in 2004, a challenge remains to successfully charge all damages to those organisations and individuals that have taken part in undeclared work.

Public acceptance of tackling undeclared work seems also imperative both from the perspective of the inspectors and the institutions that are actually controlling workers, but also in order to convince the general public not to pursue or make use of undeclared work.

Furthermore, human resources for implementing the controls could become an issue, especially if the competencies of the Federal Customs Administration were further enlarged.<sup>126</sup> . In 2015 the parliament granted a significant increase of staff for the Federal Customs Administration to intensify the checks on minimum wages (BT-Drs. 18/7525). Trade unions are also in favour of extending the competencies of FKS to control working conditions. The crafts associations propose better control of undeclared economic activities (Federal Ministry of Finance 2013).

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<sup>125</sup> Central Customs Authority - The Federal Customs Administration. Yearly statistics 2016 (Der Zoll. Jahresstatistik 2016), January 2017

<sup>126</sup> Internet: <http://www.bundestag.de/presse/hib/2015-11/-/395434> and <http://dip21.bundestag.de/dip21/btd/18/066/1806644.pdf>

## **Factsheet on Undeclared Work – GREECE (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

The term most widely used in Greece in order to describe unobserved (shadow) economic and employment activities is underground economy (παράοικονομία). The underground economy, as used in political and academic discussions in Greece, comprises both predominately legal and criminal activities exhibiting a common feature: they are not declared to the authorities either because they are illegal per se, or in order to avoid paying taxes and social security contributions. With respect to different organisations adopting different UDW definitions, as of 2014, the two main agencies involved in combating UDW in Greece (the Hellenic Labour Inspectorate, SEPE, and the United Body of Social Insurance, EFKA) are conducting inspections using the same definitions and the same operational methods.

#### **2.1.2 Characteristics of undeclared work**

UDW is thought to be very much concentrated in a limited number of sectors and occupations, notably in agriculture, construction, distributive trades, hotels and restaurants and among domestic workers. Agriculture has always been associated with informal activities and informal work is not the same as UDW according to the definitions. Yet it is common knowledge that the agricultural sector employs thousands of seasonal workers, mostly from the ranks of economic immigrants and the Roma. These people work, according to the press, without formal contracts and of course, without social security rights and obligations. UDW is most widespread in construction sector. Clandestine workers typically comprise of students, registered unemployed, multiple job holders and especially foreigners (both legal and illegal). There is also wide tolerance of UDW in construction by Greek society, as most household renovations and maintenance jobs are carried out by unregistered contractors. In the retail trade, there are unofficial reports by the press according to which the share of underground trade may be as high as 20% of the total (in terms of turnover), reaching as much as 40% in certain items, notably clothing. Finally, with regard to hotels and restaurants, estimating UDW is hindered by the existence of a huge number of tiny enterprises, some of which are seasonal in character. Clandestine workers here comprise all categories known to participate in UDW, namely multiple job holders, inactive (students, housewives and pensioners), unemployed people and immigrants.

With respect to the distribution of UDW by employer size, in 2014 there were almost 700,000 enterprises, the vast majority of which were micro enterprises. Micro enterprises comprised 97% of the total, employing less than 60% of the total number of persons employed and generating just over 37% of the total Gross Value Added (GVA)<sup>127</sup>. Micro and small enterprises often resort to UDW in order to cut down costs, remain competitive and survive the crisis.

Regarding motivations, since the start of the crisis Employment Protection Legislation (EPL) has been made less strict and firing costs have been adjusted to lower levels. In addition, wage flexibility has increased thus reducing incentives for employers to resort to this type of work. The tax system however, may be one of the main reasons for the continuing prevalence of UDW. The tax burden has increased substantially during the last few years, thus increasing incentives to conceal incomes.

Lastly, with respect to unemployment benefits, provision is currently confined to a minority of the unemployed, while ordinary benefits expire after 12 months (at a time when the majority of the unemployed are long-term unemployed). In general,

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<sup>127</sup> European Commission (2105), *SBA Factsheet: Greece*, Brussels.

unemployment benefits do not discourage job search in Greece and can hardly be blamed for the existence of undeclared work. It is possible though that by being grossly inadequate, benefits indirectly subsidise the propensity of seeking undeclared employment and the same holds for the extraordinary benefits for seasonal workers.

The situation as far as UDW is concerned, is likely to have been aggravated by the economic crisis. The crisis may have given birth to new forms of UDW, such as declaring to the authorities lower than actual earnings and/or hours of work and 'fake' dismissals (so as to receive unemployment benefits). Multiple job holding (moonlighting) is also believed to have increased, with persons holding a formal job in the morning and an informal one in the afternoon.

### **2.1.3 Estimated scale of undeclared work**

The size of the undeclared economy is commonly estimated to be equivalent to some 25% of GDP in Greece. A catalyst for its prevalence is the relatively high level of self-employment and large share of micro- and small enterprises. Micro enterprises with 1-9 employees represent 96% of all enterprises in Greece, employing 55% of the labour force (compared with less than 30% in the EU-28). Greece also has the highest percentage of self-employed people in the EU28 at a rate of more than 32% (14% in the EU-28) According to the 2013 Eurobarometer survey, of all undeclared work in Greece, 67.3% was waged employment (with 13.3% wholly undeclared waged employment and 54% under-declared employment), 10.2% was undeclared self-employment and 22.5% was paid favours for close social relations. Undeclared work is undertaken by all social groups. However, there appears to exist a necessity driven 'lower tier' populated by younger people and those with financial difficulties, and a more voluntary-oriented 'upper tier' occupied by professional groups such as lawyers, doctors and accountants, who not only appear to gain greater rewards from their undeclared work but also from using undeclared labour such as for domestic cleaning and home maintenance (just 24% of unemployed people but 40% of self-employed and 34% of employed people purchase undeclared goods and services). It would thus be a mistake to adopt a laissez-faire approach towards the undeclared economy based on the belief that it is a survival strategy for populations excluded from the declared economy. What interventions are required, therefore, to tackle the undeclared economy.

Regarding recent trends, there are some indications according to which UDW may be falling. According to Schneider & Williams (2013), the size of the shadow economy (expressed as % of the GDP) declined monotonically from 28.2% in 2001 to 24% in 2012. To the extent that this trend is accurate, it can partly be attributed to increased efforts by the authorities to tackle tax evasion by improving the tax audit function, by introducing electronic cross-checking of the tax data and by organising public campaigns to discredit tax evaders. In this frame, it should be also noted that the fines imposed on employers for employing undeclared personnel have been made stricter since 2013. Falling trends may also reflect the recorded decline in the number of immigrants.

According to the results of joint inspections carried out by the Labour Inspectorate (SEPE) and the United Body of Social Insurance (EFKA, Greece's main social security institution) for 2016, undeclared workers were employed in 16.3% of companies inspected (5,577 out of 34,241). Of the 130,608 employees, 7.1% (9,270) were identified as undeclared workers, with fines imposed amounting to over EUR 97 million.

Inspections for 2016 revealed that businesses with undeclared workers accounted for 27.6% during the targeted inspections in textile production, 19.4% in the garment industry, 18.2% in activities providing personal services and 10.9% in sports and leisure/entertainment, and 10.0% in catering services.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

In Greece the main authorities for addressing undeclared work are namely:

- the Ministry of Labour, Social Security and Social Solidarity and Hellenic Labour Inspectorate (SEPE) for labour law violations;
- the Ministry of Finance for tax non-compliance, and
- the United Body of Social Insurance (EFKA) for social security fraud.

### **2.2.2 Characteristics of the responsible organisations**

#### ***Ministry of Labour, Social Security and Solidarity***

The Ministry of Labour, Social Security and Solidarity takes overarching responsibility for labour law violations, and as tackling undeclared work in Greece is primarily perceived as concerning the social protection of workers, this Ministry is viewed as the lead Ministry in tackling undeclared work, taking responsibility for the definition and implementation of policies on employment, working conditions and social security, coordinating the system of labour administration, including the Labour Inspectorate (SEPE) and the Labour Force Employment Organization (OAED).

#### ***Hellenic Labour Inspectorate (SEPE)***

This was established in 1955 and restructured to its present form in 1999. In accordance with Article 2 of Act 3996/2011: the "project of the Labour Inspection Corps is the supervision and control of the implementation of the provisions of labour legislation, the investigation of the insurance cover and illegal employment of workers, reconciliation and settlement of labour disputes, and the provision of information to workers and employers concerning the most effective means of complying with the current provisions". It reports to the Ministry of Labour, Social Security and Solidarity, so as to ensure a unified policy for monitoring the implementation of labour legislation. In accordance with Law 2639/1998 (FEK A' 205) on 'regulation of labour relations, establishment of a Labour Inspectorate and other provisions'. SEPE is responsible for:

- a) monitoring the implementation of labour legislation (labour accidents, health and safety etc);
- b) the investigation of incidents of illegal labour and uninsured labour; and
- c) the provision of information and proposals regarding the effective application of labour legislation.

SEPE has the authority to freely enter all workplaces in the private and public sector, at any time of the day or night, and without prior notification. It carries out necessary examinations, monitoring or investigations of all types, with a view to determining whether the provisions of labour legislation are being observed. It can temporarily suspend operation of the whole or part of an enterprise, if the labour inspectors deem that workers' safety and health are directly at risk.

The total staff of SEPE at the end of 2016 was 736 employees, of whom 335 were labour relations inspectors, 249 health and safety inspectors and 44 inspectors under training. The labour inspectors are civil servants selected by a state personnel selection commission. Candidates for labour inspection posts must have a university degree in economics, public administration, social studies, or law and very good knowledge in at least one European language. Informatics ability is also a prerequisite. Candidates for the technical and medical posts are required to have a degree in engineering or medical studies respectively. A training period of three weeks takes place after the nomination as labour or technical and medical labour inspector. SEPE responds to grievances, or targets certain sectors or enterprises for inspections. SEPE sets annual plans and publishes annual reports, posted on the site of the Ministry of Labour, Social Insurance and Social Solidarity.

### ***Manpower Employment Organization (OAED).***

This is the public body responsible for the implementation of employment policy and services. In particular, OAED is responsible for information on the labour force and the unemployed, for the professional orientation of the labour force, the delivery of technical education and training, facilitating the link between labour demand and supply, and the payment of benefits such as unemployment benefits, maternity benefits etc. OAED is responsible for maintaining the registry of unemployed in Greece, which, according to the Governor of OAED (interview 26 April 2016) is interoperational with SEPE and IKA. OAED is co-owner of ERGANI and data is cross-checked.

They are also connected with the revenue administration, from which they draw data on taxpayers. OAED draws hiring announcements from ERGANI, gets the AFM (taxation number), cross-checks this, and seizes unemployment benefits if the person is employed.

Furthermore, the unemployed are obliged to appear physically once every three months to sign that they are unemployed. In cases of employment, the unemployment benefits are suspended. According to the same source, the problem with undeclared work is that they work without appearing in any data sets.

### ***United Body of Social Insurance (EFKA)***

The Law 4387/201613 created a new legal organ of public law, namely EFKA (Uniform Social Insurance Fund), which will subsume the existing social insurance funds for principal insurance, i.e. IKA (employees), ETAA (engineers, doctors, lawyers), OAEE (self-employed), OGA (agricultural workers), NAT (seafarers), TAYTEKW (public welfare organizations employees), and ETAT (bank employees). EFKA is a legal entity supervised by the Ministry of Labour, Social Security and Social Solidarity.

EFKA carries out inspections in much the same way as SEPE, albeit with a different focus. Inspections by IKA seek to check whether social insurance legislation is being complied with. EFKA's inspections are carried out by local branches as well as by the Special Insurance Control Services (EYPEA). The latter are administrative units specifically set up for fighting social security contribution evasion. Since 2014, a large amount of inspections at enterprises and work sites are carried out by mixed units consisting both of EYPEA (Special Insurance Control Service) and SEPE (Labour Inspectorate) employees.

### ***Ministry of Finance***

The Ministry of Finance, meanwhile, takes responsibility for that aspect of the undeclared economy related to tax non-compliance. This Ministry is responsible for tax revenue and more particularly in relation to the undeclared economy, tax non-compliance, and includes the Financial and Economic Crime Unit (SDOE) which is the tax inspectorate and takes responsibility for investigating tax non-compliance, the Public Revenue Service and the General Secretariat of Information Systems (GSIS).

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

During the last few years, a number of measures were taken in order to improve the services engaged in monitoring unlawful employment (EFKA (IKA), SEPE, SDOE) and increase collaboration between them. In this respect, a Ministerial Decision (M.D. No. 11321/11115/802/2.6.2014 (ΦΕΚ 1851/ Β' 12.6.2014) has envisaged the coordination of inspections through the cooperation of IKA and SEPE. The inspections at enterprises and work sites are now being carried out by mixed units consisting both of EYPEA (Special Insurance Control Service) and SEPE (Hellenic Labour Inspectorate) employees, working on the basis of a common UDW definition and imposing the same fines. The fines imposed by SEPE are communicated to the tax authorities, whereas the fines imposed by EFKA (IKA) are communicated to the social security organisations.



The checks conducted by SEPE involve a sample of companies from all sectors of economic activity, whereas the checks conducted by EFKA (IKA) focus on sectors which are known to exhibit high incidences of UDW, namely hospitality services, personal services, retail trade, transport services, manufacturing activities, construction, car repair companies, cleaning services and security services.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The intention to combat undeclared work has always been a core policy objective in Greece, emphasised on various occasions. The need to limit its extent, for example, has figured prominently in the various National Reform Plans and other official documents. Recently taken measures include the introduction of an operational plan to combat UDW (ARTEMIS), stricter fines, simplifications reducing the administrative burden for companies, mandatory reporting of hiring and dismissals through ERGANI, and reductions in non-wage costs. Earlier taken measures include a special voucher used as a compensation for those professions where undeclared work is extensive, mainly domestic workers (Law 3996/2011) and attempts to modernise the policy on immigration.

In 2016 the ILO, the Greek Government and the social partners, as part of a project funded by the European Commission on "Supporting the transition from informal to formal economy and addressing undeclared work in Greece", has produced a report on the Diagnosis of Undeclared Work in Greece. The Diagnostic Report was endorsed by the Greek Government and the social partners in a high level tripartite validation meeting on 6 July 2016. The validated report provides a set of policy recommendations that reflect the ILO's vision of a balanced approach combining incentives with compliance measures, as enshrined in the ILO Recommendation n.204 on the transition from the informal to the formal economy, adopted at the International Labour Conference in June 2015. In addition, on 19 July 2016, the national social partners (GSEE, SEV, GSEVEE, ESEE, SETE) signed a Joint statement - declaration, which refers to labour market issues, including the extension of the collective labour agreements. After reaching a tripartite agreement on the main characteristics and drivers of informality, the next step was to design, through tripartite dialogue, a road map for addressing undeclared work in Greece. This road map aims to contain a balanced regulatory and policy framework for preventive and appropriate corrective measures that will facilitate the transition to the formal economy and tackle undeclared work. It was validated in October 2016 with an implementation period of 36 months, starting on January 2017.

### **2.3.2 Measures to tackle UDW**

According to Law 4144/2013, aimed at combating illegal employment, the Hellenic Labour Inspectorate will remain the body responsible for the enforcement of labour law. However, the new Law (4144/2013) provides that the Financial Police is equally competent to control undeclared employment of workers. The new law also attempts to fight undeclared employment of workers who illegally receive unemployment benefits. In addition to other penalties provided by law, the new law introduced a special fine of EUR 3 000 for each worker who is employed while receiving unemployment benefits. If the worker who is receiving unemployment benefits was fired and consequently rehired by the same employer, the fine amounts to EUR 5,000 per employee.

Another law adopted recently (Law 4225/2014), aimed at improving the situation with regard to the prevention of undeclared and uninsured employment. It provides: a) a significant increase in fines in case of work declared only to the Ministry of Labour but not to the competent social security organization, b) the responsibility of social security authorities to check within 30 days whether the stated social security contributions were in fact paid by the companies, and c) the immediate registration of any change in employees' work hours through "ERGANI" Information System (Article 55 of Law 4310/2014). In the previous scheme, changes in the work hours required the company

to submit the revised work schedules to the Labour Inspectorate within 48 hours of the introduced changes. Thus, some employers could change the work schedules at will and declare the modification only if an inspection was carried out. Pursuant to the new provision, any change in employees' work hours should be registered with the Labour Inspectorate no later than the same day of the modification and in any case, before employees' new shift by submitting to the "ERGANI" Information System the appropriate electronic form, which includes modified work schedules.

The fines imposed in cases of UDW were also increased substantially, as of 15 September 2013. According to the relevant Ministerial Decision, the fine for each undeclared employee is now EUR 10,550, about 18 times the minimum wage. The intention behind this Ministerial Decision was to make uninsured and undeclared work unprofitable for employers. Further the fines are imposed immediately and on the spot by inspectors, with assistance from the Ministry's information systems and network. Soon after the issuance of the new Ministerial Decision, many employers opted for the 'legitimization' of undeclared workers among their personnel, in order to avoid paying the fines, resulting in a substantial increase in new hiring.

It is also worth noting that the level of social security contributions has been reduced by approximately 5pps since 2012. A more employment-friendly tax system may prove beneficial not only for the level of employment but also for the levels of UDW.

Mention should also be made of an IT system, ERGANI, which has been established through a Ministerial Decision (5072/6/25.2.2013 (ΦΕΚ 449/Β'/25.2.2013), with the aim to record (in real time) all employment flows in the private sector of the economy. Starting from early 2013, all employers are obliged to report electronically recruitments, voluntary departures and dismissals, as well as data on overtime, part-time and job rotation, firm-level agreements and annual leave. The results from the electronic registration of all enterprises and employees are regularly published in the frame of a dedicated action plan to combat UDW, ARTEMIS, enabling the detailed stocktaking of the entire dependent employment in Greece. Published information contains the sectoral and geographical distribution of enterprises, the classification of enterprises by size, the breakdown of employees by age, working time, salary, etc. It is evident that apart from monitoring of the trends in the wage market, ERGANI contributes to a reduction of the administrative burden for enterprises and enables the implementation of targeted and efficient controls in the field of combating UDW.

In addition, during the last decade or so, Greece has taken steps to modernise its migration policy. Policy reforms in this field included three regularisation exercises (amnesty), simplification of the permit procedures, and eased residence permit renewal procedures. Although the number of immigrants still residing illegally in Greece is thought to be substantial, it is thought that in the absence of these measures it is likely that the situation with respect to UDW would have been worse.

Lastly, the three year roadmap for fighting undeclared work (from January 2017 until December 2019) was ratified and provides a set of 25 policy recommendations to implement a holistic integrated strategic approach to tackle undeclared work in Greece.

Out of these 25 recommendations, we highlight:

- Establishment of a national body for the implementation of the roadmap and the national strategy to combat undeclared work as subgroup of the Supreme Work Council (SWC/ASE).
- Action Plan against Bogus Self-Employment.
- Strengthening the exchange of data and establishing common rules for risk analysis between different competent authorities.
- Ratification of the International Convention no129.
- Increasing responsibility in public works. Framework for public works will hold the contractor responsible for violation of labour laws by the subcontractors
- Obligation of electronic payments.

- Pilot program of targeted audits with the collaboration of SEPE, PECA, ADRC and Financial Police in the Region of Attica in the period May - September.
- Changing the institutional framework for imposing fines on undeclared work.
- Combating new forms of work-related delinquency.
- Establishment of electronic overtime register.
- Establishment of a personnel table for major technical projects.
- Upgrading Geographical Competence & Institutional Support of Labour Inspectorate Body.
- Legislative framework for operation of Information Centres.

The organisational structure of SEPE includes the creation of four new regional divisions and a new Directorate in the Aegean area to effectively tackle the violation of labour law in the tourism sector. Also, for the overall upgrading of the SEPE's service delivery, the Support Directorate has been re-established by creating departments for legal support and information management systems.

In the framework of its overall activity, SEPE puts special emphasis on conducting targeted country wide campaigns in specific sectors, in order to tackle the shift of violation of labour law from fully undeclared to partially undeclared work, while making full use the Integrated Information System of SEPE.

### **2.3.3 Good practice**

The recording of all employment flows on a database (ERGANI) appears to be a good policy example (please see above).

### **2.3.4 Challenges and barriers**

According to all existing evidence, undeclared work (UDW) is quite pronounced in Greece, and the task of reducing its size constitutes a major challenge for the authorities. In spite of the efforts to combat UDW, it is commonly acknowledged that successive governments and past measures have failed to tackle the phenomenon and that UDW, with all its consequences, continues to thrive. UDW should be treated not only as a purely economic but also as a social phenomenon. People often view undeclared employment as something legitimate, and this might perhaps explain why previous policy efforts (comprising of altering administrative procedures and making fines more severe), have partly failed. What is needed is a well-organised, multi-dimensional plan, comprising actions in a number of policy fields (including awareness campaigns), and zeal to overcome all obstacles (regulatory, administrative, technical).

## Factsheet on Undeclared Work – HUNGARY (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

The Hungarian government's employment strategy for 2014-2020<sup>128</sup>, refers to undeclared work as employment that is not reported to the national authorities. It also mentions envelope wages as a common form of the grey economy.

The Department of Labour Inspections (Employment) focuses on the enforcement of obligations concerning labour contract, such as reporting the beginning and end of the employment relationship or observing working time rules. Therefore the Department does not include envelope wages in their definition of undeclared work (as the employment relationship is duly reported to the authorities). By contrast, the Tax Authority is concerned with all forms of tax fraud, thus covering envelope wages as well.<sup>129</sup>

#### 2.1.2 Characteristics of undeclared work

There are three main types of undeclared work in Hungary: employees who are not fully declared to the authorities by their employers, self-employed individuals who fail to declare some or all of their income, and bogus employment.

Within both of the two basic types we can distinguish between fully (black) and partly (grey) unreported employment. Data is limited on the issue but one source suggests that at most 15% of the employees receive higher wages than their declared salary<sup>130</sup>, while the share of undeclared employment is estimated around 17%. According to other estimates, 0.6-0.7% of GDP goes unreported due to grey employment<sup>131</sup>. Please note: this data does not necessarily reflect the views of the Hungarian government.

Socially embedded undeclared work or illegal immigrant work does not seem to be significant. According to the yearly report of the Department of Labour Inspections (Employment) of the Ministry for National Economy (DLIE) undeclared work of third country workers is below 2% of the all reported undeclared work cases in 2015 in Hungary.<sup>132</sup>

According to Elek-Köllő (2015), between 2001 and 2006 agriculture, transportation, construction and personal services exhibited higher probabilities of undeclared work (8-16 pp, 14-25 pp and 3 pp higher than industry respectively).<sup>133</sup> Elek et al. (2012)<sup>134</sup> find that the proportion of employees paid envelope wages was higher than average in construction, trade and catering (around 12%, 10% and 9%, respectively).

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<sup>128</sup> Proposal for the Hungarian Government's Employment Strategy for 2014-2020. Internet: [http://2010-2014.kormany.hu/download/8/4c/01000/Fogl\\_Strat\\_14-20.pdf](http://2010-2014.kormany.hu/download/8/4c/01000/Fogl_Strat_14-20.pdf)

<sup>129</sup> Cf the relevant section of the law on taxation (2003. évi XCII. törvény az adózás rendjéről, 86. § (1) "Az adóhatóság az adóbevétel megrövidítésének, a költségvetési támogatás, adó-visszaigénylés jogosulatlan igénybevételének megakadályozása érdekében rendszeresen ellenőrzi az adózókat és az adózásban részt vevő más személyeket. Az ellenőrzés célja az adótörvényekben és más jogszabályokban előírt kötelezettségek teljesítésének vagy megsértésének megállapítása.")

<sup>130</sup> Benedek et al (2012), p. 174.

<sup>131</sup> Ibid, p. 177.

<sup>132</sup> Annual Report on Labour Inspections, 2015. Department of Labour Inspections (Employment), Ministry for National Economy. Internet: [http://www.ommf.gov.hu/letoltes.php?d\\_id=6675](http://www.ommf.gov.hu/letoltes.php?d_id=6675)

<sup>133</sup> Elek, P., Köllő, J.: Undeclared employment in permanent jobs – estimates from matched administrative and survey data. 2015. Paper presented at the Annual Conference of Hungarian Economics Association.

<sup>134</sup> Péter Elek, János Köllő, Balázs Reizer, Péter A. Szabó: Detecting Wage Under-Reporting Using a Double-Hurdle Model. *Research in Labor Economics*, Volume 34, 2012, pp.135 - 166.

According to the 2016 Report of the DLIE<sup>135</sup>, which reviews the outcome of inspections carried out annually, among the cases where undeclared work was detected 69% involved undeclared employees and 12% involved the lack of an employment contract. Other causes included undeclared casual work<sup>136</sup> (14%), a full-time employee being declared as a part-time employee (2%), bogus contracts (artificial agreements, 2%), and various other reasons (1%). According to the results of the inspections carried out in 2016, 38% of the undeclared employees worked in the construction sector. 7% of undeclared workers were employed in the agricultural sector, 9% in the manufacturing industry, 11% by private security firms, 9% in retail and 12% in catering. However, these numbers are influenced by the number of inspections in the respective sectors: 20% of the inspections were carried out in the construction sector, 12% in the manufacturing industry, 12% in private security firms, 22% in retail and 16% in catering.

Undeclared work tends to vary inversely with employer size. Elek-Köllő (2015) find that unregistered employment was 15% more likely in micro firms between 2001 and 2006.<sup>137</sup> Envelope wages were also more common in micro (19%) and small firms (12%) in 2006 (Elek et. al 2012).

As also admitted by the Government Employment Strategy, the main motivation is to gain a competitive advantage by avoiding the payment of taxes and social security contributions (SSC). It must be noted that employees are not always aware of the fact that they are not registered by their employer.

### **2.1.3 Estimated scale of undeclared work**

As detailed above, the estimated size of completely unreported employment was 10-17% of total employment in the period 2001-2006.

According to one 2013 study on the black and grey economy, in 2004 more than 40% of the self-employed were not reported<sup>138</sup>, while for formal enterprises the share of undeclared work was between 10% and 17%, based on a comparison of the Labour Force Survey data and Pension Insurance records (16-17% between 2001 and 2005, Elek et al 2009)<sup>139</sup>. Most recently, Elek – Köllő (2015)<sup>140</sup> show that among employees with stable jobs (with more than one year tenure), between 2001-2006 on average 10% of employment went unreported<sup>141</sup> <sup>142</sup>. Again, please note: this data does not necessarily reflect the views of the Hungarian government.

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<sup>135</sup> Annual Report on Labour Inspections, 2016. Department of Labour Inspections (Employment), Ministry for National Economy. Internet: [http://www.ommf.gov.hu/letoltes.php?d\\_id=7190](http://www.ommf.gov.hu/letoltes.php?d_id=7190)

<sup>136</sup> Casual workers can be employed on simplified terms (called simplified employment) in some branches of the economy, such as seasonal agricultural work

<sup>137</sup> Ibid.

<sup>138</sup> Benedek, D, Elek, P and Köllő, J (2013): A Tax avoidance, tax evasion, black and grey employment. In: Fazekas, K., Benczúr, P. and Teledgy, Á. (eds.) The Hungarian Labour Market, 2013. CERS, HAS, Budapest. pp. 161-178.

<sup>139</sup> Elek, P., et al (2009): A feketefoglalkoztatás mértéke Magyarországon. (Measuring undeclared employment in Hungary [in Hungarian].) In: Semjén, A. and Tóth, I. J. (eds.), Rejtett gazdaság. Be nem jelentett foglalkoztatás és jövedelemeltitkolás – kormányzati lépések és a gazdasági szereplők válaszai KTI Könyvek 11., p. 84-102.

<sup>140</sup> <sup>140</sup> Elek, P., Köllő, J.: Undeclared employment in permanent jobs – estimates from matched administrative and survey data. 2015. Paper presented at the Annual Conference of Hungarian Economics Association.

<sup>141</sup> This paper relies on matching employment histories as reported in the Hungarian Labour Force Survey with data from the Hungarian Pension Directorate. The figure above relates to the discrepancy between the self-reported and officially recorded number of years work for a given employer.

<sup>142</sup> Similar results are obtained by survey-based using self-reported undeclared work data. For the time period of 2001-2009 Semjén et al. (2009) found that the extent of UDW is 15 %, while Czibik-Medgyesi (2007) estimated 10%. See: Czibik Ágnes–Medgyesi Márton (2007): A lakosság

Estimates of the extent of partly unreported employment (envelope wages) vary substantially. According to Semjén et al (2008)<sup>143</sup>, in a 2008 survey of 1,000 respondents aged 15-60, 15% reported to have received 'envelope wages' at least once in the preceding two years. Elek et al. (2012)<sup>144</sup> found that about 6% of all private sector employees received 'envelope wages' in 2006.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing undeclared work

There are two key bodies:

**Labour Authorities (LAs) within District Offices of County Government Offices:** Inspections of labour authorities (LAs) are focused on all the work related legal relations. The directive of the Ministry for National Economy for labour inspections in 2016 focus on prevention by informing employers of employment rules<sup>145</sup>. LAs do not examine the reporting or payment of taxes or SSC.

**National Tax and Customs Administration of Hungary (NTCA):** this is the general tax authority in Hungary that is responsible for collecting taxes and SSC and inspecting tax compliance.

### 2.2.2 Characteristics of the responsible organisations

**LAs** - The Labour Authority was restructured in 2015 (along with the PES). Before 2011 the Hungarian Labour Inspectorate (OMMF) had seven regional offices.

The Labour Authority has currently two levels: (1) the Minister for National Economy who is responsible for the professional guidance of lower levels. At the district level the role of the former territorial offices of the OMMF was gradually transferred to (2) the District Offices of the General Government Offices at the district level, and executed by their departments of 'Labour Inspection and Supervision'. The operational and professional activities of these district level departments are guided by the DLIE.<sup>146</sup>

The remits and powers of LAs are set out by the Act LXXV of 1996 on Labour Inspection. LAs are responsible for checking compliance with the statutory requirements at any enterprise in Hungary regardless of nationality and can take measures against employers in cases of breach of law. In particular, LAs inspect the registration of employment, the mandatory substantial elements of the employment contract, working and resting time, the payment of wages, observing minimum wage regulations, special employment conditions, posting and assignment of workers and temporary agency work, and the employment of third-country nationals in Hungary.<sup>147</sup> During their inspections LAs target

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nyugdíjjal kapcsolatos megtakarítási tudatossága és hajlandósága. Egy lakossági kérdőíves felvétel elemzése. MKIK GVI, Budapest.; Semjén A., Tóth, I. J., Medgyesi, M. and Czibik, Á. (2009): Adócsalás és korrupció – lakossági érintettség és elfogadottság. In: Semjén András–Tóth István János (eds.): Rejtett gazdaság. Be nem jelentett foglalkoztatás és jövedelemeltitkolás – kormányzati lépések és a gazdasági szereplők válasza. KTI Könyvek, 11.

<sup>143</sup> Semjén, A, Tóth, I. J, Medgyesi, M., Czibik Á. (2008): Adócsalás és korrupció: lakossági érintettség és elfogadottság. Discussion Papers MT-DP – 2008/13. Budapest: Institute of Economics, Hungarian Academy of Sciences. Internet: [http://www.econ.core.hu/file/download/mtdp/MTDP\\_0813.pdf](http://www.econ.core.hu/file/download/mtdp/MTDP_0813.pdf)

<sup>144</sup> Péter Elek, János Köllő, Balázs Reizer, Péter A. Szabó: Detecting Wage Under-Reporting Using a Double-Hurdle Model. *Research in Labor Economics*, Volume 34, 2012, pp.135 - 166.

<sup>145</sup> LXXV of 1996 Act on Labour Inspection and Announcement of the State Secretary for the Labour Market on guidelines on labour inspections in 2016.

<sup>146</sup> Government Decree No. 320/2014. (XII. 13.)

<sup>147</sup> Internet: [http://www.ommf.gov.hu/?akt\\_menu=547&set\\_lang=123](http://www.ommf.gov.hu/?akt_menu=547&set_lang=123)

sectors in which infringements are frequently detected and which were not under inspection in the previous year.<sup>148</sup>

**NTCA** - The tax authority has three organisational levels. At the local level there are the 22 offices of NTCA; the second level is the central office of NTCA; while on the top is the Minister of National Economy. The central office of NTCA guides its county offices in all issues, while the Minister is responsible for the supervision of the whole NTCA and acts as the appellate authority.<sup>149</sup>

NTCA must conduct inspection in the following cases: voluntary liquidation is ordered at a company; at the call of the Court of Audit; at the instruction of the Minister of National Economy; and in cases of the decision of the city council at local authorities. In each year NTCA inspects 10 % of the newly established firms based on its risk analysis system. Otherwise, the priorities are set by the president of NTCA.<sup>150</sup> According to the announcement of the head of NTCA in 2015, NTCA especially targeted to detect unregistered employees by inspecting companies that reported large revenues and few employees. In addition it targets companies using manpower leasing and services to households (private doctors, vets, hairdresser, electricians, plumbers, etc.) and sectors with a low share of material costs (insurance agents, real estate agents, designers, etc.).

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

**LAs** - According to Section 8 of the Act LXXV of 1996 on Labour Inspection, during their proceedings LAs cooperate with other authorities. In this cooperation LAs provide information ex officio to the public employment service (PES) about the infringements of the employment rules on a monthly basis. To meet this requirement LAs maintain an electronic database and record of the personal data of affected employees.

For inspections in other fields LAs maintain a database of employers against whom legally binding decisions have stated infringement.<sup>151</sup>

**NTCA** - Based on the Annual Report of NTCA cooperation is mainly between tax and custom authorities.<sup>152</sup> There is no available information on cooperation regarding employment contracts.

In terms of data exchange and cooperation between national authorities other Member States, activities are as follows:

**LAs** - According to the Act LXXV of 1996 on Labour Inspection DLIE cooperates with all the employment related authorities of the EU. In this cooperation DLIE provides all the information about the findings of its inspection activity and the related legislation.<sup>153</sup>

**NTCA** - The collaboration between NTCA and other Member States (MSs) is described in the Directive 2011/16/EU which aims to facilitate the information exchange and inspections by MSs.<sup>154</sup> In 2014 NTCA exchanged information in 18 000 cases of which 90 % were between MSs. NTCA cooperates most frequently with Germany, Slovakia, Czech Republic and Romania. There is no data on employment related cooperation at NTCA.<sup>155</sup>

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<sup>148</sup> Act LXXV of 1996 on Labour Inspection

<sup>149</sup> Act XCII of 2013 on the Rules of Taxation 10. §

<sup>150</sup> Act XCII of 2013 on the Rules of Taxation 86-89. §

<sup>151</sup> Act LXXV of 1996 on Labour Inspection

<sup>152</sup> Annual Report of National Tax and Customs Administration of Hungary, 2014.

<sup>153</sup> Act LXXV of 1996 on Labour Inspection

<sup>154</sup> Directive 2011/16/EU. Internet : <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32011L0016&from=en>

<sup>155</sup> Annual Report of NTCA (2014).

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

According to the Government's Employment Strategy for 2014-2020, Hungary needs to combine deterrence and motivation.

Motivating measures include further cuts in the Personal Income Tax, targeted reductions of SSC in the Job Protection Action Plan and targeted information campaigns in industries that are most affected by undeclared work.

Deterrence measures include more frequent controls and stricter penalties, with an emphasis on their frequency. Firms are expected to accept these changes more easily as the cost of employment has decreased in recent years.

The strategy also aims to improve compliance with health and safety regulations and to enable social dialogue by strengthening the representation of the interests of various stakeholders, including those of employees, as this could further decrease undeclared employment.

### **2.3.2 Measures to tackle UDW**

Investigations are carried out regularly by the DLIE and by the NTCA. For 2016, the following target values were set by the Minister for National Economy for LAs: at least 10 % of the inspections must be carried out in the sector of private security firms, at least 10 % in the manufacturing industry. At least in 80 % of the cases where undeclared work was detected, inspection authorities shall investigate if the employer has rectified the situation by reporting the employees affected.<sup>156</sup>

A major project, TÁMOP 2.4.8<sup>157</sup> was launched in 2012 to increase the effectiveness of labour inspections. The goals of the project include the development of the system and processes of inspections, increasing the quality, targeting and depth of inspections, and the provision of more information to employees and employers.

A new project that has been announced recently also aims to further enhance the effectiveness of labour inspections.<sup>158</sup>

### **2.3.3 Good practice**

The EU co-funded project TÁMOP 5.2.3.B established 116 JOGPONT+ (Legal point +) Mini offices in Hungarian cities throughout the country, providing employers and employees with free services and information on the legal framework of employment. By making participants of the labour market more aware of their rights and obligations, this national network of offices is expected to contribute to the decrease of undeclared work, although impact assessments are not yet available.

The database of the cases addressed in the JOGPONT+ offices provides information on the number of cases and the typical nature of issues in each specific region. Reports on these data are published at the project's website.

### **2.3.4 Challenges and barriers**

The main challenge to decreasing undeclared work in Hungary is that taxes and SSC on employment are high, especially in the case of low-skilled workers (excluding casual workers). This implies that firms that do not comply with regulations have a significant cost advantage.

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<sup>156</sup> Announcement of the State Secretary for the Labour Market on directives on labour inspections in 2016. Internet: [http://www.ommf.gov.hu/letoltes.php?d\\_id=6447](http://www.ommf.gov.hu/letoltes.php?d_id=6447)

<sup>157</sup> Internet: <http://tamop248.hu/2/>

<sup>158</sup> <https://www.palyazat.gov.hu/megjelent-a-jogszer-foglalkoztats-fejleszts-felhvs>



The government aims to tackle this by decreasing taxes on employment along with increasing the efficiency and frequency of inspections.

In the newly reorganised system, the Minister for National Economy has more direct control over the targeting of inspections. The restructuring also created new challenges, as the former OMMF had seven regional offices, but the new structure is integrated into the District Offices of the Government Offices at the district-level (one department at each county seat in the 19 counties and Budapest). Officers need to adapt to the new structure.

## Factsheet on Undeclared Work – IRELAND (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

Undeclared work (UDW) is neither defined in Irish Law nor specifically targeted and measured by the Irish administration.<sup>159</sup> The Office of the Revenue Commissioners define the 'shadow economy' as "activity in respect of which businesses (including professions) and individuals engage in inappropriate practices with the aim of not complying with their legal obligations relating to matters such as taxes & duties, PRSI, licenses and employment. Shadow economy activity includes not declaring, or under-declaring, a source of income (for example, not declaring or under-declaring 'cash jobs') so as to avoid tax and other liabilities; employers paying employees in cash under an 'off the books' arrangement so as to evade tax and PRSI liabilities; 'working and signing' - working or running a business whilst at the same time falsely claiming job-seekers benefit from the Department of Social Protection (DSP); non-operation of the VAT system; tobacco smuggling including the sale of illegal tobacco products; oil laundering including the sale of washed diesel. Most of the shadow economy activity takes place within that which is referred to as the 'cash economy' (i.e. the payment for goods and services by way of cash)."<sup>160</sup>

#### 2.1.2 Characteristics of undeclared work

The main types of UDW in Ireland, as outlined by the Office of the Revenue Commissioners Annual Report 2014, include activities such as paying employees 'off the books' and individuals doing 'nixers'<sup>161</sup> either in addition to their normal employment or while also claiming DSP payments.<sup>162</sup>

Another issue, highlighted through the Revenue Commissioners' strategy on tax evasion, was evidence of employers classifying workers as self-employed ('bogus self-employment') which increases the likelihood of undeclared work.

The main sectors in Ireland that are affected by undeclared work are those that are labour-intensive and where cost competition is strong, such as, construction, domestic services, hotel and catering, agriculture, retail and the food and drink industry (Eurofound, 2013).<sup>163</sup> According to the Revenue Commissions Annual Report 2014, their audit and assurance activity placed a particular focus on sectors of the economy that traditionally have been susceptible to shadow activity, specifically cash businesses such as the hospitality sector, including bars, nightclubs, fast-food restaurants and entertainment, and white collar such as doctors, dentists, solicitors, accountants, and engineers.<sup>164</sup>

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<sup>159</sup> Cronin, Maedhbh (2013). *The Role of the Irish National Inspection System (National Employment Rights Authority – NERA) as part of a strategic policy response to undeclared work*. Geneva: ILO. Internet:

[http://www.ilo.org/wcmsp5/groups/public/@ed\\_dialogue/@lab\\_admin/documents/genericdocument/wcms\\_224583.pdf](http://www.ilo.org/wcmsp5/groups/public/@ed_dialogue/@lab_admin/documents/genericdocument/wcms_224583.pdf)

<sup>160</sup> Internet: <http://www.revenue.ie/en/business/shadow-economy/index.html>

<sup>161</sup> According to the Revenue Commissioners "The term 'nixer' generally refers to part-time work that an individual undertakes and the income from which is not reported to relevant authorities such as the Revenue Commissioners." Internet: <http://www.revenue.ie/en/business/shadow-economy/nixers.html#section1>:

<sup>162</sup> Revenue Commissioners (2015a). *Annual Report 2014*. Revenue Commissioners: Dublin. Internet: <http://www.revenue.ie/en/about/publications/annual-reports.html>

<sup>163</sup> Internet: <https://www.eurofound.europa.eu/observatories/emcc/case-studies/tackling-undeclared-work-in-europe/labour-inspectorate-controls-ireland>

<sup>164</sup> Revenue, 2015a. Internet: <http://www.revenue.ie/en/about/publications/annual-reports/2014/downloads.html>

The presence of numerous small and medium-sized businesses in the Irish economy is quoted as a factor for undeclared work (Eurofound, 2013).<sup>165</sup> The principal reason for engaging in UDW in Ireland is in order to avoid payment of tax and/or remain below certain income thresholds in order to qualify for welfare benefits. Schneider (2011) states that the higher the tax burden, measured by personal income tax, payroll taxes, and/or indirect taxes, the larger the shadow economy.<sup>166</sup> The tax burden in Ireland has increased substantially since the beginning of the financial crises. Successive budgets have widened the tax net to include workers on relatively modest pay levels with the introduction of the Universal Social Charge (USC)<sup>167</sup> and had the effect of reducing take home pay for the majority of workers. The introduction of other taxes, such as property and water charges, have also had an impact on earnings of both employees and the self-employed.

### **2.1.3 Estimated scale of undeclared work**

The DSP, Revenue, and the National Employment Rights Authority (NERA) [now the Workplace Relations Commission (WRC)] collect data specific to their own areas of responsibility but there are no specific data relating to UDW collected at national level. Cronin (2013) estimated that UDW represents two-thirds of the shadow economy which equates to approximately 8 % of GDP (EUR 14 billion in 2013). In 2012, the Irish Construction Industry Federation (CIF) estimated the value of the shadow economy at EUR 19.97 billion and Irish Business and Employers Confederation (IBEC) estimated the value at EUR 21 billion.

According to the Multiple Indicator and Multiple Courses (MIMIC) used by Schneider, in 2011,<sup>168</sup> Ireland's shadow economy was reported at 12.7 % of GDP. So based on that report and on the 2015 GDP figure from the Central Statistics Office (CSO) of EUR 204 billion, the shadow economy could possibly have been in the region of EUR 26 billion in 2015. The World Bank's research on informal workers, including those working without contract, informal self-employment and unpaid family work found that Ireland had a high level of informal economy at 33 % of the labour force in 2011.<sup>169</sup>

Since 2003 the DSP has been undertaking periodic surveys to determine the level of benefit fraud across the various welfare schemes<sup>170</sup>. In aggregate it is estimated that fraud and error<sup>171</sup> account for between 2.4 and 4.1 % of the annual welfare spend, however, undeclared work represents only a component of this. Nevertheless, the issue of undeclared work is considered a major problem in Ireland due to the revenue lost in

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<sup>165</sup> Internet: <https://www.eurofound.europa.eu/observatories/emcc/case-studies/tackling-undeclared-work-in-europe/labour-inspectorate-controls-ireland>

<sup>166</sup> Schneider, F., (2011). *The Shadow Economy and Shadow Economy Labor Force: What Do We (Not) Know?*, IZA Discussion Papers 5769, Institute for the Study of Labor (IZA).

<sup>167</sup> The Universal Social Charge is a tax payable on gross income, including notional pay, after any relief for certain capital allowances, but before pension contributions. Internet: <http://www.revenue.ie/en/tax/usc/> for more information.

<sup>168</sup> Internet: <http://www.economics.unilinz.ac.at/members/Schneider/files/publications/2012/ShadEcEurope31.pdf>

<sup>169</sup> World Bank's research working paper 5912 on "Informal Workers across Europe": Michails Hazans, December 2011; for measurement issues see Section 2.1 and Table 3, p.33; Internet: <http://ftp.iza.org/dp5871.pdf>.

<sup>170</sup> These surveys involve inspectors reviewing a random selection of claims from each benefit area to assess the underlying level of fraud and error to identify the scale of any excess payments.

<sup>171</sup> Error describes the situation where an excess payment is made from unintentional errors either through errors related to the administration of the benefit or incorrect information from the claimant.

fraudulent claims for both Jobseekers Allowance and Jobseekers Benefit<sup>172</sup>. Payments to jobseekers (both Jobseekers Allowance and Jobseekers Benefit) stood at EUR 3.7 billion in 2013 declining somewhat to EUR 3.3 billion in 2014. Survey based estimates suggest that fraud accounts for approximately 1.4 % of total expenditure for jobseekers allowance<sup>173</sup>. While no figure is available for excess payments in Jobseekers Benefit, if we apply the 1.4 % rate to total payments of Jobseekers Allowance and Jobseekers Benefit the data implies that eliminating fraud in this area, primarily due to undeclared work, could potentially save the Irish exchequer up to EUR 46 million per annum.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing Undeclared Work**

The **Department of Social Protection (DSP)** concentrates on reducing welfare fraud through its Fraud Initiative. The **Office of the Revenue Commissioners** (Revenue) aims to maximise the government's tax take by focussing on the shadow economy. The aim of the **Workplace Relations Commission** (WRC) established on 1 October 2015 is to maintain good workplace relations and promote compliance with relevant workplace legislation.

### **2.2.2 Characteristics of the responsible organisations**

The **DSP** supports the Minister for Social Protection in the discharge of governmental, parliamentary and departmental duties.<sup>174</sup> The Mission Statement of the DSP is to promote active participation in society through the provision of income supports, employment services and other services. Their main functions are to advise government and formulate appropriate social protection and social inclusion policies and to develop and deliver effective and cost efficient income supports, activation and employment services to clients. The DSP has over 6 700 staff.<sup>175</sup> The delivery of local services is organised on a regional basis with 3 regional and 13 divisional offices supporting a nationwide network of some 125 social welfare local and branch offices.

The **Office of the Revenue Commissioner's** Mission Statement is to serve the community by fairly and efficiently collecting taxes and duties and implementing customs controls.<sup>176</sup> Their core role is the assessment and collection of taxes and duties and their mandate derives from obligations imposed by statute and by government and as a result of Ireland's membership of the European Union. Their main functions are to assess, collect and manage taxes and duties that account for over 93 % of exchequer revenue. They also administer the customs regime for the control of imports and exports and collection of duties and levies on behalf of the EU and work in co-operation with other state agencies in the fight against drugs and in other cross departmental initiatives. There are over 110 Revenue offices countrywide with just over 5 700 staff.

The **WRC**, established on 1 October 2015, assumes the roles and functions previously carried out by the National Employment Rights Authority (NERA) [now the WRC], Equality Tribunal (ET), Labour Relations Commission (LRC), Rights Commissioners Service (RCS), and the first-instance (Complaints and Referrals) functions of the Employment Appeals Tribunal (EAT). Staff of the Workplace Relations Commission, are employees of the Department of Jobs, Enterprise and Innovation and its finances are

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<sup>172</sup> Jobseekers benefit is time limited and based on social insurance contributions whereas jobseekers allowance is means tested and has no duration limit for claiming. Claimants can migrate from jobseekers benefit to jobseekers allowance provided they meet the relevant criteria.

<sup>173</sup> Internet: [https://www.welfare.ie/en/downloads/JASurvey\\_14.pdf](https://www.welfare.ie/en/downloads/JASurvey_14.pdf), page 6.

<sup>174</sup> Internet: <https://www.welfare.ie/en/Pages/The-Department.aspx>

<sup>175</sup> Internet:

<https://www.welfare.ie/en/Pages/Overview%20of%20the%20Department.aspx>

<sup>176</sup> Internet: <http://www.revenue.ie/en/about/index.html>

administered through the department's budget and form part of the department's accounts. At the end of 2014 NERA [now the WRC], had 100 staff, including 57 inspectors spread over 5 regions and 30 staff trained as information officers.<sup>177</sup>

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

**Special Investigation Unit (SIU)** – Set up by the DSP in 1978 to detect and prevent social welfare fraud. In 1990 the SIU and Revenue Commissioners combined expertise and resources to set up Joint Investigation Units (JIUs) to investigate social welfare fraud and tax and PRSI evasion.<sup>178</sup> These specialist units also work in collaboration with An Garda Síochána (Irish police force) and Labour Inspectors of the WRC. The multi-agency JIUs identify and target sectors where UDW and shadow economic activity are common.

**The Hidden Economy Monitoring Group** - this is a multi-agency group which advances ideas and initiatives to combat UDW and shadow economic activity in Ireland. The group is chaired by Revenue and consists of representatives from government agencies including the DSP, the Department of Jobs, Enterprise and Innovation and the Workplace Relations Commission. There are also representatives from employer groups including the Irish Business and Employers Confederation, Retail Ireland, Small Firms Association, Construction Industry Federation as well as representatives from the Irish Congress of Trade Unions.

**High Level Group** – this group involves the senior executives from DSP and Revenue. Their aim is to ensure that collaboration is targeted at specific issues including social welfare fraud and tax evasion. In terms of collaboration with social partners, the Irish Business and Employer's Confederation (IBEC), the Small Firms Association (SFA), Services Industrial Professional and Technical Union (SIPTU) and the Irish Congress of Trade Unions (ICTU) submit policy proposals to government in order to educate employers and workers on their rights and obligations and in some cases pursue claims on behalf of the latter.<sup>179</sup>

**Cross Border Operational Forum** – this group comprises of senior fraud managers from the DSP, the Department for Work and Pensions and the Northern Ireland Social Security Agency of the Department for Social Development. The Forum's remit is to liaise at operational level and ensure that measures are in place to ensure effective co-operation, prevention and detection of fraud. Case by case data-matching takes place between the DSP and the Department of Social Development (DSD) in Northern Ireland on cases where social welfare fraud or abuse is occurring. In 2011, 4 288 checks were carried out by the DSD on behalf of the DSP. Similarly, 2 716 checks were carried out by the DSP on behalf of the DSD for the same year.<sup>180</sup>

Furthermore, a **Memorandum of Understanding between the Government of Ireland, the Government of the United Kingdom of Great Britain and Northern Ireland** is in place to ensure Co-operation and Mutual Assistance in the Administration of Social Security Programmes in matters of mutual interest in the areas of fraud in their respective social security systems and an annual summer school is run jointly by the

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<sup>177</sup> National Employment Rights Authority (2015). *Review of 2014*. NERA: Dublin. Internet: [https://www.workplacerelations.ie/en/Publications\\_Forms/NERA-Review-2014.pdf](https://www.workplacerelations.ie/en/Publications_Forms/NERA-Review-2014.pdf)

<sup>178</sup> Internet: <http://www.welfare.ie/en/Pages/SWI---Powers-of-Social-Welfare-Inspectors.aspx>

<sup>179</sup> Internet:

<http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1280&context=intl>

<sup>180</sup> Internet: <https://www.kildarestreet.com/wrans/?id=2012-11-06a.1353>

DSP and the DSD, Northern Ireland to explore issues of social policy facing their departments and their societies in general.

The DSP carries out data matching with external agencies to help detect fraud. The Irish government has legislated for the sharing of data among agencies for the purpose of fraud detection and control.<sup>181</sup> DSP aims to utilise this data effectively by employing predictive analytics to better detect potential fraud.

The Revenue authority examines electronic systems of businesses, copies and downloads electronic data for further analysis with use of computer-assisted intelligence automated techniques. Revenue also places a strong emphasis on the value of third party information in detecting UDW and shadow economic activity. This is facilitated through the anonymous reporting of suspected UDW by members of the public using an online form on the Revenue website. A similar form is provided by the DSP for reporting individuals suspected of fraudulently claiming welfare payments while working. The DSP also has a dedicated phone number for reporting suspected fraudulent claims.

In 2014, Revenue analysed 2.8 million PAYE transactions of which 10 721 were stopped for further investigation yielding EUR 1.4 million.<sup>182</sup> As of April 2014 the data sharing and data matching initiatives outlined in Section 1.3.2 led to 941 investigations resulting in the disallowance of EUR 25.7 million in social welfare payments.

At a wider EU level, NERA (now the Workplace Relations Commission) was directly involved in multilateral projects under the auspices of the EU and the International Labour Organisation (ILO) as follows:

- The joint ILO and European Commission project on strengthening the role of Labour Inspectorates in combating undeclared work.
- The exchange of best practices conducted through the 2012 Mutual Learning Programme peer review in the Czech Republic on "Upgrading of mechanisms to monitor undeclared work".
- PROGRESS – Posting of Workers: enhanced administrative cooperation & access to information. There are 14 Member States collaborating in an exchange of information on legislative and administrative practices.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Ireland employs a multi-agency approach to tackle UDW. As outlined above the main agencies involved are the **Revenue Commissioners, Department of Social Protection (DSP), Workplace Relations Commission (WRC)**. Other collaborative work among different agencies includes, Special Investigation Unit (SIU), the Hidden Economy Monitoring Group and High Level Group discussed in the section above.

### **2.3.2 Measures to tackle UDW**

*Deterrence Measures:* Revenue places a strong emphasis on the value of third party information in detecting UDW and shadow economic activity as discussed in section 1.2.3 above through anonymous online reporting. The JIUs take a sectoral approach with a focus on high risk sectors including construction, trade suppliers, the taxi sector, white collar sectors engaged in cash transactions, casual traders, couriers, clothes recycling,

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<sup>181</sup> Internet:

[http://www.oireachtas.ie/parliament/media/committees/pac/correspondence/2014-meeting12415/\[PAC-R-1362\]-Correspondence-3C.2---Dept-of-Social-Protection-Anti-Fraud-Strategy.pdf](http://www.oireachtas.ie/parliament/media/committees/pac/correspondence/2014-meeting12415/[PAC-R-1362]-Correspondence-3C.2---Dept-of-Social-Protection-Anti-Fraud-Strategy.pdf)

<sup>182</sup> Revenue, 2015a

car valeting, solid fuel merchants, hairdressers, security sector and haulage.<sup>183</sup> Streetscape Projects are strategies used by JIUs where an inspection is carried out in all cash businesses in a street, small town or village.

The DSP carries out data matching with external agencies to help detect fraud. The Irish government has legislated for the sharing of data among agencies for the purpose of fraud detection and control.<sup>184</sup> DSP aims to utilise this data effectively by employing predictive analytics to better detect potential fraud.

Revenue undertakes compliance interventions on individuals suspected of non-compliance. This typically begins with a telephone conversation and may escalate to a full audit. A range of potential sanctions exist depending on the severity of non-compliance.<sup>185</sup>

*Enabling Measures:* Preventative approaches are used in Ireland to stop UDW from happening in the first instance. The first step to prevent UDW from occurring is to provide information on employment options to jobseekers and employers.<sup>186</sup> The National Employment and Entitlements Service (NEES) and Public Employment Services (PES) are part of this approach through engagement with jobseekers. Reforms in 2012 (*Intreo* and *Jobpath* reforms) are designed to lead to more active engagement.

The introduction of the Home Renovation Incentive (HRI) Scheme in October 2013 provides for tax relief on home renovation and repair works carried out by qualifying contractors. This incentivises homeowners to use legitimate, tax-compliant contractors thereby limiting UDW in the construction sector.

During the first two years of NERA [now the WRC] multiple awareness campaigns were carried out across different sectors, including, hospitality, fishing and construction. The DSP has also used advertising campaigns to highlight the negative effects of social welfare fraud. NERA developed a Code of Practice and a Guide to Inspections document for employers, both available on their website. A code of practice for determining employment or self-employment status of individuals, prepared under the Programme for Prosperity and Fairness and updated by the Hidden Economy Monitoring Group in 2007 intends to eliminate misconceptions on who is a self-employed or a dependant worker.

Curative approaches are used to allow individuals engaging in UDW to legitimise their activities. Revenue allows a taxpayer to self-correct an error due to carelessness or non-recurring deliberate action without incurring a penalty. The taxpayer must notify Revenue in writing within twelve months of the due date for the tax return for the year in which the correction applies. If self-correction or innocent error does not apply then the taxpayer can make a qualifying disclosure before or during the compliance intervention.

Data availability on the effectiveness of measures associated with UDW is very limited in addition to precise measures of the extent of UDW in general.

In 2015 Revenue conducted 41 368 PAYE compliance checks which yielded EUR 21.6 million. There were 664 convictions secured for non-filing of Income Tax, Corporation

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<sup>183</sup> Department of Social Protection (2011). *Department of Social Protection Fraud Initiative 2011-2013*. Dublin: Department of Social Protection.

<sup>184</sup> Department of Social Protection (2014). *Compliance & Anti-Fraud Strategy 2014-2018*. Dublin: Department of Social Protection.

<sup>185</sup> Revenue Commissioners (2015b). *Compliance Code for PAYE Taxpayers*. Revenue Commissioners: Dublin.

<sup>186</sup> Mutual Learning Programme (MLP) Case Study (2012). *The Irish Approach to Tackle Undeclared Work*. EU 2020 Strategy Study.

Tax and Relevant Contracts Tax with EUR 1.7 million in fines. In 2015, 1 257 individuals were 'named and shamed' as tax defaulters with a court imposed fine/penalty. There were 160 settlements for tax avoidance which yielded EUR 42 million and 2 063 summary convictions for non-filers were obtained yielding EUR 6.4 million in fines.<sup>187</sup>

Audits focus on sectors susceptible to UDW and shadow economic activity. Revenue conducted 3 343 audits in the construction, retail, rental, wholesale, pubs, fast-food, doctors, accounting and legal sectors which yielded EUR 119 million in 2014.<sup>188</sup>

In 2014 SIUs generated fraud and control savings of EUR 64.5 million.<sup>189</sup> In 2014 the DSP recovered EUR 83 million in overpayments and over 315 cases were submitted for prosecution.<sup>190</sup> The number of calls to the DSP's dedicated phone number for reporting fraudulent claims increased from 17 000 in 2011 to 24 720 in 2013.<sup>191</sup> From 2011-2013 over EUR 1.9 billion in control savings was achieved through anti-fraud measures by the DSP.<sup>192</sup>

In 2014, NERA [now the WRC] carried out 5 591 workplace inspections involving 82 468 employees. The amount of unpaid wages recovered was EUR 861 416 in 2014. The overall rate of compliance was reported at 57 %. NERA also detected 600 possible breaches of the Employment Permits Acts in 2014 with 63 employers successfully prosecuted.<sup>193</sup>

### **2.3.3 Good practice**

The sharing of data among agencies and the use of data analytics has made the detection and prevention of UDW more efficient. DSP is committed to the widespread implementation of predictive data analytics models to make detection more efficient.

An example of good practice involving the multi-agency approach relates to a case in 2014 where DSP, Revenue and NERA [WRC] officials carried out an inspection on a construction site having received intelligence relating to possible fraud. Of the 48 employees interviewed on the construction site, 11 were found to have current social welfare claims. Savings of EUR 197 000 were made resulting from the cessation of claims and recovery of overpayments.<sup>194</sup> Awareness campaigns and reporting facilities also represent good practice. The number of anonymous tip-offs to the DSP has increased from 16 917 in 2011 to 24 720 in 2013. This indicates a low tolerance for undeclared work and welfare fraud in Ireland.

### **2.3.4 Challenges and barriers**

UDW and shadow economic activity tend to increase during recessions and periods of high unemployment. While unemployment in Ireland has been decreasing since 2012, it remains relatively high at 8.8 %.<sup>195</sup> The amount of data available in the integrated multi-agency system is difficult to analyse. There may also be data protection issues. The government has introduced specific legislation for the sharing of data. The DSP is working on improved data analytics models for analysing such data. Construction activity is increasing in Ireland. This is one of the main areas susceptible to UDW and government agencies must be vigilant in ensuring work is carried out by tax-compliant contractors.

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<sup>187</sup> Revenue Commissioners (2016). *Revenue Commissioners Headline Results for 2015*. Revenue Commissioners: Dublin.

<sup>188</sup> Revenue, 2015a

<sup>189</sup> Internet: <https://www.welfare.ie/en/pressoffice/Pages/pr091214.aspx>

<sup>190</sup> Department of Social Protection (2015). *Department of Social Protection Compliance & Anti-Fraud Strategy 2014-2018*. Dublin: Department of Social Protection.

<sup>191</sup> DSP, 2015

<sup>192</sup> DSP, 2015

<sup>193</sup> National Employment Rights Authority (2015).

<sup>194</sup> DSP, 2014

<sup>195</sup> Monthly unemployment rate for February 2016, Central Statistics Office (CSO).



The Home Renovation Incentive Scheme incentivises homeowners to use tax-compliant contractors.

## Factsheet on Undeclared Work – ITALY (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

In Italy a univocal definition of UDW, as defined by law, does not exist. From a judicial perspective, UDW is any regular and remunerated activity which has not been declared to the relevant authorities, such as the National Institute of Social Security (INPS), the National Institute for the Insurance against Accidents at Work (INAIL), the Revenue Agency, the Employment Services (Law 248/2006 Disposizioni urgenti per il rilancio economico e sociale, per il contenimento e la razionalizzazione della spesa pubblica, nonché interventi in materia di entrate e di contrasto all'evasione fiscale). The Law 183/2010 has strictly connected UDW with the formal communication to relevant authorities at the beginning of the employment relationship. In national accounts and according to Istat (Italian national statistical institute), the professional services that do not comply with the fiscal rules are considered non-regular. This is because these services are not observable in enterprises, institutions and administrative sources (Istat, 2015).<sup>196</sup>

In this perspective, ISTAT definition can be most relevant. The common understanding is that UDW should always be considered as the sum of: (i) "black" labour, i.e., the worker does not have any contract and is totally unknown to fiscal and enforcement authorities and, thus, she/he does not have any legal protection; and (ii) "grey" labour, i.e., the worker is regularly hired, but the amount of working hours declared is lower than the actual amount, or the declared remuneration is lower than the actual sum.

#### 2.1.2 Characteristics of undeclared work

In Italy, a crucial feature of UDW derives itself from the incidence of part-time employment, as a percentage of total employment. According to a pilot study carried out by Istat<sup>197</sup>, one fifth of part-time contracts correspond with full-time contracts but also include an under-statement of taxable amounts and cash-in-hand salary, as the actual working hours exceed the hours declared by 40%. Furthermore, in false part-time contracts, the pay-per-hour is lower than the pay of full time employees. It is worth mentioning that in Italy, according to the Eurobarometer<sup>198</sup>, the number of employees who received cash-in-hand payments decreased by 5% between 2007 and 2013.

Migrant employment is becoming more and more common in Italy. An Isfol study<sup>199</sup>, based on the findings of a survey on a sample of workers who are predominantly not regularly employed, indicates that 55% of irregularly employed migrant workers claim to be underpaid. "Black" labour among migrants involves mainly males, while the

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<sup>196</sup> Istat, *Non observed economy in national accounts (L'economia non osservata nei conti nazionali)*, Rome, 2015. Internet: <http://www.istat.it/it/files/2015/12/Economia-non-osservata.pdf?title=Economia+non+osservata+-+04%2Fdic%2F2015+-+Testo+integrale+con+nota+metodologica.pdf>

<sup>197</sup> Istat, Carlo De Gregorio, Annelisa Giordano, *"Half black": part-time contracts and full-time positions amongst employees of Italian companies ("Nero a metà": contratti part-time e posizioni full-time fra i dipendenti delle imprese italiane)*, Istat working papers, N. 3, Rome, 2014. Internet: <http://www.istat.it/it/files/2014/09/IWP-n.-3-2014.pdf>

<sup>198</sup> European Commission, Eurobarometer, *Undeclared work in the European Union*, Brussels, March 2014.

<sup>199</sup> Isfol, *Undeclared work of foreigners in Italy (Il lavoro sommerso e irregolare degli stranieri in Italia)*, Rome 2014, Internet: [http://isfoloa.isfol.it/bitstream/handle/123456789/895/Ficco\\_Iadevaia\\_Pomponi\\_Tagliaferro\\_Lavoro%20stranieri.pdf;jsessionid=468795E76FA95CA279D50F3A0B8A0497?sequence=3](http://isfoloa.isfol.it/bitstream/handle/123456789/895/Ficco_Iadevaia_Pomponi_Tagliaferro_Lavoro%20stranieri.pdf;jsessionid=468795E76FA95CA279D50F3A0B8A0497?sequence=3)

distribution between men and women stands at around 50% in “grey” employment. This arises because male workers tend to be employed in the sectors where “black” labour is highly concentrated, such as agriculture and construction. As for the age-group, both black and grey employment are concentrated in the 25-34 age group. “Black” labour is concentrated in Southern Italy (61%), while “grey” employment is concentrated in Northern regions (65%). Less educated migrants are more exposed to the risk of working in black employment, while higher education levels represent a sort of protection from exploitation conditions.

Another peculiar phenomenon is the illegal recruitment of agricultural workers for very low wages (“*Caporalato*”): where a mediator, often linked to criminal organisations, illegally provides jobs to these workers, which are mostly irregular migrants, and takes a percentage of their earnings. This is an extreme form of black labour, very close to slavery as the pay-per-hour is EUR 2.5 to 3.

Agriculture has traditionally been a sector with high UDW because of its seasonal character and because workers are hired on a daily basis. Eurispes<sup>200</sup> estimated that, in 2014, UDW in agriculture was at 32%. UDW is also high in the construction sector and in personal care/assistance, which is however, according to Istat, the only sector registering a decrease in the rate of irregular work over recent years (from 47.4% in 2011 to 45% in 2013). The highest increase of irregular employment is observed in the construction sector: from 13.5% in 2011 to 15.4% in 2013 (Istat, 2015).

No statistical evidence on the distribution of UDW by employer size is available. Generally, the enterprises concerned are small in size (between 5 and 10 employees) and not easily visible because they lack a legal headquarters. Trade unions tend to have less of a presence in these organisations than they do in larger one and a significant share of undeclared work is focussed within families, for personal care/household assistance and restaurants, where there is an extensive use of occasional services provided by people from their direct family members (Istat, 2015).

The main motivators for UDW can be grouped in: (i) *economic motivator* (UDW allows individuals to maximize the income of the enterprise and to avoid taxes and contribution burdens); (ii) *administrative motivator*: (UDW is favoured by the abuse of flexible forms of work and the spread of sub-contracting makes it easier for employers to abuse such flexible contracts and makes regulation much more difficult); (iii) *cultural motivator*: in some areas, mainly in Southern Italy, the unobserved economy is tolerated and UDW is perceived as a means of reciprocal assistance between employers and employees.

According to the 2014 Eurobarometer survey, 33% of those surveyed believe that taxes and social contributions are too high, while 32% believe that the lack of regular jobs is among the main drivers for UDW and 22% believe that salaries in regular jobs are too low. The fast evolution of immigration started in the 1990s and has further increased the labour market dualism between regular and UDW, as migrants are much more willing than Italian nationals to accept any form of employment.

### **2.1.3 Estimated scale of undeclared work**

According to the ISTAT (2016) report on the underground economy, in 2014 UDW was estimated to be around 3.6 million full-time equivalent units (FTEs), who were mainly employees (2.5 millions). The rate of undeclared work, defined as the share of FTEs in relation to the total labour input, was 15.7% (0.7 percentage points higher than in 2013). In the recent economic crisis, the overall contraction of employment has mainly affected regular employment, rather than non-regular employment. Between 2011 and

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<sup>200</sup> Eurispes and UILA, *Undeclared work, Survey on undeclared work in agriculture, (Sommerso, Indagine sul lavoro sommerso in agricoltura) Rome, 2014*. Internet: <http://eurispes.eu/content/sintesi-sottoterra-indagine-sul-lavoro-sommerso-agricoltura-eurispes-uila>

2013, the prevalence of non-regular employment has decreased significantly, reaching the minimum level registered in 2002-2003.

According to the latest Eurispes survey<sup>201</sup>, 28,1% of the sample has worked without contract in the previous year. This was experienced by more than: 50% of people who had been seeking their first job; 29.6% of students; 22.4% of housewives; and 13.8% of pensioners. It is also worth mentioning that the Foundation of Labour Advisors (*Fondazione Consulenti del Lavoro*) estimated that 1.9 million people work in a totally undeclared positions<sup>202</sup> but declining by about 200,000 units compared to 2014, thanks to the reform of labour market (*Jobs Act law - 2015*) and the three-year contribution exemption.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

Under the current system, UDW is mainly tackled by 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). The activities of these organisations are now coordinated by the new National Labour Inspectorate (NLI) who gathers all the relevant Offices involved in the field, implemented by Territorial Labour Offices (DTL).

The main aim of the NLI is to rationalise inspection activities, optimise the available resources and reduce the risk of overlapping and duplicating the activities of the different entities presently devoted to tackling UDW.

Today the Ministry of labour and social policies and the National Labour Inspectorate ensure the correct application of the law, including the rules applying in the construction sector, and of collective agreements, promote training, tackle UDW and verify that workers are legally contracted, while INPS and INAIL deal with compliance to social security rules. NLI will carry out all inspections.

### **2.2.2 Characteristics of the responsible organisations**

The core function of the NLI is to coordinate all of the inspection activities covering employment, social contributions, obligatory insurance, and health and safety at work; these activities are limited to some sectors, especially construction, while many controls are worked out by the local health authorities (ASL), for example in the maritime sector. This is done through:

- Planning inspection activities;
- Defining inspection procedures and tools, and developing guidelines and operational directives for all the personnel involved;
- Proposing targets and monitoring their achievement;
- Planning training activities for inspectors; and
- Seeking coordination with other relevant bodies.

The NLI will report to the Ministry of Labour and Social Policies; it will be run by the Director General and will be supported by an ad hoc committee (Central Commission for Coordination of Monitoring) of representatives from INAIL INPS, the Carabinieri (military police), the Finance Police, trade unions and employers' associations. The NLI will be based in Rome, with a maximum of 6,357 staff.

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<sup>201</sup> Eurispes, *Italy Report* (Rapporto Italia), Rome, 2016.

<sup>202</sup> Foundation of Labour Consultants, *Black labour costs 25 Billion* (Fondazione Consulenti del Lavoro, *Il nero costa allo stato 25 miliardi*), Press Release, Rome, 25 March 2016. Internet: [http://www.consulentidellavoro.it/files/PDF/2016/FS/Indagine\\_Lavoro\\_nero\\_FS.pdf](http://www.consulentidellavoro.it/files/PDF/2016/FS/Indagine_Lavoro_nero_FS.pdf)

### 2.2.3 Cooperation and collaboration between authorities and cross-border authorities

As mentioned in the paragraph 1.2.1, the new INL, ensures an effective model of cooperation between different Authorities.

The National Statistical System (Sistan), a network of public and private entities that provides the country and international organizations with official statistical information, collected from national and regional bodies, and including national and local institutes of statistics such as the ISTAT (the Italian national institute of statistics), the INAPP (National Institute for the Analysis of Public Policies, previously named ISFOL Institute for the development of vocational training of workers) and collect all the relevant data also coming from administrative sources.

The INPS has signed agreements with some regions, according to which regional and local authorities provide the INPS with access to databanks on workers who are enrolled within the PES Network and ensure information flows to the INPS regarding procurement.<sup>203</sup> Another agreement was signed between INPS and the Ministry in the framework of the Decree 109/2012 on the emergence from UDW of the irregular migrants. The INPS provided a list of all families and employers that have paid the lump-sum to regularise the contract of their employees. The objective of this action was to ensure an effective monitoring of the emergence from UDW.<sup>204</sup>

In order to tackle illegal mediation, the Ministry has also signed an agreement with the ACI (Italian Automotive Club). ACI provides labour inspectors with access to the Public Automotive Register (P.R.A.)<sup>205</sup> in order to double-check the ownership of vehicles used during production and to compare such data with information collected during inspections or taken from other databanks.

The Ministry also cooperates with the Finance Police (*Guardia di Finanza*) and the Military Police (*Carabinieri*) by providing training to on UDW and on the "maxi-sanction" (see below).

In the field of the campaign against the "Caporalato", recently (May 2016) a memorandum of understanding was signed between the Ministry of Labour and Social Policies, the Ministry of Defence, the Ministry of Agriculture and the National Labour Inspectorate with the aim of sharing information, strategies for a more and more effective system, involving the main relevant social parties and civil society organisations, interested in this issue.

In 2010, an agreement on safety and health at work and on posted workers was signed between the Italian Authorities and the Romanian Labour Inspection Service on undeclared work. The protocol envisaged coordinated inspection activities and timely communication of the changes occurred in labour legislation<sup>206</sup>.

Another form of cooperation dates back to 2008 when Italy signed an agreement with the French authorities on the exchange of information and of good practices on labour inspection, to be put into practice through periodic meetings and workshops. On the Italian side, INAIL and INPS were involved.

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<sup>203</sup> Internet: [http://www.regione.liguria.it/component/docman/cat\\_view/42-scuola-formazione-e-lavoro/100-lavoro/1114-qualita-del-lavoro-regolarita-e-responsabilita-sociale/1116-regolarita-del-lavoro/1156-protocolli-dintesa-in-materia-di-lavoro-sommerso-e-irregolare.html](http://www.regione.liguria.it/component/docman/cat_view/42-scuola-formazione-e-lavoro/100-lavoro/1114-qualita-del-lavoro-regolarita-e-responsabilita-sociale/1116-regolarita-del-lavoro/1156-protocolli-dintesa-in-materia-di-lavoro-sommerso-e-irregolare.html)

<sup>204</sup> Internet: [http://www.isfol.it/sistema-documentale/banche-dati/normative/2013/normativa-statale\\_2013/circolare-10-luglio-2013/20130710\\_CC.pdf](http://www.isfol.it/sistema-documentale/banche-dati/normative/2013/normativa-statale_2013/circolare-10-luglio-2013/20130710_CC.pdf)

<sup>205</sup> Internet: <http://www.lavoro.gov.it/archivio-doc-pregressi/Notizie/Protocollo%20ACI%202%20settembre%202015.pdf>

<sup>206</sup> Link to the protocol: <http://www.ance.it/docs/docDownload.aspx?id=9093>

In 2012 another Protocol was signed between the Italian Ministry of labour and social policies and the Ministry of labour, the family and the social protection of Romania, with the aim of cooperating and sharing data in the fight against the UDW.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The policy approach in Italy consists of the sanctioning system and enforcement procedures on the one hand, and the policy measures and incentives to transform UDW into regular employment on the other.

As for deterrence, three main tools are in place:

- (1) administrative sanctions, that can lead to the suspension of the business' activity and to economic/monetary sanctions (*maxi-sanction*)<sup>207</sup>;
- (2) civil sanctions, due in cases of failure to pay, incorrect payments or evasion of social security contributions;
- (3) penal sanctions, regulated by the penal proceeding code; and
- (4) promotion and prevention activities carried out by Territorial Labour Offices on UDW.<sup>208</sup>

As for enabling compliance, curative approaches have been implemented or are in place. After the experience in the '90s of the re-alignment contracts (see section 1.3.2) that can be considered within amnesties, similar policies have been recently adopted, such as the one aimed at promoting the regularisation of foreign irregular workers. A further policy tool is the job-voucher, which is becoming more commonly used by families and enterprises, which can also be considered a prevention action.

Another strategic prevention tool has been put in place by INL, with the aim of disseminating the culture of legality by programming and implementing specific prevention and promotion actions (by Article 8 of Legislative Decree 124/2004), through dissemination, information and update meetings, on the main innovations on work, social legislation and workplace safety field, addressed to employers and workers, trade union organisations or other professional organizations.

In order to combat the phenomenon of the "Caporalato", a new offence has been introduced (by law 199/2016) that punishes both the intermediary and the employer, who exploit workers in a position of weakness and in need, in the agricultural field.

### **2.3.2 Measures to tackle UDW**

The measures in place to tackle UDW in Italy can be summarised as follows.

**Re-alignment contracts:** Although their experience ended in 2001, they are worth mentioning as they represent the first measure introduced to tackle UDW: being specifically introduced to encourage enterprises to act legally within the cooperation between enterprises, trade unions and the public administration.

**Job vouchers:** the previous rule, recently abrogated by new legislation, introduced a remuneration system that employers could use to pay for workers, employed with discontinuity. The worker did not have to pay any tax but the activity was considered for pension calculations; the employer could act according to law, providing safety and health insurance (INAIL). The value of one voucher was EUR 10 and it could be used by families, enterprises, agricultural enterprises, not-for-profit organisations and public employers.

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<sup>207</sup> In accordance with article 22 of the legislative decree 151/2015

<sup>208</sup> In accordance with article 8 of the legislative decree 124/2004.

The recent legislation<sup>209</sup> in place of the so called "Voucher" has introduced two types of tools, with the same aim of the "Voucher": the one, signed by a private employer, for domestic works (the "libretto di famiglia") and the "occasional contract", signed by an enterprise, with no more than five employees, for any other work, except for building sector. Whereas, in the agricultural field, it can be only applied to unemployed, students and retired persons. These kind of contracts, provide the same social and fiscal benefits for employers and workers, than the previous instrument and can apply only through the INPS web site.

**Administrative sanctions** can be decided by inspectors of the Ministry, INPS and INAIL. A "maxi-sanction" is imposed when the employer has not duly informed relevant authorities of a new hiring. The "maxi-sanction" is applicable only in cases of dependent employment and is not applicable to household employment.

The new sanctions' regime, in force from September 2015, envisages three ranges that vary according to the length of the violation:

- From EUR 1,500 to 9,000 for each irregular worker, if he/she worked for maximum 30 days;
- From EUR 3,000 to 18,000 for each irregular worker, if he/she worked for maximum 60 days; and
- From EUR 6,000 to 36,000 for each irregular worker, if he/she worked for more than 60 days.
- The sanction is higher if workers are foreign or minors. Furthermore, the relevant authorities can suspend the business' activity if irregular workers constitute 20% of the total employees.

The "injunction mechanism" (*diffida*, ex art. 13 of Legislative Decree 124/2004) is also worth mentioning: the employer hiring irregular workers has to comply with the injunction by hiring and maintaining the irregular employee for a minimum 3 months (including, in cases of compliance with the injunction, proof of payment of taxes and social contributions and of one fourth of the fine envisaged by law, to be paid within 120 days). Such a mechanism is not applicable in cases of minors and of irregular non-EU migrants without a residency permit.

**Civil sanctions** are imposed by the INPS if employers delay notifying authorities of a new hire.

**Penal sanctions** can be imposed in case of child labour, workers without residence permits, and the exploitation of workers.

Vouchers mainly cover young people: 31% of beneficiaries are younger than 25. According to the Report of the Ministry of labour and social policies, in the first quarter of 2017, 28.5 million of Voucher have been sold, -2.1% compared with the first quarter of 2016.<sup>210</sup>

### 2.3.3 Good practice

An example of good practice that can be identified in Italy, has to do with the fight against all forms of UDW, with a focus also on *Caporalato*. In the summer and autumn months, ad-hoc local task forces have been set-up to tackle illegal job mediation in agriculture and UDW in tourist areas. Task forces are formed by inspectors, police forces; they have been concentrated in the areas most at risk of violations. This experience enables an exchange of practices and experiences between inspectors working in different contexts.

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<sup>209</sup> Law 96/2017

<sup>210</sup> <http://www.lavoro.gov.it/notizie/pagine/pubblicata-nota-trimestrale-su-tendenze-occupazione-iv-trimestre-2016.aspx/>

The investigations carried out in different areas, have made it possible to achieve important objectives in terms of irregularities found and sanctions imposed.<sup>211</sup>

Another example of good practice is the short access ("Accesso breve"), a form of inspection aimed at detecting UDW without investigating other areas of compliance.

Inspection accesses will be carried out, in advance, in geographically selected areas as they are considered mainly, to be at risk areas, but can be extended to the entire national territory.

Moreover, another important project, directed by the INPS, in cooperation with the Ministry of Labour and social policies, the Ministry of Defence, the Ministry of Agriculture and the National Labour Inspectorate, is the Quality Agricultural Work Network, in order to select agricultural companies and other subjects indicated by current legislation which, with the necessary requirements for registration, are distinguished for compliance with labour standards, social legislation, taxes on income and value added tax.

#### **2.3.4 Challenges and barriers**

A relevant challenge is to establish a mix of approaches that are tailored towards different targets (women, youth and migrants) in a way that reduces the convenience of working irregularly.

The quick implementation and development of both the National Agency for Active Labour Market Policies (ANPAL) and the National Labour Inspectorate is also a crucial issue in the future ability of the Country to (i) reduce the risk that in the transition from one job to another, workers without jobs or work-focused training opportunities are hired in an irregular manner and (ii) increase the probability of detecting UDW.

The biggest challenge remains however the cultural background, as any legislative and policy change will not be fully effective as long as UDW is not considered to be a relevant socio-economic problem.

In order to address these challenges, the latest labour market reform (Jobs act) introduced hiring incentives for permanent contracts, starting from January 2015. Private employers hiring new personnel can benefit from exemptions of social security contributions for a maximum period of 36 months.

With specific regard to young people, an inter-ministerial decree introduced important novelties on apprenticeships that are likely to promote the use of such measures (e.g. in order to hire further workers with a professional apprenticeship contract, enterprises with more than 50 employees are obliged to hire at least 20 % of the apprentices in force in the enterprise in the previous 36 months)<sup>212</sup>.

The key remaining challenge relates to migrants carrying out UDW. It is necessary to break the link between migration and UDW due to the fact that irregular migrants do not have options alternative to UDW. This could be eased by using ad-hoc contracts, or by increasing the efficiency of labour matching and, as a result, of the PES.

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<sup>211</sup> Rapporto annuale sull'attività di vigilanza in materia di lavoro e di legislazione sociale – anno 2016 – <https://www.ispettorato.gov.it/it-it/studiestatistiche/Pagine/Rapporti-annuali-sull-attivita-di-vigilanza.aspx>

<sup>212</sup> Legislative Decree 81/2015, art. 42, provision 8.



## Factsheet on Undeclared Work – LATVIA (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

There is no definition of undeclared work in Latvian legislation.

The Ministry of Welfare, State Labour Inspectorate (SLI) and State Revenue Service, key institutions in the area of UDW in Latvia, use the definition: *Work that is legal in its nature but work without a written employment agreement and/or without notification (registration) to the State Revenue Service.*

#### 2.1.2 Characteristics of undeclared work

The main types of undeclared work in Latvia are envelope wages and unreported employees. According to the SLI there is a shift from classic work without labour contract and without any registration of workers with the State Revenue Service to that of concluding labour contracts for part time work while in practice workers work full time and maybe even overtime.

According the study by Sauka and Putniņš<sup>213</sup>, which is the main local source of data on the shadow economy in Latvia<sup>214</sup>, in 2016 the shadow economy was estimated at 20.3% of GDP, and envelope wages made up 40.2% of this total while 17.7% could be attributed to unreported employees<sup>215</sup>.

The main sectors where undeclared work is found in Latvia are as follows: (the figures in brackets show the number of employees found working illegally in the 2015 and 2016 inspections of workplaces). In 2015 these were: construction (361), hotels and catering (202), agriculture, fishery and forestry (185), wholesale and retail (178) and manufacturing (168). The numbers of 2016 were: construction (357), hotels and catering (191), manufacturing (183), agriculture, fishery and forestry (155) and wholesale and retail (154).

Data for the shadow economy is available distributed by employer size. The average 2014-2016 figures are as follows:

- 1-5 (employees): 26.7% (shadow economy in the company)
- 6-10: 27.0%
- 11-20: 18.2%
- 21-50: 22.0%
- 51-200: 21.2%
- 200+: 22.7%

This data is also from the study by Sauka and Putniņš on the size of the shadow economy in the Baltics. In conformity with general practice in Latvia their definition of the shadow economy excludes illegal activity such as contraband, drugs trade, weapons trade, etc.

A key motivator for UDW in Latvia is low tax morale. However, the only data available is from the research Sauka and Putniņš' report on the shadow economy who find that the statistically significant factors are:

- Balance of costs and benefit associated with tax evasion;
- Discontent is associated with more shadow activity;

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<sup>213</sup> Putniņš, T., Sauka, A. (2017). SSE Riga Shadow Economy Index 2009-2016. Internet: <http://www.sseriga.edu/en/centres/csb/shadow-economy-index-for-baltics/>

<sup>214</sup> Estimates of the shadow economy in European countries by Friedrich Schneider yield similar results for Latvia i.e. in 2014 the estimate for Latvia was 24.7 % of GDP and in 2015 23.6 % of GDP. See Schneider 'Size and development of the shadow economy of 31 European countries and 5 other OECD countries from 2003 to 2015: different developments' Internet: <http://www.econ.jku.at/members/Schneider/files/publications/2015/ShadEcEurope31.pdf>

<sup>215</sup> Unreported business income formed the biggest share at 42,1%.

- Discontent with business legislation (strongest effect), State Revenue Service work, tax policy, government support for business (weakest effect);
- Higher tolerance of involvement in the shadow economy is associated with higher involvement in the shadow economy;
- Smaller firms tend to be more involved in the shadow as economy compared with large ones; and
- Russian speakers are more inclined to be involved with shadow activity.

No evidence is available for other types of UDW.

### **2.1.3 Estimated scale of undeclared work**

The main form of UDW is envelope wages where a worker has a legal work agreement but a significant share of remuneration is undeclared. The Putnins and Sauka estimate of the shadow economy in 2016 is 20.3% of GDP and, if we take their estimates of the importance of envelope wages and undisclosed workers in the shadow economy, then UDW, broadly defined, corresponds to about 11.8% of GDP.

The SLI conducts work place inspections to detect undeclared work and workers. In 2016 the SLI conducted 3,026 inspections with aim of detecting UDW, of which 431 were repeat inspections. The number of undeclared workers revealed was 1,371, 881 of whom were without a labour contract and without registration, 342 had a labour contract that was not registered, and 148 had no labour contract but were registered with the SRS. As a result 846 fines were imposed totalling EUR 609,497.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing Undeclared Work**

The main institutions responsible for identifying, tackling and preventing UDW are:

- the Ministry of Finance,
- the Ministry of Welfare,
- the State Labour Inspectorate,
- the State Revenue Service, and
- the Shadow Economy Combating Board (consisting of the Prime Minister, the Minister of Economics, the Minister of Finance, the Minister of Internal Affairs, the Minister of Welfare, the Minister of Transport, the Minister of Justice, the Minister of Health, the Minister of Agriculture, the Solicitor General, the Head of the Corruption Prevention and Combating Bureau, the Head of the State Labour Inspectorate, the Head of the State Revenue Service, the Head of the State Police Department, the Head of the State Health Inspectorate, the President the Employer's Federation of Latvia, the Chairman of the Municipality Association of Latvia, the Chairman of the Free Unions of Latvia, and the President of the Trade and Industry Chamber of Latvia). In addition there is a Consultative Board for Reduction of Shadow Economy operating under the Ministry of Finance.

However, in practice many other institutions may play a part in tackling and preventing UDW, including various police forces or the Border Guard. In the new draft "Action Plan for the Reduction of the Shadow Economy 2016-2020" 30 different institutions are listed as being involved.

The Ministry of Finance in association with the Ministry of Welfare and other ministries is responsible for development of legislation regarding UDW especially with respect to tax compliance.

The State Labour Inspectorate supervises and controls the enforcement and the general compliance of labour market practice with labour law.

The State Revenue Service collects taxes, it registers and enumerates tax payers, as well as controlling for the compliance of tax payers' documents with the law, prevents

and detects criminal activity associated with state taxes, fees, and other obligatory state payments, and customs duties;

The Shadow Economy Combating Board co-ordinates the organisations involved in measures aimed at preventing shadow economy activities.

### **2.2.2 Characteristics of the responsible organisations**

The Ministry of Finance (MoF) is responsible for (i) the formation of financial policy of the state including the state budget; (ii) organisation and coordination of tax policy; as well as (iii) performing various statutory regulatory functions. The MoF is interested in all sectors of the Latvian economy. The MoF is part of the central government and its coverage is national, it operates from its office in Riga.

The Ministry of Welfare (MoW) is responsible for (i) the formation of policies on employment and the labour market, social security, child and family rights, as well as equal opportunities for handicapped persons, and gender equality; (ii) organising and co-ordinating implementation of the above policies (iii) liaising with other labour market related institutions such as the State Employment Agency and the SLI. The MoW is concerned with all sectors of the Latvian economy. The MoW is part of the central government and its coverage is national, it operates from its office in Riga.

The State Revenue Service (SRS) collects taxes, registers and enumerates tax payers. It controls for the compliance of tax payers' documents with the law, and seeks to prevent and detect criminal activity associated with state taxes, fees, and other mandatory state payments, and customs duties. The SRS is interested in all sectors of the Latvian economy, is a sub-body of the MoF and covers the whole state. It operates from its office in Riga and has approximately 4 100 employees.

The State Labour Inspectorate (SLI) supervises and controls the enforcement of labour legislation including labour protection and health and safety at work. The SLI is interested in all sectors of the Latvian economy, is a sub body of MoW, and it covers the whole state. It operates from its main office in Riga, as well as its 5 regional inspectorate centres (there are structural SLI units in 13 different cities in Latvia). In 2016 the SLI employed an average of 165 persons.

The Shadow Economy Combating Board is a government body whose function is to coordinate all organisations involved in combatting the shadow economy. It consists of 19 board members, operates nationally and with interest in all sectors. Board meetings are organised in Riga.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

Although each of the executive authorities (SLI and SRS) operate separately, they can request data from other authorities (Article 12, paragraph 4 of SLI regulations and Article 4, paragraph 17 of SRS regulations ensure co-operation in the form of data sharing — *the general director of SRS can authorize the SRS officials to acquire and share information*).

In practice there are number of institutions (SRS, State Employment Agency, State Social Insurance Agency, Register of Enterprises, Road Traffic Safety Directorate, State Police, Border Guard, Municipal Police, State Fire and Rescue Service, Office of Citizenship and Migration Affairs, State Building Control Bureau, State Land Service, Fines Register, and the Rural Support Service) that SLI cooperates with in the terms of information sharing to help identify violations of the Labour Law (including undeclared work).

While the largest exchange of information is with the SRS the State Police and the Municipality Police also provide much information and administrative protocols to work on. Moreover, quite frequently joint inspections are practiced with the State Police, the State Border Guard and then Municipality Police. This is done for two reasons – the safety

of SLI inspectors (to prevent aggression from violators) and for cases where there might be obstacles to entering the premises

As described above and the MoW claims that this data sharing is very fast and highly efficient. Information is shared between SRS and SLI using an FTPS server where both institutions frequently put relevant information regarding companies where UDW has been discovered by any of the participant institutions.

There are no external evaluations of effectiveness but internally the SLI evaluates its co-operation with the SRS and other institutions involved as fairly effective.

In 2014, 38 Latvian labour inspectors participated in experience-exchange programmes in Slovakia, Finland, Estonia, and Lithuania which focussed on the monitoring and control of undeclared work.

There is an annual meeting of all three Baltic State SLIs where the agenda includes exchange of information and practices on UDW issues.

There has also been practical cooperation in the form of cases when information about violation performed in one Baltic country by a company from another country is then given to the neighbouring SLI to prosecute the case.

Also SLI are taking part and contributing to the European Platform tackling undeclared work, which **enhances cooperation between EU countries. It brings together relevant authorities and actors involved** in fighting undeclared work, to tackle this issue more effectively and efficiently, while fully respecting national competences and procedures.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Apart from policy implemented by the SLI, policy on UDW is seen as one aspect of policy on the shadow economy and a rather limited part at that since the main concern regarding the shadow economy is the lost revenue it represents rather than the economic distortions it generates.

The main instruments for addressing UDW are aimed at making the controlling mechanisms more effective i.e. deterrence. There have also been attempts at informing society of the negative consequences of UDW i.e. with the aim of improving tax morale. These have included: promotional campaigns and press conferences.

A new 'Shadow economy control strategy for 2016-2020'<sup>216</sup> was adopted in January 2016 and as usual improving revenue collection is the main aim of the plan and a mix of compliance and tax morale issues are noted to be addressed. However, from the point of view of UDW there is an important innovation: it is proposed that the payment of envelope wages be criminalised and employers who use them be subject to fines.

### **2.3.2 Measures to tackle UDW**

The SLI conducts inspections of workplaces in order to check for the presence of undeclared workers and other violations of labour legislation. Employers found employing undeclared workers are liable to fines.

For the period 2014-2016, there have been 3,998, 3,081, and 3,026 inspections conducted respectively, that revealed 1,586, 1,454, and 1,371 undeclared employed persons. The declining trend in undeclared employed persons is seen as a sign that policies are working, and is consistent with the evidence that the shadow economy itself appears to be declining.

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<sup>216</sup> Internet: <http://www.slideshare.net/FinMin/nu-ekonomikas-ierobeoanas-stratija-un-valsts-iestu-darba-plns-nu-ekonomikas-ierobeoanai-20162020gadam>

### 2.3.3 Good practice

In terms of the SLI definition of UDW, what has been found to work is more inspections and more targeted inspections as well as higher fines for violations.

Other practices that appear to work are:

- Changes in the regulations requiring the registration of a worker in the SRS at least 1 hour prior to employment, possibilities for the SLI to check this information and also impose a fine for non-compliance. This has probably contributed to decreasing the prevalence of UDW but this is difficult to prove;
- Access to the data bases of the SRS and other institutions as well as increased cooperation between the SLI and other institutions involved in combating UDW. Nevertheless, the truth is that the main form of UDW in Latvia – envelope wages – has hardly been addressed so good practice in this area is hard to find.

### 2.3.4 Challenges and barriers

Latvia's main challenge is systemic: both tax morale and tax compliance are low leading to a bad equilibrium where envelope wages are paid in one enterprise because most other enterprises are paying them. The challenge is to achieve a good equilibrium with high tax morale and high compliance as in the Nordic countries. It is unlikely that this can be done piecemeal and perhaps with existing institutions e.g. it has recently been revealed that a number of SRS employees have been involved in tax avoidance/evasion schemes. In the Latvia Competitiveness Report it was suggested that the SRS should be outsourced to an efficient tax administration such as the Danish one in the same way that the City of Stockholm has outsourced the management of its metro to the Hong Kong Mass Transit System.

There have been informational campaigns, the latest one being 'Work contract – safer tomorrow'<sup>217</sup>, which addressed specifically the costs of not having a work contract. There have also been numerous changes made to the tax policy in order to reduce the tax burden (e.g., increasing non-taxable income; increasing the minimum wage). However, all of these have been piecemeal and have not generated systemic momentum. The current 'Shadow economy control strategy for 2016-2020' looks quite promising on paper but the details have yet to be revealed (June 1st) and then implemented.

The key challenge remains systemic change. More specific challenges include: co-operation of workers in revealing undeclared work practices and tackling the causes of undeclared work rather than simply the consequences.

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<sup>217</sup> Internet: <http://www.vdi.gov.lv/lv/kampanas/sabiedribas-informesana/darba-ligums-drosaka-ritdiena/>

## **Factsheet on Undeclared Work – LITHUANIA (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

The notion of undeclared work is not defined in Lithuanian legislation (a definition is to appear in a new version of the Lithuanian Law on Employment, enforcement being foreseen from 1<sup>st</sup> of July 2017). The current Labour Code of the Republic of Lithuania (LC) only provides a definition of illegal work. According to the LC (Art. 98), illegal work is defined as work, which is performed in favour of an employer and under an employer's management or supervision, where in performance of his/her job functions the employee shall obey the established work organisation procedure, and which satisfies at least one of the characteristics below: (1) work is performed without the conclusion of an employment contract in writing although the characteristics of an employment contract are present; (2) the employer has not informed the State Social Insurance Fund Board (SSIFB) on the commencement of work one day before the expected commencement; (3) work is performed by foreign citizens, third-country nationals (TCN) or stateless persons employed without complying with the procedure of their employment established by regulatory acts; (4) work is performed by TCN employed in breach of the statutory requirements. Organisations with an interest in UDW in Lithuania are following the same definition.

#### **2.1.2 Characteristics of undeclared work**

According to the data<sup>218</sup> provided by the State Labour Inspectorate (SLI) and the State Tax Inspectorate (STI), the following types of infringements of labour relations appear to be the most common in Lithuania:

- Infringements relating to the recording and organisation of work (non-recording of all hours worked, non-recording or improper recording of overtime, night work and/or work on holidays; non-compliance with the requirements on the organisation of work and rest time; etc.). Infringements of this type accounted for 74% of a total of 1,208 infringements of labour relations registered by the SLI in Lithuania in 2016.
- Infringements relating to remuneration for work (envelope wages, inappropriate wording of employment contracts resulting in incorrect remuneration for work and non-payment of taxes to the state, etc.). The latter infringements made up 15% of all infringements of labour laws detected by the SLI in Lithuania in 2016.
- Infringements relating to the signing, performance and termination of employment contracts (work is performed without a contract of employment; civil contracts with individuals engaged in bogus activities under individual business certificates/licences are substituted for employment contracts; transacting individual business without registration; recruitment of TCN without complying with the statutory procedure (without employment contracts, residence/work permits); etc.). Infringements of this type accounted for 14% of all infringements of labour laws identified by the SLI in Lithuania in 2016.

The recent trend in Lithuania is that the share of infringements relating to the signing, performance and termination of employment contracts has been going down (from 37% in 2009 to 11 % in 2016 in the total number of detected infringements of labour laws), while the share of infringements relating to work and rest time has been growing (from 32% in 2009 up to 73% in 2016).

The construction sector has been the most risky for a number of years: according to the SLI, construction sector accounted for 50.9% of the total number of undeclared (illegal)

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<sup>218</sup> Shadow economy: Inspection results and trends in 2009-2014. State Labour Inspectorate, State Tax Inspectorate, 2015 Available on Internet at: [http://www.vdi.lt/PdfUploads/ND\\_SeselineEkonomika.pdf](http://www.vdi.lt/PdfUploads/ND_SeselineEkonomika.pdf)

workers detected in Lithuania in 2016. Other sectors where undeclared work is found include other community, social and personal service activities (9.7%), wholesale/retail trade (9.3%), agriculture, forestry and fisheries (8.5%) and accommodation and catering services (6.4%).

According to STI's figures, in 2016, the biggest number of infringements relating to paying envelope wages was detected in such sectors as wholesale and retail trade and repair of motor vehicles (29% of the total detected infringements), manufacturing industry (13%) and construction (26%).

Although there is no official data, SLI experts note that small enterprises (with 10-50 employees) and micro enterprises (up to 10 employees) account for the majority of detected cases of UDW in Lithuania.

Based on research findings (Pocius<sup>219</sup>, 2015; Patapas and Gudonis<sup>220</sup>, 2014), one of the main motivators for UDW in Lithuania is the high tax burden and low wages: in the conditions of the overall low level of income and high tax wedge, people are more inclined to increase their income through UDW. Other identified motivators for UDW in Lithuania include a high administrative burden (in case of labour relations), in order to continue receiving support from the state (e.g. unemployment or social benefits) after entering employment, and avoidance of financial obligations (e.g. payment of child support, debts, etc.).

### **2.1.3 Estimated scale of undeclared work**

Based on SLI's data, institutions for control and prevention of undeclared work identified a total of 2,171 undeclared (illegal) workers in 2016 (as compared to 2,393 in 2015). During 2009-2016, the total number of detected undeclared (illegal) workers increased by 47.2%: from 1,474 to 2,171. According to the SLI, 1,208 infringements of labour laws were detected in 2016 (as compared to 1,013 in 2015). In 2016, the STI detected a total of 45 cases involving payment of wages not reflected in accounting records. The amount of paid down unaccounted wages exceeded EUR 534,000.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

In Lithuania, UDW control functions are delivered by five state institutions, namely: STI, SLI, SSIFB, the Financial Crime Investigation Service (FCIS) and the Police Department (PD). Most of inspections are carried out and most infringements are identified by the SLI and STI (52% and 44%, respectively, of total infringements in 2016).

The SLI is assigned the function to carry out control of UDW, as well as to coordinate activities of institutions carrying out control of UDW in accordance with the procedure established by the Government of the Republic of Lithuania (GRL). By controlling the compliance with laws regulating labour relations, the SLI inspects compliance with the provisions of the LC, including those related to employment contracts, work pay, organisation of work and rest, as well as the enforcement of respective legislation.

The STI carries out control of undeclared (illegal) work, payment of envelope wages, infringements of the procedure of wage accounting and payment, as well as other functions delegated to it in the STI Regulations and other legislation.

The PD is responsible for carrying out control and prevention of undeclared (illegal) work and human trafficking for forced labour.

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<sup>219</sup> Pocius, A. Evaluation of shadow economy and informal employment in Lithuania. Lithuanian Journal of Statistics. 2015. Vol. 54, No.1, p. 18-32. Available on Internet at: <http://www.statisticsjournal.lt/index.php/statisticsjournal/article/viewFile/138/pdf>

<sup>220</sup> Patapas, A.; Gudonis, N. The problem of undeclared work control efficiency in Lithuania. Public Policy and Administration 2014, Vol. 13, No. 4, p. 659-670. Available on Internet at: <https://www.mruni.eu/upload/iblock/d96/VPA-14-13-4-09.pdf>

The SSIFB receives employer notifications of signed employment contracts and collects such information in the information system of the SSIFB. SLI inspectors check employment-related information in the course of their control operations.

According to Law No IX-816 on the FCIS, it detects and investigates the acts related to fraudulent or negligent keeping of accounts of taxpayers, submission of knowingly false data on taxes, state (municipal) fees and charges and other payments to responsible institutions and agencies, evasion of taxes, state (municipal) fees and charges, state social insurance contributions and other payments, etc.; implements preventive measures against evasion of taxes, state (municipal) fees and charges and other payments.

### **2.2.2 Characteristics of the responsible organisations**

The SLI performs prevention of violations of legislation regulating OHS, labour relations, as well as the prevention of accidents at work and occupational diseases in enterprises, by controlling the compliance with this legislation and by providing consultations to employees, their representatives, trade unions, employers, OHS services and committees in enterprises, as well as carrying out a public educational role within the framework of the SLI competence. In total, approximately 300 employees (including administration officers) were working at the SLI in 2016.

The STI is a central tax administrator subordinate to the Minister for Finance. The key tasks of the STI are to assist taxpayers and tax withholding agents; to implement tax laws; to ensure the payment of taxes to the budget; to ensure efficient work of local STI offices. In 2016, the STI had a total of 10 service offices with approximately 1,300 staff members (including administration officers).

The SSIFB is an agency established at the Ministry of Social Security and Labour (MSSL) to organise state social insurance (SSI) and handle and account for SSIFB's funds in an expeditious manner. While organising SSI, the SSIFB performs the following functions: ensures the implementation of the goals and objectives of social insurance policy set by the MSSL and of the tasks assigned by the GRL; ensures the implementation of legislation regulating SSI; presents offers to the MSSL on the improvement of SSI legislation and performs other functions. The SSIFB's structure consists of the Board, two specialised units and 10 local (territorial) units with 63 customer contact points. In 2016, about 3,400 staff members were employed within the Board and units in total.

The FCIS is a state law enforcement agency accountable to the Ministry of the Interior (MI). It is a public legal entity with the purpose of detection and investigation of crimes, other violations of law against the financial system and related crimes, other violations of law. In total, approximately 160 employees were working at the FCIS in 2016.

The PD is a central agency of the interior for the organisation and control of the functioning of the police system in order to ensure public order and the safety of individuals and the general public. The PD is headed by the Police Commissioner General. In 2016, the PD had approximately 200 employees.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

In accordance with GRL Resolution No 1407 of 26 November 2001 On Coordination of Control Measures over Illegal Employment, the SLI was commissioned to coordinate UDW control measures implemented by the SSIFB, STI, FCIS and PD. This Resolution also defined the functions of the institutions and the scheme of cooperation for UDW control. In compliance with the Resolution:

- The SLI drafts methodologies and recommendations for controlling UDW, organises seminars, sets the procedure for joint UDW inspections; drafts forms for recording UDW, analyses the inspection results and submits conclusions; organises educational activities and meetings of all institutions and agencies involved in controlling UDW;



- The FCIS carries out operational activities at a request of institutions controlling UDW and implements prosecution activities when the constituent elements of financial crimes are identified; and
- The PD, within the limits of its competence, provides assistance to public authorities and agencies carrying out prevention of UDW.

The aforementioned institutions regularly exchange relevant information, organise joint UDW inspections and large-scale check-ups of risky ventures. In addition, every year Lithuania approves UDW control and prevention measures aimed at combating UDW. On 17 March 2016, the *Commission for the Coordination of Cooperation among the State Institutions of Economic and Financial Control and Law Enforcement Institutions* approved the Measures for Combating the Shadow Economy in 2016–2017. One chapter of this paper, “Transacting unregistered economic activities and/or avoidance of income recognition and illegal work” is dedicated to UDW. It provides for UDW control measures and institutions responsible for the implementation thereof. These institutions report on a semi-annual basis the progress of the implementation of assigned tasks and measures to the Chancellery of the GRL (CGRL).

Cooperation between authorities is effective as the authorities not only regularly exchange relevant information, but also work together and implement joint operations. For example, in 2015-2016 target inspections were carried out by the SLI together with the STI and the PD in the construction sector, public catering enterprises, and sports and entertainment clubs. In 2016-2017, the SLI, STI and SSIFB conducted joint check-ups in undertakings paying MW or lower wages to the majority of their employees. In addition, interdepartmental groups are set up to deal with specific issues. On a regional level, there are coordination councils and UDW coordination groups composed of representatives from all institutions involved in the control and prevention of UDW.

The SLI has signed two bilateral collaboration agreements with Poland and Norway, and a trilateral agreement with Latvia and Estonia. The mentioned agreements are aimed at promoting institutional cooperation and exchanging relevant information between the countries. There are annual conferences held with Latvia and Estonia to discuss UDW control-related problems and exchange good practices.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

In order to reduce the scale of UDW, Lithuania applies both deterrence and enabling compliance policy approaches. From 2012 onwards, there is an increasing emphasis on the enabling compliance policy approach in Lithuania, whereas until 2012, more emphasis was put on the methods of detecting and punishing non-compliances in tackling undeclared work. With regard to the enabling compliance approach, the method of fostering commitment is probably most frequently applied in Lithuania, based on awareness-raising and information campaigns for different social groups to inform them of the costs and risks related to undeclared work. It is also important to note that Lithuania has recently made big progress in strengthening collaboration with various education establishments and NGOs in order to change population’s attitudes towards UDW and, consequently, to reduce the incidence of UDW in Lithuania.

### **2.3.2 Measures to tackle UDW**

In order to ensure compliance with tax obligations related to labour relations, the following deterrence measures have been in place in Lithuania since 2010:

- Inspections carried out by national authorities (both individual and combined efforts). When choosing companies to be inspected, particular attention is paid to companies most prone to UDW (construction, woodworking, other) and those hiring the majority of employees on a part-time basis and/or paying wages close to MW. In 2016, the controlling bodies identified a total of 2 171 of undeclared workers in Lithuania;

- Systemic model of preventive control measures “Warned to Choose”. In accordance with this model, the managers of companies qualified as risky taxpayers are sent warning letters or invited to the STI to give explanations on low wages or other risk indicators. Failing to explain the existing situation or rectify it within a certain time, the companies are subject to strict control procedures by the STI. In 2016, STI and SSIFB officers sent more than 40 000 warning letters of this type to companies’ managers;
- Administrative penalties. In compliance with Article 413 of the Code of Administrative Violations of Law of the Republic of Lithuania (ATPK), for undeclared (illegal) work the employers or their representatives shall be subject to a penalty ranging from EUR 868 to EUR 2,896 for each undeclared (illegal) worker. According to UDW protocols issued by SLI inspectors, penalties imposed on employers by courts exceeded EUR 293,000 in 2016; an average penalty was EUR 817.5 per undeclared (illegal) worker.

As mentioned above, the SLI and other authorities not only carry out strict control of UDW, but also pay attention to measures to prevent UDW/promote transparent business, such as:

- Holding awareness-raising campaigns in schools and other vocational education and training establishments, local (territorial) units of the Lithuanian Labour Exchange (LLE) and youth centres to highlight the rights and obligations of persons in the area of labour relations, the importance of the legality of labour relations and the negative effects of UDW. In 2016, the SLI held 47 seminars in local LLEs, 79 seminars in LLE’s youth centres, and 64 educational events for students;
- Organising consultancy seminars for small- and medium-sized enterprises, start-ups, municipal institutions and other economic entities. In 2016, 167 seminars were organised for companies and 5 consultancy events on UDW prevention were held for municipal institutions;
- Posting press releases on the prevention of UDW. In 2016, there were 33 press releases posted in relation to UDW prevention and labour law;
- Preventive comic films highlighting the importance of bringing employment relationships within the law (conclusion of employment contracts, recording of overtime, etc.). These films were posted on the SLI’s website and social networks, displayed next to cash registers in shopping centres, large stores and public transport.
- The SLI’s displays a helpline number on its website urging to report UDW cases.

The aforementioned action plan for UDW measures, as approved in February 2017, provides for the following key performance indicators used to assess the effectiveness of measures in Lithuania:

- The number of violations of labour laws – a total of 1,208 violations of labour laws were recorded in 2016, i.e. approximately by 19.2% more than in 2015;
- The amount of imposed penalties – according to the protocols of administrative violations of law issued by SLI inspectors, penalties imposed on employers by courts exceeded EUR 293,000 in 2016;
- The number of identified undeclared (illegal) workers – in 2016, institutions for the control and prevention of UDW detected a total of 2,171 undeclared (illegal) workers in Lithuania, including 1,338 persons transacting unregistered business activities and 833 undeclared (illegal) workers. The total number of undeclared (illegal) workers detected in 2009-2016 increased by 47.3%, from 1,474 in 2009 to 2,171 in 2016;
- A decrease in the share of employees paid less than MW – according to the STI, the share of employees earning minimum wage or near-minimum wage decreased by 2.66 percentage points from 21.34% in January 2016 to 18.68% in December

2016. In companies where the “Warned to Choose” model was applied, a decrease in the percentage of employees paid minimum or lower wage was around 7%.

Moreover, there are a number of other indicators used to assess the effectiveness of individual measures to combat UDW (e.g. the calculated amount of additional taxes payable to the budget; the number of initiated pre-trial investigations, etc.).

### **2.3.3 Good practice**

To reduce risks relating to non-recording of all hours worked by employees and payment of a part of wage/salary in envelopes, the STI, in cooperation with the SLI and the SSIFB, has for several years now applied a complex model of sanctions, known as the “Warned to Choose” model. Risky taxpayers, selected by a decision of the interdepartmental working group, have been sent more than 40,000 warning letters. According to the STI, this measure has proved to be effective: in companies where the aforementioned model was applied, average wages increased by approx. 24% in Q4 of 2016 comparing to Q4 of 2015.

### **2.3.4 Challenges and barriers**

One of the challenges is that the number of undeclared (illegal) alien workers is growing in Lithuania: in 2009, 15 undeclared (illegal) alien workers were identified compared to 58 identified in 2016. One more recent trend is TCN, especially Ukrainians, who obtain visas in Polish travel agencies and arrive to work in Lithuania. Not aware of their rights and not knowing the Lithuanian language, they often live and work in subhuman conditions and are not adequately paid for work.

Several pre-trial investigations have been launched concerning likely human trafficking for forced labour, abuse of aliens and smuggling of aliens across the Lithuanian borders. There are responsible institutions to monitor the situation; legislation is being improved; etc. Due mention should be given to the Recommendations for identification of victims of trafficking in human beings, pre-trial investigation and interdepartmental cooperation, as approved by Order No. I-327/1V-1015/A1-758 of 17 December 2015 of the Prosecutor General of the Republic of Lithuania, the Minister for the Interior of the Republic of Lithuania and the Minister for Social Security and Labour of the Republic of Lithuania, which are currently followed by officers from various institutions/authorities and NGO professionals dealing with human trafficking for forced labour in Lithuania.

- It is not always easy for authorities to identify infringements relating to labour relations (e.g. signing of civil contracts instead of employment contracts) due to the relatively low number of inspectors against the number of (possibly – bogus) self-employed people;
- Tax administrators lack the specialised knowledge of law, for example, to separate royalties from salaries. According to a Report<sup>221</sup> of the National Audit Office of Lithuania, it is difficult to prove that royalties paid to persons actually constitute salaries/wages.

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<sup>221</sup> Summary information. National Audit Report on Taxation of Personal Income No. VA-P-60-16-16. September 23, 2008. National Audit Office of Lithuania. Available on Internet at: [https://www.vkontrole.lt/failas\\_senas.aspx?id=2744](https://www.vkontrole.lt/failas_senas.aspx?id=2744)

## Factsheet on Undeclared Work – LUXEMBOURG (July 2016)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

Undeclared work, referred to in the context of Luxembourg law more precisely as clandestine labour (*travail clandestin*), is defined explicitly by the 1977 law<sup>222</sup> (and reinterpreted by a consecutive series of cases of jurisprudence since the introduction of the legal framework in the 1970s<sup>223</sup>) and reconsidered under article L.571-1 of the Code of Work introduced by law in 2006<sup>224</sup>. Undeclared work, concerning both wage earners and the self-unemployed, is defined in the law first for the self-employed as 'the activity on a self-employed basis of any occupational activities listed in Article 1er of the Law of 2 September 2011 regulating access to the professions of craftsman, traders and industrial to certain liberal professions without being in possession of the authorisation provided there' and second, for wage earners, in the case of 'the provision of wage labour, when the wage earner exercise, knows that the employer does not have the authorisation provided by the Law of 2 September 2011 mentioned above or, knows that his position as an employee is not lawful under the laws concerning deductions on wages or legislation on social security'<sup>225</sup>. The 2011 law<sup>226</sup> mentioned in the context of non-declared work does not only stipulate the access to these specific activities, but also ensures their protection as far as illegal access is concerned.

The definition followed by the main actors in Luxembourg is based on an existing legal framework and therefore broadly shared.

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<sup>222</sup> Loi du 3 août 1977 ayant pour objet : I. d'interdire le travail clandestin, II. de modifier l'article 26 a) de la loi du 2 juin 1962 déterminant les conditions d'accès et d'exercice de certaines professions ainsi que celles de la constitution et de la gestion d'entreprises, modifiée et complétée par la loi du 26 août 1975, Mémorial A, numéro 45, 8 août 1977 (Law of 3 August 1977 on the suspension of undeclared work).

<sup>223</sup> Some parliamentary questions introduced since the enforcement of the law have also dealt with non-declared work such as the latest to have been introduced in October 2014 (Parliamentary question Nr. 548, 25 September 2014, [www.chd.lu](http://www.chd.lu)).

<sup>224</sup>

Internet:

[http://www.legilux.public.lu/leg/textescoordonnes/codes/code\\_travail/Code\\_du\\_Travail.pdf](http://www.legilux.public.lu/leg/textescoordonnes/codes/code_travail/Code_du_Travail.pdf)

<sup>225</sup> For the purpose of this factsheet, the expert has translated the original French law as there is no official English translation available. The original text stipulates in the definitional context that '*Est considéré comme travail clandestin: 1. l'exercice à titre indépendant de l'une des activités professionnelles énumérées à l'article 1<sup>er</sup> de la loi du 2 septembre 2011 réglementant l'accès aux professions d'artisan, de commerçant, d'industriel ainsi qu'à certaines professions libérales, sans être en possession de l'autorisation y prévue; 2. la prestation d'un travail salarié, lorsque celui qui s'y livre: a) sait que l'employeur ne possède pas l'autorisation prévue par la loi du 2 septembre 2011 précitée, ou b) sait que sa situation en qualité de salarié n'est pas régulière au regard de la législation concernant les retenues sur salaires ou de la législation relative à la sécurité sociale*'.

<sup>226</sup> Loi du 2 septembre 2011 réglementant l'accès aux professions d'artisan, de commerçant, d'industriel ainsi qu'à certaines professions libérales et - modifiant l'article 542-2 du Code du travail; - modifiant la loi modifiée du 16 juillet 1987 concernant le colportage, la vente ambulante, l'étalage de marchandises et la sollicitation de commandes; - modifiant la loi modifiée du 10 juin 1999 relative à la profession d'expert-comptable; - portant abrogation de la loi modifiée du 21 février 1976 ayant pour objet d'instaurer un jour de fermeture hebdomadaire dans les stations de vente de carburant et de lubrifiant pour véhicules automoteurs, Mémorial A, number 198, 22 September 2011 (Law of 2 September 2011 regulating access to the professions of craftsman, traders and industrials, and to certain liberal professions, Memorial A, Number 198, 22 September 2011).

### 2.1.2 Characteristics of undeclared work

Research for this factsheet has not revealed any data on prevalent types of undeclared work in Luxembourg.

National Labour Inspectorate (the *Inspection du Travail et des Mines* – hereafter the ITM<sup>227</sup>) data for 2016<sup>228</sup>, in respect to their own controls and investigations, show that the restaurant/accommodation industry, the transport and commerce industries, as well as the construction and industry sectors, are predominant sectors where undeclared work is found. Available data, however, does not indicate if these controls and investigations are directly related to non-declared work or if other missions by the ITM were carried out during these controls and investigations.

For the research of this factsheet, no data has been found on the relation between employer size and non-declared work. However, a succinct overview of press articles related to what is referred to as '*coup de poings*' (larger controls) reveals that both larger and smaller companies resort to various strategies of undeclared work. However, the material is scarce so that an overall picture of the situation is impossible to be drawn. An example of a larger control conducted by the ITM was reported in the press by the government in 2011 and dealt with undeclared work (together with controls of health, working conditions, and security standards) on a construction site with more than 21 companies controlled and a total of 129 employees<sup>229</sup>. This example shows the various aspects of controls, and their breadth both in terms of elements under control, inter-ministerial cooperation between agencies, as well as mobilisation of manpower.

A thorough archival research for this factsheet has revealed that the subject is still understudied, with no qualitative data on the motivations behind illegal work. Non-declared work in Luxembourg is difficult to measure and only estimations exist with a few components being studied. However, Clément and Maas (2007)<sup>230</sup>, in a pioneering work on non-declared work in Luxembourg and based on a larger trade union study - entitled '*Etude 2Plus*' - financed by the government and the FSE in 2006, sought to identify some potential motivations behind non-declared work. More broadly, these authors conclude that most drivers are in the majority of cases economy-related such as for example that non-declared work would permit avoiding paying social contributions and as a result increase company revenues. For employers, in particular, illegal work is identified as a means to avoid staff costs and the payment of VAT. The study also unravels the following potential pillars of undeclared work: administrative burdens for companies to declare jobs; or the reduction of costs when resorting to non-declared work as a company strategy to survive in competitive activity sectors.

Although these motivations should be cautiously evaluated (with an obvious bias due to the fact that the research was conducted by the trade union and no longer existing research centre, Jean Baptiste Rock), they have not lost their relevance and should constitute a guide for future studies in the field of non-declared work: VAT has increased since January 2015 (consumer consumption increased before implementation, but decreased afterwards) and the fact that some sectors (such as construction) remain highly competitive, especially if crisis-related tensions on the sectors are considered. At the same time, efforts have been made at the government and municipal levels to better regulate, but the impact on non-declared works remains unknown. Clément and Maas (2010), in their study, rightly point towards the still non-studied phenomenon of 'occult

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<sup>227</sup> Internet: <http://www.itm.lu/home.html>

<sup>228</sup> Internet:

<http://www.itm.lu/files/live/sites/Itm/files/Itm/Rapports%20Annuels/06.pdf> (p. 34)

<sup>229</sup> Internet: <https://www.gouvernement.lu/756169/15-itm?context=971660>

<sup>230</sup> Franz Clément and Roland Maas, *Le travail non déclaré au Luxembourg*, Luxembourg Institute of Socio-Economic Research LISER (former CEPS/INSTEAD), col. Gouvernance et Emploi, Number 1, November 2007. Internet : [www.liser.lu](http://www.liser.lu)

subcontracting' (*sous-traitance occulte*), a phenomenon which involves companies under subcontracts for companies and with non EU workers who are conducting tasks inter-professionally. Another research focus could be the question of why non-declared work flourishes in particular in new activity sectors: this constitutes an element to be further explored in the face of a diversified economy in Luxembourg and new emerging sectors such as ICT, logistics or activities in the finance sector. Other potential motivations have been hinted at in the press reveal why individuals would resort to non-declared work for financial reasons (i.e. jobseekers who like to earn some extra cash) or in the case when companies refuse to conduct smaller tasks in private homes for example<sup>231</sup>. More recently, related to the self-employed, the Minister of Labour and Employment has identified the phenomenon of so-called '*salariés autoemployeurs*' (a mix between adopting the status of employee and employer in parallel) and where the working relation is difficult to be made out<sup>232</sup>.

### **2.1.3 Estimated scale of undeclared work**

Research for this factsheet reveals that data on the number of cases of non-declared work in Luxembourg are not available<sup>233</sup>. The only found estimations on non-declared labour for 1998 are identified in the 2007 study by Clément and Maas (2007): between 15 000 and 42 000 (representing between 6.3 % and 17.7 % of the working population of 236 400 at the time of this publication. Since the publication, the study on the estimated number of non-declared workers has not been re-conducted and no additional data has become available. The study only provides an estimated number, while the scale in different sectors as well as the type of non-declared work has not been estimated. In terms of controls, ITM provides the following data in its 2014 report<sup>234</sup>: 680 controls were conducted (among which there were 13 in industry, 51 in the construction sector, 60 in commerce, 120 in the transport sector, 283 in accommodation and catering, and 69 in ICT and financial activities; further, a total of 105 investigations were carried out with 13 in industry, 7 in the construction sector, 60 in commerce, 65 in accommodation and catering, and 2 in ICT and financial activities, with a majority of these occurring at the level of the Luxembourg-city branch. No information on the number and type of business entities controlled are disclosed. More linked to non-declared work (related to health and safety at work), 257 were conducted out of which 31 breaches of law were identified<sup>235</sup>. At the moment of writing, no data on fines, lost revenue, or the share of the different types of non-declared work in the estimated size of non-declared work could be identified.

Considering the rapid growth of the workforce since the publication of the above study, it is likely that the abovementioned figures have increased too. The law also stipulates that activities of 'a lesser importance' are not regarded as clandestine work so that it is difficult to identify a final number of non-declared cases.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

Undeclared work in Luxembourg is tackled through the cooperation of a network of several government agencies. The interacting network is referred to as the Inter-administrative unit to fight against illegal work (*Cellule inter administrative de lutte contre le travail illégal* - CIALTI). The main actor is the National Labour Inspectorate (ITM). Other actors which are usually mobilised in the context of larger controls are: the National Police (*Police Grand-ducal*), the Customs and Tax Administration

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<sup>231</sup> L'essentiel, *Le travail au noir, une banalité cachée*, 6 February 2013.

<sup>232</sup> Le Quotidien, *Inspection du travail: quel chantier!*, 13 November 2015.

<sup>233</sup> This part refers to desk research conducted by the expert.

<sup>234</sup> Internet:

<http://www.itm.lu/files/live/sites/Itm/files/Itm/Rapports%20Annuels/06.pdf> (p. 34)

<sup>235</sup> Ibidem, p. 35.

(*Administration des douanes et accises*), the National Tax Administration (*Administration de l'enregistrement et des domaines*), the Prosecutor General's Office (*Parquet*), as well as various responsible units from the major ministries (i.e. the unit dealing with health at the workplace within the Health Ministry or the national PES).

In the context of controls related to non-declared work, it can be underlined that the various actors have specific missions and are mobilised for different purposes. Officials mobilised from the Ministry of Health check for instance if employees are in the possession of an occupational certificate (*certificat d'aptitude valide*): they are more broadly in charge of controlling if health standards are met. The potential violation by the employer of the right of establishment is for example controlled by the Tax Administration.

### **2.2.2 Characteristics of the responsible organisations**

As mentioned above, organisations involved in the fight against non-declared work are mobilised for specific controls and according to their missions. The main actor, the ITM, overhauled by law in 2007<sup>236</sup> (with ongoing discussions regarding a new overhaul), operates through its various units under the umbrella of the Ministry of Labour and Employment and whose mission it is to contribute through support to the general well-being of employees and the security of companies. ITM covers all sectors and operates at the national level and based on a legal framework (Art. L. 613-4 of the 2007 law on the reform of the ITM) through three regional branches (Luxembourg, Esch-sur-Alzette, Diekirch) with a total of 92 employees (among which are currently 23 inspectors). Besides a management board and an administration, the National Labour Inspectorate comprises the Labour Inspectorate based on two departments and several units, among which are a 'Help Center' and – more significant for the subject under analysis – a control unit (*Inspections, contrôles and investigations* - ICE). The internal organisation of the various units is defined by grand-ducal legislation. More broadly, non-declared work is one of the many missions to be conducted by ITM, as the administration deals more generally with health and security issues at the workplace.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

Broadly, the cooperation is cross-cutting, inter-ministerial, and pluri-disciplinary. The 2007 law on the reform of the National Labour Inspectorate stipulates under articles L. 613-1 and L. 613-2 the creation of the 'Steering committee of the national labour inspectorate system' (*Comité de coordination du système national d'inspection du monde du travail*) which is in charge of organising the collaboration between the various government agencies and establishing synergies and with the objective to pursue a global vision. The Ministry of Work is not represented in the aforementioned Steering Committee. The Steering committee is composed of the ITM, representatives from the Ministry of Health, the Customs authorities, the National Service in charge of the security in the Civil Sector (*Service national de la sécurité dans la Fonction publique*), and the Insurance associations against accidents (*Association d'assurance contre les accidents*).

No information on data exchange and related exchange protocols exists to the knowledge of the author at the time of writing.

No evidence regarding effectiveness was identified in the research process for this factsheets. A review of press articles reveals that cooperation between the various actors shows some degree of efficiency, but this material should be further studied through

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<sup>236</sup> Loi du 21 décembre 2007 portant réforme de l'Inspection du travail et des mines, Mémorial A, numéro 249, 31 décembre 2007 (Law of 21 December 2007 on the reform of the Labour and Mines Inspectorate, Memorial A, Number 249, 31 December 2007).

qualitative research with the involved administrations in order to get a more thorough overview of cooperation efforts in dealing with non-declared work.

ITM regularly conducts controls with agencies in the neighbouring countries (i.e. Belgium and France) although no specific data exists to the knowledge of the author at the time of writing. Contacts with international agencies such as the French Training Institute for Inspectors (INTEFP) were broadened, and ITM participated in 2014 in the project '*Euro-détachement*' based on the exchange of information and data between countries<sup>237</sup>.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The government has mainly opted for a deterrence approach in the fight against non-declared work. This approach is also identified for other violations of the Labour Code such as the non-payment of the social minimum wage or violations against health standards at the workplace. In the case of non-declared work, articles L.571-5, L.571-5 and L.571-6 stipulate sanctions: if the law is violated, penalties of EUR 251 to a maximum of EUR 5 000 are applied; if violations are repeated within the period of five months after the first violation, an imprisonment period of between eight days and six months (based on documents by the Tax customs) is applied, or double of the maximum penalty applies. Other measures include VAT recovery by the National Tax Authority (*Administration de l'Enregistrement et des domaines*), or the withdrawal of the commercial authorisation is decided by the Department of Small and Medium sized Enterprises of the Ministry of the Economy.

### **2.3.2 Measures to tackle UDW**

As described above, the Labour Code stipulates a series of penalties to be applied in the context of non-declared work. These include fines, imprisonment or the withdrawal of authorisations. More broadly, in terms of policy, research for this factsheet has unveiled that Luxembourg intends to reinforce efforts to tackle undeclared work, and continue its efforts already voiced under the Luxembourg Presidency and in the context of the EU Council decision of March 2016 on establishing a European Platform to tackle undeclared work.

No information on the effectiveness of measures exists to the knowledge of the author at the time of writing.

### **2.3.3 Good practice**

No case of good practice was identified regarding the fight against non-declared work. Nonetheless, available data analysed for this factsheet highlights the strong cooperation between the various administrations and the mobilisation in cases of controls, as well as the embeddedness of non-declared work in the national Labour Code.

### **2.3.4 Challenges and barriers**

Some challenges and barriers are identified in the Clément and Maas study (2010). Two groups of challenges can be identified. The first group of challenges concerns the administrative level and focuses on the training aspect of agents dealing with controls. The improvement of training is a current issue in critical debates around the current ITM reform, especially as the occupational career of an inspector does not exist in Luxembourg<sup>238</sup>. The second group mainly deals with the changing labour market and the inherent challenges therein, such as the emergence of new sectors (ICT, logistics), intricate forms of subcontracting, as well as issues of migration.

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<sup>237</sup> Internet : <http://www.eurodetachement-travail.eu>

<sup>238</sup> For a discussion, see Le Quotidien, *Inspection du travail: quel chantier!*, 13 November 2015.



These challenges are addressed by a plan to further reform the ITM, details of which are not yet available. There seems to be no change announced in the way the Labour Code tackles non-declared work, such as for example an overhaul of penalties.

A key remaining challenge, as far as available data is concerned, deals with training issues within the ITM and the number of staff ready to conduct controls. It also remains to be seen if, as the 2007 study points out, issues such as further efforts in terms of better regulation at the national and municipal level, or subsidies for companies, could lead to a decrease of non-declared work.

## **Factsheet on Undeclared Work – MALTA (July 2016)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

Maltese legislation does not define undeclared work. Government documents (such as the National Reform Programme 2013)<sup>239</sup> which occasionally mention the term, do not provide a definition. On other occasions, wider terms such as black economy, shadow economy, and grey economy are used instead of undeclared work.

Since no legal definition of undeclared work exists, each organisation in Malta with an interest in undeclared work tackles the issue according to its remit.

#### **2.1.2 Characteristics of undeclared work**

Little data exists on the characteristics and scale of undeclared work in Malta.

The information that is available suggests that partially undeclared self-employment is among the most prominent types of undeclared work. Nearly a fourth of the Maltese (23%) are estimated to have purchased goods or services that may have included undeclared work from firms or businesses.<sup>240</sup> Migrants, particularly those from sub-Saharan Africa residing in open centres, are prone to engage in exploitative undeclared employment. Seasonal or part-time employment also attracts a significant number of students in undeclared work, and a proportion of formally inactive women also do undeclared work. A declining number of persons registering as unemployed engage in undeclared work while claiming unemployment benefits.

The main sectors which appear to attract undeclared work are tourism (including hotels and restaurants), services (such as health care and private tuition), sales and construction. Construction appears to attract illegal immigrants and persons registering for employment work. Young people often do undeclared work in the tourism sector. Formally inactive women often engage in household services (e.g. cleaning) and contribute to family businesses.

Undeclared work appears to be more common among small local employers rather than larger international companies. The latter companies have stricter rules of employee engagement and are usually unionised.

While other countries blame the lack of regular jobs as a motivator to take part in undeclared work, only 11% of Maltese persons feel that this is an important factor.<sup>241</sup> On the other hand, 37% of Maltese persons consider the lack of control of authorities as a prime motivating factor.<sup>242</sup> Such a lack in enforcement could promote a trade-off between employer and employee, in which the employee settles for an hourly wage rate below that provided by law, in return for avoiding national insurance contributions and income tax. Customers may also buy undeclared goods and services as they are cheaper.

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<sup>239</sup> Ministry for Finance (2013). Malta's national reform programme under the Europe 2020 strategy. Weblink: [https://mfin.gov.mt/en/home/popular\\_topics/Documents/National%20Reform%20Programme/2013/National%20Reform%20Programme%202013.pdf](https://mfin.gov.mt/en/home/popular_topics/Documents/National%20Reform%20Programme/2013/National%20Reform%20Programme%202013.pdf)

<sup>240</sup> European Commission (2014). Special Eurobarometer 402 – Undeclared work in Europe. Weblink: [http://ec.europa.eu/public\\_opinion/archives/ebs/ebs\\_402\\_en.pdf](http://ec.europa.eu/public_opinion/archives/ebs/ebs_402_en.pdf)

<sup>241</sup> European Commission (2014).

<sup>242</sup> European Commission (2014).

### 2.1.3 Estimated scale of undeclared work

Schneider (2012) estimated Malta's black economy to amount to 25.3% of the GDP in 2012.<sup>243</sup>

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing undeclared work

The national authorities involved consist of the following:

- The Department of Industrial and Employment Relations (DIER) – which mainly deals with the protection of the conditions of employment as stipulated by the Employment and Industrial Relations Act (2002). When persons are found to be involved in undeclared work, they are reported to the relevant authority for further action.
- The Employment and Training Corporation (ETC) through its Law Compliance Unit (LCU), which investigates infringements as laid down in the Employment and Training Services Act (1990) and in the Manpower Records (Commencement or Termination of Employment) Regulations (1993). The LCU aims to curb abuses involving undeclared work.<sup>244</sup>
- The Ministry for the Family and Social Solidarity (MFSS), through its Benefit Fraud and Investigation Department (BFID), investigates reports of alleged abuse in social security benefits and investigates social benefit abuse, including that relating to unemployment.<sup>245</sup>
- The Department of Social Security (DSS), which falls under the remit of the MFSS, takes action in cases referred by the BFID involving potential social security fraud.
- The Tax Compliance Unit (TCU), a semi-autonomous unit within the Ministry for Finance (MFIN), addresses tax evasion and tax fraud through detailed tax audits. Among others, it carries out tax inspections and helps to enforce revenue collection.
- The Inland Revenue Department forms part of the MFIN, and has the remit to carry out audits in relation to the Income Tax Act (1949).
- The Vat Department falls under the remit of the MFIN and is in charge of auditing infringements as laid down in the Value Added Tax Act (1999).
- The Malta Police Force (MFP) carries out various activities related to the identification and tackling of UDW. Its Economic Crimes Unit investigates cases of fraud, misappropriation, custom-related cases and money laundering among others. In 2014 the MFP had an overall staffing complement of 1,916 employees,<sup>246</sup> with the Economic Crimes Unit consisting of 34 employees.<sup>247</sup>

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<sup>243</sup> Schneider, F. (2012). Size and development of the shadow economy of 31 European and 5 other OECD countries from 2003 to 2012: some new facts. Weblink: [http://www.econ.jku.at/members/Schneider/files/publications/2012/ShadEcEurope31\\_March%202012.pdf](http://www.econ.jku.at/members/Schneider/files/publications/2012/ShadEcEurope31_March%202012.pdf)

<sup>244</sup> Employment and Training Corporation (2015). Annual report 2015. Weblink: <https://secure.etc.gov.mt/homedir/temp/ETCAAnnualReport2015.pdf>

<sup>245</sup> Ministry for the Family and Social Solidarity (2014). Annual Report 2014. Weblink: <http://mfss.gov.mt/en/Documents/MFSS%20Annual%20Report%202014.pdf>

<sup>246</sup> Office of the Prime Minister (2014). Annual report of the Office of the Prime Minister. Weblink: <https://www.gov.mt/en/Government/Publications/Documents/Annual%20Reports/2014/OPM%20Annual%20Report%202014.pdf>

<sup>247</sup> Ministry for Home Affairs and National Security (2014). Annual report 2014. Weblink: [https://www.gov.mt/en/Government/Publications/Documents/AnnualReports/2014/MHAS Annual Report 2014.pdf](https://www.gov.mt/en/Government/Publications/Documents/AnnualReports/2014/MHAS%20Annual%20Report%202014.pdf)

## 2.2.2 Characteristics of the responsible organisations

The characteristics of the national authorities with a role in addressing undeclared work are described below:

- The DIER aims to “to protect the interests of parties in employment contracts while actively promoting a healthy employment relationship in a spirit of social partnership, and to contribute towards stable industrial relations”.<sup>248</sup> The department is composed of six branches as follows: Director’s office; International affairs and industrial relations; Enforcement; Termination and legal office; Research and IT; Administration. The DIER operates at a national level and has a staff complement of around 30 employees.
- The ETC is Malta’s public employment service organisation and aims to enhance employability through policies and initiatives targeting job seekers and employers. The organisation has seven divisions: corporate planning, employment services, inclusive employment services, EU funded schemes, training services, finance and corporate services, and the Gozo services. Its law compliance unit deals with: persons who register for employment while working; employers that do not notify the ETC on the engagement of new employees; employers who employ persons of compulsory school age without an authorisation; and employers engaging third country nationals without employment licences. The ETC has a national coverage and employs around 320 persons.<sup>249</sup>
- The BFID, which operates at a national level, aims to tackle social benefits fraud by (a) identifying specific cases or trends in social benefit abuse, (b) investigating reported or suspected cases of abuse, (c) making recommendations that can lead to eliminating or restricting benefit fraud, and (d) acting fairly respecting the social aspect.<sup>250</sup> In 2014 it employed 13 persons (including the Director’s secretariat).<sup>251</sup>
- The DSS administers Social Security Legislation, providing for the payments of benefits both under the contributory and the non-contributory schemes. One of the regulatory functions of the DSS is that of evaluating and deciding on cases brought forward by the BFID. During 2014, the DSS employed 306 persons.<sup>252</sup>
- The TCU collaborates with the investigative and enforcement units of other tax departments (namely the VAT, Inland Revenue and Customs departments) and with the ETC, BFID, DSS and the Police. The TCU also establishes industry benchmarks, and conducts visits at business premises collecting information such as the level of turnover, capital investment, number of employees and business capacity.<sup>253</sup> In 2015 the TCU, which operates at a national level, with 16 staff.<sup>254</sup>
- The IRD deals with the administration of the Income Tax and Capital Transfer Duty Acts and the enforcement of social security contributions, at a national level.

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<sup>248</sup> Department for Industrial and Employment Relations: <https://dier.gov.mt>

<sup>249</sup> Employment and Training Corporation (2015).

<sup>250</sup> Ministry for the Family and Social Solidarity: <http://mfss.gov.mt>

<sup>251</sup> National Audit Office (2014). Performance audit, addressing social benefit fraud.

Weblink: <http://nao.gov.mt/loadfile/84e4bdce-6fc4-4cca-870c-bf2a49588959>

<sup>252</sup> Department for Social Security (2015). Annual report 2014. Weblink: <http://www.socialpolicy.gov.mt/en/Publications/Documents/Annual%20Report%202014.pdf>

<sup>253</sup> Ministry for Finance (2013)

<sup>254</sup> House of Representatives (2015). PQ XII 16619. Weblink:

<http://pq.gov.mt/PQWeb.nsf/7561f7daddf0609ac1257d1800311f18/c1257d2e0046dfa1c1257e5a0044d720!OpenDocument>

- The VAT Department, operating at a national level, employs 72 inspectors.<sup>255</sup> Its enforcement functions include examining business records and accounts in order to certify that registered persons make proper tax declarations. Spot checks are carried out to ensure that clients are being provided with fiscal receipts.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The LCU, the DSS, the BFID, the TCU, the Vat Department and the MFP collaborate with each other on cases involving undeclared work. The DIER instantly informs the ETC whenever cases involving undeclared work, foreign nationals working with expired or without employment licenses or any other relevant information falling within the remit of ETC are uncovered during inspections / investigations. On the other hand, ETC informs the DIER of cases where there are doubts as to employment conditions.

Data exchange between organisations with an interest in UDW seems to be limited, although the ETC has agreed to provide the DIER with access to its databases.

No data on the effectiveness of cooperation on undeclared work between national organisations, and between Malta and other Member States, is currently available.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The policy approach to tackling undeclared work in Malta features the following elements:

- Reducing direct taxation (enabling compliance) – With minimum wage incomes being exempt from income taxes. In recent Budgets, there were measures to reduce the rate of personal income tax, which may encourage persons in undeclared work to regulate their employment status.
- Reducing tax evasion (deterrence) - Since 2015, any type of commercial activity is obliged to register with the VAT Department and file VAT returns, regardless of the amount of sales per year. This amendment obliges commercial activities to declare income, both for VAT and for income tax purposes.<sup>256</sup>
- Active Labour Market Policies (enabling compliance) - In recent years, there has been increased emphasis on active labour market policies. The setting up of an Active Labour Market Counselling and Action Committee in 2013, composed of social partners is a case in point.
- Precarious employment (deterrence) - New mandatory criteria for contractors bidding for government tenders were introduced in 2013. Among others, contractors must provide information about the wages of their employees. A tribunal was set up to exclude employers in breach of employment from the adjudication of government tenders.
- Improving the efficiency of inspections (enabling compliance and deterrence) - In 2015, a White Paper was issued proposing to reform business inspections by: improving policy outcomes; enhancing compliance; carrying out more relevant inspections; and reducing inspections and the related burdens for businesses.<sup>257</sup>

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<sup>255</sup> House of Representatives (2011). PQ XI 28234 Weblink: <http://pq.gov.mt/PQWeb.nsf/7561f7daddf0609ac1257d1800311f18/c1257881003b3b78c125792e002aa98d!OpenDocument>

<sup>256</sup> Ministry for Finance (2014). Budget document 2015. Weblink: [http://mfin.gov.mt/en/The-Budget/Documents/The\\_Budget\\_2015/Budget\\_Doc\\_2015.pdf](http://mfin.gov.mt/en/The-Budget/Documents/The_Budget_2015/Budget_Doc_2015.pdf)

<sup>257</sup> Office of the Prime Minister (2015a). Improving business inspections. Weblink: <https://opm.gov.mt/en/PublicService/Documents/Inspections%20Reform%20Digital.pdf>

Following a public consultation exercise, it was decided to set up a Central Inspection Coordination Unit to co-ordinate and set standards for inspections.<sup>258</sup>

### 2.3.2 Measures to tackle UDW

As mentioned above, income tax has been decreased considerably in recent years, thus encouraging the uptake on formal employment. The government also increased the controls so that precarious employment is eliminated from subcontracting in the public sector. Maltese legislation obliges registered jobseekers to accept employment or training opportunities offered to them, or they will be removed from the employment register. Inspections are carried out by the ETC to identify persons registering as unemployed while at the same time engaging in undeclared work. A free phone service and an online reporting system exist to encourage the public to report undeclared work.<sup>259</sup> As stated earlier, apart from the ETC, other different government entities (such as the DIER and BFID) carry out inspections meant to reduce UDW.

Available data on the effectiveness of measures to address undeclared work are provided below:

- ETC Enforcement – During 2014, 6,528 targeted inspections were undertaken, uncovering 2,488 infringements.<sup>260</sup> In 2014, 552 individuals were removed from the unemployment register, which were mostly Maltese workers found working at establishments without their employer notifying ETC.<sup>261</sup>
- BFID Enforcement - During 2014, the BFID conducted 1,391 on-site inspections. Following investigations 1,022 cases were concluded and resulted in the suspension of a total of 887 social benefits.<sup>262</sup> The estimated annual savings for 2014 totalled € 3,831,983.<sup>263</sup>

### 2.3.3 Good practice

The Community Work Scheme for registered unemployed persons administered by ETC is among others serving as a deterrent against undeclared work. Between 2009 and 2013, 52 persons who refused to participate were removed from the unemployment register, 19 persons lapsed from registration and 47 persons declared to have found employment when contacted to participate in the scheme.<sup>264</sup>

### 2.3.4 Challenges and barriers

A main barrier to tackling undeclared work is the lack of effective enforcement, mostly due to disjointed inspectorate/ enforcement regime and a lack of resources. For instance the National Audit Office remarked about the “strained relationship between BFID and DSS due to divergent views on the administration of social policy”.<sup>265</sup> Fragmentation is also present in revenue earning departments, subjecting tax payers to burdens of

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<sup>258</sup> Office of the Prime Minister (2015b). Government response to public feedback on improving business inspections. Weblink: [https://socialdialogue.gov.mt/en/Public\\_Consultations/OPM/Documents/L-17-2015%20Improving%20Business%20Inspection/Consultation%20Outcome%20Report%20-%20Improving%20Business%20Inspections.pdf](https://socialdialogue.gov.mt/en/Public_Consultations/OPM/Documents/L-17-2015%20Improving%20Business%20Inspection/Consultation%20Outcome%20Report%20-%20Improving%20Business%20Inspections.pdf)

<sup>259</sup> Ministry for Finance (2015). Malta national reform programme. Weblink: [http://ec.europa.eu/europe2020/pdf/csr2015/nrp2015\\_malta\\_annex2\\_en.pdf](http://ec.europa.eu/europe2020/pdf/csr2015/nrp2015_malta_annex2_en.pdf)

<sup>260</sup> Employment and Training Corporation (2014). Annual report 2014. Weblink: [https://secure.etc.gov.mt/homedir/temp/ETC\\_Annual\\_Report\\_2014.pdf](https://secure.etc.gov.mt/homedir/temp/ETC_Annual_Report_2014.pdf) Data is collected regularly on an annual basis.

<sup>261</sup> Ministry for Finance (2015).

<sup>262</sup> Ministry for the Family and Social Solidarity (2014).

<sup>263</sup> Ministry for Finance (2015).

<sup>264</sup> Ministry for Finance (2013).

<sup>265</sup> National Audit Office (2014).

multiple investigations by different departments. Another challenge that needs to be tackled is the engagement of irregular migrants in undeclared work.

These challenges are being addressed in several ways. New inspectors were recently engaged with BFID, VAT and DIER, and there is an ongoing process to amalgamate the revenue earning departments into one authority. The creation of a Central Inspection Coordination Unit (CICU) should enhance coordination and cooperation among the different regulators and inspection regimes. The government announced that it will carry out legal and organisational changes so that the unit will be able to set standards for inspections and carry out its operations. Advisory and consultative bodies are to be set up as to facilitate the development and implementation of the Common Policy Framework.<sup>266</sup> The Budget 2016 includes a proposal for the setting up of an Immigration Work Office for the regularisation of irregular migrants' work.

According to the Minister for Education and Employment, more preventive and curative policies are required. These could include awareness raising campaigns on the consequences of undeclared work targeted at enterprises, workers and the general public.<sup>267</sup>

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<sup>266</sup> Office of the Prime Minister (2015b).

<sup>267</sup> The Malta Independent (29 April, 2015). Minister Helena Dalli addresses EU conference on combating undeclared work. Weblink: <http://www.independent.com.mt/articles/2015-04-29/local-news/Minister-Helena-Dalli-addresses-EU-conference-on-combating-undeclared-work-6736134628>

## Factsheet on Undeclared Work – NETHERLANDS (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

The **Central Bureau for Statistics** (CBS) uses the definition to “work legally as such, but without registration for income tax and social security”. The **Dutch tax authority** describes undeclared work as work that is not reported to the tax authority, usually paid in cash. This definition is also common in the Dutch society where often the payment in cash is associated with undeclared work. **The Labour Inspectorate** and other controlling authorities use the definition of the CBS and make clear differences between undeclared work and criminal activities. Though the definition of the tax authority seems very broad they also make a clear distinction between undeclared work and criminal activities. Money earned through hobbies and for family or friends without profit are most of the times tax-free and do therefore not need declaration. Most common examples given on information websites about undeclared work are those in the sectors of housekeeping, construction, hospitality and agriculture. There is relatively little information available on under-declared work however the tax authority emphasises that employees should be aware of the out of work income that they need to declare to the authorities.

#### 2.1.2 Characteristics of undeclared work

Undeclared work in the Netherlands is most commonly found in the construction, household, agriculture and hospitality services. In the **construction sector** most undeclared work is done during the building or the renewal of a private house. People pay part(s) of the construction in cash because the constructor is willing to work for less when they are not paying taxes. Because of this, jobs like painting or paving are frequently undeclared. There are also concerns of the exploitation of immigrants in the construction sector.<sup>268</sup> To be able to control these exploitations the European inspections should work closer together according to the Minister of Social Affairs and Employment, Mr. Asscher. It was one of his main tasks during the Dutch chairmanship of the European Union in Spring 2016.

In **agriculture** most undeclared work is done by immigrants or young people working during their studies. Students prefer to receive more salary in cash (undeclared) instead of legally where they will have to pay social premiums and other labour costs. However a lot of students are not aware that by working undeclared they are not entitled to an 8% holiday payment and are not insured. There have been some incidents with Eastern-Europe immigrants and third country nationals working for Dutch farms in very poor conditions. In 2009 the police discovered an extreme situation where immigrant workers were working in conditions described as close to slavery on a Dutch farm.<sup>269</sup> In 2015 some Polish workers mentioned that an employer was withholding social premiums from their salaries but did not pay these premiums to the insurance authorities. In the same news item Minister Asscher promised changes in legislation to tackle these problems as

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<sup>268</sup> Cobouw. (2016, February 9). *Aanpak van uitbuiting leeuw of lam (Addressing of exploitation, lion or lamb)*. Internet: <http://www.cobouw.nl/artikel/1617181-aanpak-van-uitbuiting-leeuw-lam>

<sup>269</sup> Trouw. (2010, March 10). *Duistere praktijk achter blanke asperges*. Internet: <http://www.trouw.nl/tr/nl/4324/Nieuws/article/detail/1585611/2010/03/10/Duistere-praktijk-achter-blanke-asperges.dhtml>



more and more stakeholders were addressing their concerns about the working conditions in the agricultural sector.<sup>270</sup> These will be elaborated in section 1.3.

There have been a couple of incidents in the media of undeclared work in the **hospitality sector**. Examples are the exploitations of mostly Asian employees by restaurants<sup>271</sup> and the systematic undeclared work done by cleaning companies in fast-food restaurants<sup>272</sup>. Cleaners claim that they are working 7 nights a week, not all worked hours are compensated and employees are not receiving holiday payments. Besides this cleaners are ordered to wait until the morning for the fast-food personnel to control their cleaning work. These hours are not compensated. These findings were results of a series of inspections carried out on some fast food restaurant's cleaning companies on the basis of rumours of undeclared work. The Inspectorate SZW intensified the workplace inspections in 2016 at fast-food restaurants together with the Dutch tax authority, the UWV (the Employee Insurance Agency), the IND (the Immigration and Naturalisation Service) and municipalities and put pressure on fast-food restaurants to stop hiring malicious cleaning companies. Companies such as fast-food restaurants and hotels are stimulated to use certified cleaning companies or employ cleaning personnel themselves.<sup>273</sup>

In 2012 the Dutch tax authority published a report indicating that almost 20% of all driving schools are suspected of engaging in undeclared work. The tax authority warns that they are going to put more time and effort into this area in order to control potential undeclared work.<sup>274</sup>

Other 'typical' undeclared jobs in the Netherlands are hairdressers, car mechanics and taxis. Work undertaken and not declared in these areas is usually carried out by someone from the customer's network making it difficult to detect and tackle.

Research undertaken by the CBS in 2011 asking people about their experiences and thoughts of undeclared work resulted in an overview of the Dutch informal economy. However, the research is based on a small group of respondents and should therefore be interpreted cautiously.<sup>275</sup> The survey combined internet distributed questionnaires with face-to-face conversations in order to get the most reliable data. The research shows that approximately 9.1% of the total Dutch population between 15-64 years of

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<sup>270</sup> Omroep Brabant. (2015, February 9). *Minister Asscher belooft maatregelen tegen uitbuiting Oost-Europeanen in land- en tuinbouw* (Minister Asscher promises action against exploitation of Eastern Europeans in agriculture). Internet: <http://www.omroepbrabant.nl/?news/224434732/Minister+Asscher+belooft+maatregelen+tegen+uitbuiting+Oost-Europeanen+in+land-+en+tuinbouw.aspx>

<sup>271</sup> Telegraaf. (2010, September 17). *Kok restaurant veroordeeld voor uitbuiting (Chef restaurant sentenced for exploitation)*. Internet: [http://www.telegraaf.nl/binnenland/20344033/\\_\\_Kok\\_restaurant\\_veroordeeld\\_\\_.html](http://www.telegraaf.nl/binnenland/20344033/__Kok_restaurant_veroordeeld__.html), and NOS. (2013, March 18). *Celstraffen voor uitbuiting kok (Prison sentences for exploitation chef)*. Internet: <http://nos.nl/artikel/485949-celstraffen-voor-uitbuiting-kok.html>

<sup>272</sup> Metro. (2016, February 16). *Nog veel mis bij schoonmaakbedrijven in de fastfood (Still a lot of problems at cleaning businesses in fastfood)*. Internet: <http://www.metronieuws.nl/nieuws/binnenland/2016/02/nog-veel-mis-bij-schoonmaakbedrijven-in-de-fastfood>

<sup>273</sup> Jaarverslag 2016 Inspectie SZW (<https://www.inspectieszw.nl/publicaties/jaarverslagen/2017/17/17/jaarverslag-2016>)

<sup>274</sup> AD (2012, November 16). *'Eén op de vijf rijsscholen geeft zwart rijles'* (Undeclared work in one out of five driving schools).. Internet: <http://www.ad.nl/ad/nl/1012/Nederland/article/detail/3348778/2012/11/16/Een-op-de-vijf-rijsscholen-geeft-zwart-rijles.dhtml>

<sup>275</sup> CBS. (2012). *Een onderzoek naar zwartwerk onder uitkeringsgerechtigden en de totale bevolking in 2011* (An investigation into undeclared work among welfare recipients and the total population in 2011). The Hague: Centraal Bureau voor de Statistiek.

age has done undeclared work in 2011. From this portion most of the respondents are between 15-34 years (69%) suggesting that most undeclared work is accounted for by young people. The percentage of undeclared work engaged in by people who receive a benefit is lower than the total (between 2.4% and 5%).

The main motivators found in the survey are money-related or related to the (high) regulation of declared work. Some are motivated solely by the fact that undeclared work has a higher pay-out while others said they need the extra money to be able to pay for basic needs. Also, some people use the money to save for something special. A different report on behalf of the ILO, placed the emphasis on the presence of fraudulent temporary work agencies.<sup>276</sup>

### 2.1.3 Estimated scale of undeclared work

The research of Schneider (2012)<sup>277</sup> estimates the Dutch shadow economy to be 9.8% of GDP making it one of the smallest in Europe (19.2% average). In 2008 around 12,000 temp agencies were registered at the Dutch Chamber of Commerce. It was estimated that between 5,000 and 6,000 of these were contravening the law. In 2012 19,000 agencies were registered of which 11% were members of one of the employers' organisations. This 11% represents 80% of the total sector turnover suggesting that the unregistered organisations are often small. The high number of these agencies is related to the liberation of the market and the increased demand for Eastern and Central European workers. Practices that occurred include: illegal employment, bogus self-employment, non-payment of taxes and fees, underpayment and deductions from salary under the claim of e.g. unlawful costs of administration or disproportionate fines. These agencies are mostly active in sectors where the margins are small and a lot of SMEs are found like agriculture, meat industry, construction, cleaning industry and transport. The Dutch minister of Social Affairs and Employment has acknowledged this problem but says the problem is hard to tackle because of the nature of these organisations which are mostly complex and not registered anywhere, also the financial profits for all parties involved can amount to high numbers.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing undeclared work

On behalf of the International Labour Office, Regioplan<sup>278</sup> has conducted research on the Labour Inspection Strategies for Combating Undeclared Work in Europe with a focus on the Netherlands. This research shows a clear overview of the Dutch organisations responsible for addressing undeclared work.

In the Netherlands there are three main organisations responsible for addressing undeclared work: Inspectorate SZW (Social Affairs and Employment), Tax Authority and the UWV (PES). Other important players are the municipalities, International Fraud Information Bureau (IBF), the Social Insurance Bank (SVB), the Netherlands Bureau for Information Exchange within the Work and Income Sector (BKWI), Labour Unions and Employers' associations.

The **Inspectorate SZW** is the most important authority concerning tackling undeclared work in the Netherlands. As part of the Ministry of Social Affairs and Employment, the focus of the inspectorate is not necessarily on undeclared work as such, but on the broader concept of 'decent' work. This concept includes fair, healthy and safe working conditions and socio-economic security for everyone. Related to undeclared work the inspectorate, in their annual plan, predicts the risks of the occurrence of illegal

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<sup>276</sup> Renooy, P. (2013). *Labour Inspection Strategies for Combating Undeclared Work in Europe: the Netherlands*. Amsterdam: Regioplan.

<sup>277</sup> Schneider, F. (2012). *Size and Development of the Shadow Economy of 31 European and 5 other OECD Countries from 2003 to 2012: Some New Facts* .

<sup>278</sup> Renooy, 2013

employment, underpayment, tax/benefit fraud and bogus employment. Besides these risks the inspectorate also focuses on unsafe working conditions, both physical and mentally.<sup>279</sup> The inspectorate is expecting an increase of 'indecent' work related to the immigration of Eastern-European workers. The inspectorate writes in its multiannual plan 2015-2018 that because of the free access to the Dutch labour market for EU members more Eastern-European workers move (temporarily) to the Netherlands because wages are higher. The inspectorate is concerned that the immigrants are willing to work for less compensation and/or under worse circumstances, as it has noticed in the recent years.<sup>280</sup>

Related to undeclared work, the **Dutch Tax Authority** (*Belastingdienst*) focuses on tax/benefit fraud. They are responsible for the collecting of taxes, and with that the inspection on fiscal, economic and financial fraud. Also they are responsible for income-related benefits for childcare, housing and care. On this aspect undeclared work can cause the offender to receive an unfair (amount of) benefit.

The **UWV** is responsible for, among others, the unemployment benefits and reintegration of job seekers. In this role the UWV is responsible for inspecting the legitimacy of social benefits. If someone decides not to declare their work then they are able to claim benefits like an unemployment benefit as long as the responsible authorities are not aware.

**Municipalities** are responsible for providing recipients with a benefit on minimum level (*bijstand*) and activation towards work. Because municipalities have their own annual budget it is important for them to find fraudulent benefit receivers in order to decrease costs.

In collaboration with the Inspectorate SZW, the **Social Insurance Bank** (SVB) ensures that benefits being received are being done so lawfully. The bank is responsible for social insurance schemes like the General Old Age Pensions Act, General Surviving Relatives Act and the General Child Benefit Act and therefore also for the verification of the compliance with the rules.

Besides the governmental institutes the **Labour Unions** and **Employers' Associations** try to address undeclared work because of the possible exploitation of employees and the unfair competition on the market via the insertion of strict rules in the Collective Labour Agreements (CAOs).

### 2.2.2 The characteristics of the responsible organisations

This topic is covered in section 1.2.1 above. The Labour Inspectorate of Ministry, the Dutch Tax Authority and the UWV have a national coverage. All these organisations have an internal organisational structure that is generally recognised in many public bureaucracies, with a division of staff and line positions. As a general rule, these organisations are well staffed, and the author knows of no effective public debate occurring regarding their 'staff to works'-ratio etc. When the current government entered office, some additional resources were devoted to strengthening the Labour Inspectorate.

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<sup>279</sup> <https://www.inspectieszw.nl/publicaties/jaarplannen/2016/jaarplan-2017/jaarplan-2017/jaarplan-2017>

Internet: <http://www.nu.nl/voorpagina/3403723/aantal-zwartwerkers-onveranderd-10-procent.html>

<sup>280</sup> Inspectie SZW. (2014). *Meerjarenplan 2015-2018 (Multi-annual plan 2015-2018)*. Utrecht: Ministry of Social Affairs and Employment.

### 2.2.3 Cooperation and collaboration between authorities and cross-border authorities

To enhance the cooperation of the different organisations the Netherlands has created the Bureau for Information Exchange within the Work and Income Sector (**BKWI**). "BKWI aims to facilitate cooperation between municipal authorities, UWV and the SVB, and other organisations which are responsible for work and income. BKWI provides solutions for efficient and reliable information exchange between these organisations. Therefore, BKWI manages the combined register Suwinet with personal data from (among others) the municipalities, registers of the Tax Authority and social security registers. The appropriate use and privacy protection of these data are safeguarded by means of participation protocols, strict authorisations and rules regarding conduct."<sup>281</sup> Although the network is effective there are concerns for the privacy. The Inspectorate SZW has found that multiple municipals were neglecting the rules concerning the privacy within the system. After taking a sample the results were so poor that the inspectorate decided to inspect all municipals. They have already noticed that the biggest municipal, Amsterdam, has neglected the safety of privacy on a great scale.<sup>282</sup>

Part of the department Enforcement of the UWV is the **International Fraud Information Bureau (IBF)**. The bureau focuses on the international exchange of data and prevention and detection of abuse of benefits outside the Netherlands. The data from IBF is also used by municipals for national and international data. The Ministry of Social Affairs and Employment has appointed the IBF as the coordination spot for cross border exchange of fraud-information. Besides the UWV, municipals, SVB and social security organisations in other countries can make use of the services of the IBF as well. Principals can request information for control and verification on a person's right to a benefit. Sometimes the IBF independently conducts research by asking for data from foreign organisations and sometimes the research is conducted by an embassy through the Ministry of Foreign Affairs.

## 2.3 Policy Focus and Measures

### 2.3.1 Policy approach

The policy of the Dutch government on tackling undeclared work is written down in the Fraud bill (Fraudewet) and has been developed in 2013 with fiercer penalties and more possibilities for the inspectorate to control. This shows that the government is taking undeclared work more seriously. This is needed because with the opening of the border for all EU members (especially Eastern and Central European countries) the occurrence of undeclared work has increased. The difference between this type of undeclared work and the type that was already present in the Netherlands is substantial. The undeclared work engaged in by Dutch citizens was often family related or people working to earn a little bit extra on top of their net salary. With the flow of labour immigrants to the Netherlands other, more serious, problems arise. Bogus temporary labour agencies have been on the rise offering jobs for immigrants in the Netherlands for less than the minimum wage to earn extra profit themselves. These practices do not only effect incomes and taxes but also the working/living conditions which are often poor. In order to address this specific problem the government has introduced the bill Bogus Constructions (Wet Schijnconstructies). With this Act the Minister of Social Affairs and Employment, Mr. Asscher, wants to tackle all kinds of bogus labour relations misusing the law to lower labour costs which can result in lowering social security and compensation to workers. It is difficult to tackle this problem, however, as many people

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<sup>281</sup> Renooy, 2013

<sup>282</sup> Het Parool. (2016, March 9). *Belofte: Snel veiliger opslag data Amsterdammers (Promise: Fast safer storage for data of people from Amsterdam)*. Internet: <http://www.parool.nl/amsterdam/belofte-snel-veiliger-opslag-data-amsterdammers~a4259990/>

are willing to accept substandard working conditions if it means they will not be unemployed. The effectiveness of the new bill still has to be proven because it has only recently been implemented.

### **2.3.2 Measures to tackle UDW**

The most important measures are taken by the inspectorate SZW and the tax authority. Based on risk analyses the organisations are able to pinpoint high-risk companies and they will inspect them on compliance with regulations. The tax authority however has no authority to enter private buildings so they are only able to find fraudulent cases by comparing their data and trying to find missing or ambiguous cash flows that can indicate fraud. The focus of the government lies with big cases and not necessary with the smaller cases like underdeclared work as these are harder to prove and have less impact on the economy and society. Also some undeclared work is permitted, for example, work for family and friends or as a hobby, within certain profit margins. Also, paid house chores like cleaning, cooking or gardening are permitted for three days a week at most.

### **2.3.3 Good practice**

As undeclared work never has been a substantial problem in the Netherlands there have not been a lot of extensive measures. CBS research has shown that the level of undeclared work has remained stable for the past 25 years, however because of the changes in the economy and society it can be stated that the situation has improved. Also, there has been a decrease in the portion of people doing undeclared work while receiving a benefit. This is proof of the success of the more thorough controls of the inspections.<sup>283</sup> The problem now moves to Eastern and Central European Immigrants and whether or not the Dutch government is able to handle this problem can only be known in the future.

### **2.3.4 Challenges and barriers**

The Dutch government is aware of the changing nature of the economy. It is commonly known that tax-payers sometimes evade tax-contributions, but the size of non- and under-declaration seems to be relatively moderate in the Netherlands in comparison with other EU-countries. Digitalisation of tax payments is likely to help in this process. The current key challenge of the Dutch government is to control the labour conditions of the labour immigrants as mentioned before. Sometimes migrants are not registered in the Netherlands, which makes it difficult to control their economic contribution. They appear to be willing to work for lower wages because the minimum wage in their own country is usually even lower. Also, ambiguous temporary labour agencies are taking advantage of the fragile situation of immigrants. It is believed that these organisations try to make the immigrant dependent upon the agency with, for example, a high commission or high housing prices. It has been suggested that in this way the immigrants are unable to stop working and to continue working longer days. To address this problem the government already implemented new regulation, however, it is felt that it needs to address this problem with even greater focus.

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<sup>283</sup> nu.nl. (2013, April 22). *Aantal zwartwerkers onveranderd op 10 procent (Number of undeclared workers unchanged at 10 percent)*.

## Factsheet on Undeclared Work – POLAND (July 2016)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

There is no single and official definition of undeclared work in Poland. However, there are two definitions of undeclared work that are widely used in Poland. The first definition is the one of 'illegal employment' laid down in article 2 of the Act of employment promotion and labour market institutions<sup>284</sup>. The Act defines 'illegal employment or other illegal paid job' as:

- Employment of a person without a written confirmation of the reached agreement and its conditions within required time,
- Failing to register the employed person, or other person performing a paid job, in social security,
- Taking up by an unemployed person employment or other paid job or activity without reporting to district labour office,
- 'Illegal employment of a foreigner', as carrying out work by a foreigner or illegally entrusting work to a foreigner<sup>285</sup>, who is not entitled to work in the understanding of article 87 item 1 or does not have a work permit, is not exempt from the obligation to have a work permit, or whose residency basis does not entitle him/ her to work, or who carries out work on other conditions or post than indicated in the work permit or who carries out work on other conditions or post than indicated in the temporary residency permit<sup>286</sup>.

This formal definition is widely used by organisations with an interest in undeclared work in Poland and institutions entitled to control the legality of employment (e.g. National Labour Inspectorate, local labour offices, Social Security Institution, tax inspection offices).

The second of the definitions has been elaborated by the Central Statistical Office for statistical purposes in their methodological approach to the measurement of this phenomenon<sup>287</sup>. For the description of UDW, the CSO uses the term 'unregistered employment', which, apart from the contract requirement, broadens the definition to any relationship (also in private households and in private farms), lack of social insurance and Labour Fund contributions and income taxes, as well as including unregistered self-employment<sup>288</sup>.

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<sup>284</sup> Act of 20 April 2004 on employment promotion and labour market institutions (Journal of Laws of 2004, No 99, item 1001, with amendments).

<sup>285</sup> Art. 2, par. 1, item 22a of the Act on employment promotion and labour market institutions.

<sup>286</sup> Subject to article 119 and 135 item 3 of the Act on Foreigners of 12 December 2013

<sup>287</sup> *Zasady metodyczne statystyki rynku pracy i wynagrodzeń* [The methodological principles of statistics of labour market and salaries], Central Statistical Office, Warszawa 2008 Internet:

[http://stat.gov.pl/cps/rde/xbcr/gus/Zasady\\_metodyczne\\_stat\\_ryнку\\_pracy\\_i\\_wynagrodzen.pdf](http://stat.gov.pl/cps/rde/xbcr/gus/Zasady_metodyczne_stat_ryнку_pracy_i_wynagrodzen.pdf)

<sup>288</sup> See for example: *Praca nierejestrowana w Polsce w 2014 r.* (Unregistered employment in Poland in 2014), Statistical information and elaborations, Central Statistical Office, Warsaw 2015.

### 2.1.2 Characteristics of undeclared work

A recent study<sup>289</sup> of UDW by the Central Statistical Office revealed that: (1) people employed in the hidden economy comprise more men (71.6 %), than women (28.4%); (2) unregistered work is performed by persons at different ages, from youth to persons at the retirement age. The highest share of the employed in the hidden economy constitutes persons aged 45-59 years (27.0 %); (3) in the structure of the employed in the hidden economy, workers with an education level no higher than basic vocational education are dominant – 57.8 %, while persons with at least secondary education comprise 42.2 %.

The National Labour Inspectorate's audits most often reveal the following irregularities<sup>290</sup>: (1) employment without a written employment contract and without social security registration or not complying with the dates for fulfilling those duties ('the first day' syndrome<sup>291</sup>); (2) registered unemployed persons, who fail to inform the local labour offices of their employment – registration in the registry of unemployed persons entitles to health insurance and state health service – thus can be attractive for persons carrying out undeclared work; (3) lowering the amount of official wages in employment contracts and, paying higher compensations than declared (wages set at the minimum wage level, and the remaining part is paid unofficially), (4) declaring part time employment in an employment contract, whereas in reality the employed person works additional hours outside the official registry (lowering social insurance fees and personal income tax), (5) hiding overtime hours (and paying for overtime 'under the table'); (6) hiding some parts of compensation: bonuses, awards and benefits paid outside the official mode, without obligatory tax and fees. In many cases one can observe 'falsely declared work', for example by signing the civil-law contract (on which the social security contributions do not need to be paid) where the conditions of work agreement are met or temporary work contract where the relationship is evidently long lasting.

The CSO study<sup>292</sup> indicates that **gardening and farming** were the most common types of work performed in the hidden economy (22.2 % of UDW), followed by **construction and installation maintenance and repair** (13.5 %) as well as **construction and installation services** (14.5 %). Other significant areas of UDW comprise: neighbourhood services (9.8 %), taking care of a child or elderly person (5.6 %), manufacturing (3.5 %) and trade (3.9 %). The most commonly performed jobs by both men and women were gardening and farming. The next most common jobs for men were construction and installation services and construction and installation maintenance and repair, while women took care of children or elderly persons or provided neighbourhood services.

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<sup>289</sup> *Praca nierejestrowana w Polsce w 2014 r.* (Unregistered employment in Poland in 2014), Statistical information and elaborations, Central Statistical Office, Warsaw 2015.

<sup>290</sup> *Ocena skali zjawiska zawierania umów cywilnoprawnych i zatrudnienie w szarej strefie* [Assessment of the scale of concluding civil-law agreements and employment in grey economy], General Labour Inspectorate, Warsaw, February 2016. Internet: ([http://rop.sejm.gov.pl/1\\_Old/opracowania/pdf/material91.pdf](http://rop.sejm.gov.pl/1_Old/opracowania/pdf/material91.pdf)).

<sup>291</sup> Currently, the Labour Code requires the signing of the labour agreement until the end of the first day of work. Therefore some employers, who use UDW, while controlled claim to have just employed the person, and deliver the signed contract at the end of the day of control (which they claim to be the first day of work).

<sup>292</sup> *Praca nierejestrowana w Polsce w 2014 r.* (Unregistered employment in Poland in 2014), Statistical information and elaborations, Central Statistical Office, Warsaw 2015.

The CSO survey<sup>293</sup> indicates that the main group of employers for whom UDW is performed is constituted by natural persons (households) (68.9 % of UDW incidences). Among the formal employers offering unregistered work, 26.5 % were private companies. Only a minority of those employed in the hidden economy (2.5 %) were self-employed. The analysis of the CSO survey results<sup>294</sup> indicates that according to the respondents, the main reasons for taking up UDW are: inability to find a formal job (58.8%) and difficult material situation (insufficient income) (39.6 %). Other reasons include: the higher pay without formal employment contract proposed by the employer (24.6 %), high insurance rate (20.5 %), and taxes discouraging from declaration of income (13.2 %). According to Human Capital Balance research carried out throughout 2010-2014<sup>295</sup>, key causes for not concluding a formal employment agreement are as follows: unwillingness of the other side to conclude an employment agreement (40 %), treating undeclared work as additional or temporary work (30 %), working mainly for family/ friends (19 %) and too high taxes and fees (18 %).

### **2.1.3 Estimated scale of undeclared work**

Analysis of the scale of undeclared work has been performed by the CSO on the basis of the special module to LFS survey in the years 1995, 1998, 2004, 2009, 2010 and 2014. The survey on unregistered employment carried out in 2014 indicated that the scale of the phenomenon is still significant, despite a slight decrease – as compared to the results of the previous surveys – in the percentage share of people employed in the hidden economy in the entire working population. In the period between January and September of 2014, unregistered work was performed by 711 000 people, i.e. 4.5 % of the total number of the employed (as compared to 2010: 732 000 / 4.6 %; 2009: 785 000 / 4.9 %; 2004: 1 317 000 / 9.6 %; 1998: 1 431 000 / 9.3 %; 1995: 2 199 000 / 14.9%). In 2014, unregistered employment constituted the main job for 396 000, i.e. for 55.7 % of the total number of the illegally employed. Also the study of Human Capital Balance estimated the scale of UDW to reach 974 000 people (4.0 % of the population) in 2014 (as compared to: 937 000 / 3.8 % in 2013; 932 000 / 3.8 % in 2012; 1 006 000 / 4.1 % in 2011; 1 210 000 / 4.7 % in 2010). Therefore one can assume that the estimates of CSO are slightly underestimated. National Labour Inspectorate on the basis of conducted controls estimates the number of illegally employed in 2015 at 600 000 workers<sup>296</sup>.

The scale of UDW as a share of GDP is difficult to estimate. First of all the estimates of the shadow economy as % of GDP are differentiated, depending on the source and methodology used. The CSO<sup>297</sup> estimates the shadow economy at 13.7 % of GDP in 2013 (13.2 % in 2012; 11.4 % in 2011; 11.9 % in 2010). At the same time the share of UDW in GDP is estimated by the CSO at 3.9 % in 2013 (3.7 % in 2012; 3.5 % in 2011; 3.3 % in 2010) – so it constitutes around one third of the shadow economy<sup>298</sup>. These

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<sup>293</sup> *Praca nierejestrowana w Polsce w 2014 r.* (Unregistered employment in Poland in 2014), Statistical information and elaborations, Central Statistical Office, Warsaw 2015.

<sup>294</sup> *Praca nierejestrowana w Polsce w 2014 r.* [Unregistered employment in Poland in 2014], Statistical information and elaborations, Central Statistical Office, Warsaw 2015.

<sup>295</sup> Bilans Kapitału Ludzkiego [Human Capital Balance], Internet: [www.bkl.parp.gov.pl](http://www.bkl.parp.gov.pl)

<sup>296</sup> *Skutki dla budżetu państwa zastępowania umów o pracę umowami cywilnoprawnymi i zatrudniania w szarej strefie* [The effects for the state budget of replacing employment contracts with civil-law contracts and shadow economy work], National Labour Inspectorate, Warszawa, kwiecień 2016 r.

<sup>297</sup> *National accounts by institutional sectors and sub-sectors 2010-2013*, Central Statistical Office, Warsaw, August 2015.

<sup>298</sup> Pasternak-Malicka M., *Zatrudnienie nierejestrowane w kontekście problematyki bezrobocia w Polsce* [Unregistered employment in the context of unemployment



calculations are often regarded as underestimated. Other available national estimates<sup>299</sup> indicate that the scale of the shadow economy oscillates around 20 % (19.5 % in 2014; 19.9 % in 2013; 21.1 % in 2012; 20.0 % in 2011; 21.0 % in 2010). Also the analyses of the shadow economy with the use of indirect methods prepared under the project initiated by Ministry of Labour in 2008 indicated roughly similar results (demand for electricity – 22.1 %; demand for money – 22.8 %). From a comparative perspective, Schneider et al.<sup>300</sup> estimates the informal economy in Poland at 23.8 % in 2013 and at 23.5 % in 2014. This suggests that the scale of the shadow economy in Poland might be two times larger than official CSO statistics. If the rough estimate of the share of UDW in the shadow economy (one third) are correct, the share of the UDW in GDP would be as much as 7-8 %.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing Undeclared Work

During the past 20 years, the control of the legality of employment in Poland underwent significant changes, especially within the institutional framework. From 1995 to 1999 the control of legality of employment was conducted by voivodeship labour offices, in 2000-2001 district governments, and further on (2001-2007) Legality of Employment Control of Voivodeship Office became the responsible organs. The **National Labour Inspectorate** has played a controlling function since 1 July 2007 on the basis of the Act of 13 July 2007 on the National Labour Inspectorate (Journal of Laws of 2007, Nr 89, item 589). The National Labour Inspectorate is governed by the Sejm of the Republic of Poland. It is supervised by the Labour Protection Council<sup>301</sup>, established by the Sejm Marshal. Controls of the legality of employment and other paid work are carried out by specialised *employment legality sections* functioning in Regional Labour Inspectorates.

The National Labour Inspectorate cooperates with a number of institutions interested in particular aspects of counteracting undeclared work and its results. Cooperation with **Public Employment Services** and state administration - **Police, Border Guards, Tax Offices** and **Social Insurance Institution**, and **local governments** is of particular importance. The control of the legality of **employment of foreigners**, which is an obligation of the National Labour Inspectorate (since 1 July 2007) and Border Guard (since 1 January 2009), is a special case of sharing competences between two institutions.

### 2.2.2 Characteristics of the responsible organisations

The organisational structure of the National Labour Inspectorate is as follows: the General Labour Inspectorate, 16 regional labour inspectorates with 42 functioning departments, and the National Labour Inspectorate Training Centre in Wrocław. On 31 December 2014, 2 751 persons were employed in the Inspectorate, including 1 572 persons employed as inspectors, including around 130 at local units dealing directly with legality of employment issues<sup>302</sup>. Legality of employment controls carried out by the

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problems in Poland], *Studia BAS*, Nr 4(36) 2013, s.27-56.

<sup>299</sup> Łapiński K., Peterlik M., Wyżnikiewicz B., *Szara strefa w polskiej gospodarce* [The gray zone in Polish economy], IBnGR, Warszawa 2014.

<sup>300</sup> Schneider F., Raczkowski K., Mróz B. (2015), *Shadow economy and tax evasion in the EU*, *Journal of Money Laundering Control*, Vol. 18 Iss 1, pp. 42.

<sup>301</sup> The Labour Protection Council is an organ of authority over working conditions and the activity of the National Labour Inspectorate. The Council is established by the Sejm Marshal and it is appointed for the term of four years (<http://rop.sejm.gov.pl>)

<sup>302</sup> The report on the activities of the National Labour Inspectorate in 2014 (*Sprawozdanie z działalności Państwowej Inspekcji Pracy w 2014 r.*), General Labour Inspectorate, Warsaw 2015.

National Labour Inspectorate are carried out based on an annual work programme, complying with an accepted plan of action. Additionally, ad-hoc measures are carried out in the form of organised seasonal actions. Another kind of action is intervention controls, carried out in response to complaints and referrals filed to the National Labour Inspectorate.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The rules of cooperation of particular services within the framework of controls of legality of employment are set out within the framework of sharing competences defined by law. The regulations are often specified by bilateral agreements between particular institutions<sup>303</sup>. The National Labour Inspectorate can also conduct controls on behalf of a cooperating institution. In 2014 there were 1 084 such controls, of which the most usual requests were from: the tax offices (513 controls), district labour offices (226), Social Insurance Institution (156) and the Police (126).

According to the reports of the Inspectorate<sup>304</sup>, cooperation between the National Labour Inspectorate and the regional **Social Insurance Institutions** has been systematically improving. Labour inspectors and Social Insurance Institution employees take part in meetings, conferences and joint trainings on labour law and social security. Moreover, cooperation between **district labour offices** (carrying out controls and explanatory actions on behalf of the National Labour Inspectorate, verification of personal data of employees as far as the obligation to inform the labour office on taking up employment, other paid work or starting activity is concerned, common prevention and information actions) is also positive. Cooperation with the **Police** (both controls by the National Labour Inspectorate with Police assisting and on behalf of the Police) is also assessed positively<sup>305</sup>.

However, cooperation is not always that effective and is hampered by many barriers. Between 2010 and 2012 there was no improvement in cooperation between National Labour Inspectorate and tax offices. The report<sup>306</sup> emphasises that the cooperation of labour inspectors and tax control offices, and tax offices is limited to informing on the breach of the tax law found during the control. Despite requests for feedback directed to tax organs, the Inspectorate is not being informed on the method of examining the information sent and on the resulting actions of tax offices. The **imperfect system of exchange of information**<sup>307</sup> has been the key barrier for many years. Labour inspectors do not have full and direct (online) access to databases and registries, like

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<sup>303</sup> Example: Agreement between General Labour Inspector and the Chief Commandant of the Border Guard of 12 May 2015 on the rules of cooperation on National Labour Inspectorate and Border Guard; Agreement of 5 November 2010 between General Labour Inspectorate and the president of Social Insurance Institution on the cooperation of National Labour Inspectorate and Social Insurance Institution.

<sup>304</sup> Report on National Labour Inspectorate operation 2007-2014. Internet: <http://www.bip.pip.gov.pl/pl/bip/sprawozdania>.

<sup>305</sup> It increases safety for controllers and enables immediate verification of personal data of workers as well as allows for operational actions by the Police, which are not allowed for labour inspectors.

<sup>306</sup> Checks legality of employment, including employment of foreigners (*Kontrola legalności zatrudnienia, w tym zatrudnienia obcokrajowców*), General Labour Inspectorate, Warsaw, May 2013 Internet: [http://rop.sejm.gov.pl/1\\_Old/opracowania/pdf/material64.pdf](http://rop.sejm.gov.pl/1_Old/opracowania/pdf/material64.pdf).

<sup>307</sup> The problems with coordination of works aiming at the limitation of undeclared work (among others: lack of central data base, dispersion and partial character of gathered data) were identified in analyses made in 2007 commissioned by the Ministry of Labour and Social Affairs. Not all the problems have been solved yet.

the personal identification system (PESEL) and data of the Social Insurance Institution – as far as the social insurance security registry and labour fund fees arrears are concerned, as well as the data of district labour offices – concerning persons in the registry of the unemployed (Syriusz system)<sup>308</sup>. Currently, the employees of the National Labour Inspectorate can use current data from databases on written request.

The National Labour Inspectorate cooperates actively in the work of international bodies such as SLIC. In 2014 under the Programme of Exchange of Labour Inspectors organised by SLIC and financed by the European Commission, the delegates of the National Labour Inspectorate have taken part in study visits in Finland, Sweden, France and the Netherlands.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Deterrence is dominant in the policy approach to combating UDW in Poland. The Labour Inspectorate is equipped with a number of measures (described below) to detect and punish the non-compliance with registering of work. Also, recent policy changes initiated by the new government are focused on the strengthening of detection and punishment of illegal practices. For example, the new amendment to the Labour Code<sup>309</sup> aims at the introduction of the obligation to confirm in writing the conditions of work related to the conclusion of an employment contract before allowing the employee to work (and not as before – no later than at the end of the first day of work). It is aimed at “increasing the protection of workers’ rights and prevention of illegal employment” by giving the National Labour Inspectorate “more effective tools to ensure the effectiveness of controls in the field of legal employment”. This amendment will lead to improving detection of the undeclared work during the inspections, as the work on the basis of the civil-law agreements where employment contracts should be signed might be contested by labour inspectors<sup>310</sup>.

Some of the elements of the existing and planned policy can be categorised as enabling (preventive) measures. The first of such policies regards the existing lowered amount of the social security contributions for the first business start-up for the first two years of performing economic activity. Such a measure effectively discourages UDW self-employment (at least in terms of the formal registration – not in hiding part of the income) and makes it easier to run companies in the first period. Another action is the announced intention of raising the tax-free amount up to 8 000 PLN, which would possibly affect the employee-initiated UDW, especially for low-paid workers.

One of the measures that can be considered ‘curative’ is the introduction (from 1 October 2011) of the possibility to easily register a childcare assistant working in the family home (i.e. nanny) to social security on the basis of the Act of 4 February 2011 on the care for children under three years of age. On the basis of the simple civil-law agreement the parents (who are formally the contribution payers) register the nanny in the Social Insurance Institution. What is important (and encouraging), is that the Social insurance contributions (pension, disability and accident insurance) and health insurance for the nanny who earns no more than the minimum wage are covered by the Social Insurance Institution from the state budget.

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<sup>308</sup> *Ocena skali zjawiska zawierania umów cywilnoprawnych i zatrudnienie w szarej strefie* [Assessment of the scale of concluding civil-law agreements and employment in grey economy], General Labour Inspectorate, Warsaw, February 2016.

Internet: [http://rop.sejm.gov.pl/1\\_0ld/opracowania/pdf/material91.pdf](http://rop.sejm.gov.pl/1_0ld/opracowania/pdf/material91.pdf).

<sup>309</sup> Project of an Act on the amendment of the Labour Code (project submitted to the Marshall of the Sejm on 4th March 2016).

<sup>310</sup> Labour inspectors have the right to start legal (court) action to establish the existence of an employment relationship, even without the consent of the employee, or to join the already ongoing proceedings - with party rights.

Apart from these actions, the National Labour Inspection undertakes a number of so-called 'preventive actions', which should in fact be categorised as actions fostering commitment, as they focus on awareness-raising campaigns (e.g. the 'Before you undertake work' campaign; 'On the wave of first work' campaign; 'Learn your rights at work' competition).

### **2.3.2 Measures to tackle UDW**

In the case of breach of duty to prepare a written contract or failure to confirm in writing the kind of contract and its conditions - not later than the first day of work of the employee - which was recorded during the legality of employment control, the employer can be charged with a **fine**. The labour inspector is also entitled to resign from giving a fine and submit a motion to court. In the case of not registering the employee in social security the labour inspector directs such information to the Social Insurance Institution, which starts adequate fine procedures<sup>311</sup>. The labour inspector is also obliged to inform other relevant institutions, including tax control, of infringements found in the course of the control. The employee who is employed illegally can also be punished in the course of a control, when he/ she was registered as unemployed and did not inform the relevant district labour office on taking up employment within seven days<sup>312</sup>. Separate penalties are provided during the legality of employment controls carried out by the Border Guard and National Labour Inspectorate, both to employer and a foreigner<sup>313</sup>. In 2014, as a result of legality of employment controls, labour inspectors fined 1 253 persons, amounting to PLN 1.5 million (352 900 EUR) in total and submitted 2 050 motions for punishment to courts. On the basis of findings from the legality of employment controls, labour inspectors submitted 138 referrals of suspected criminal offences.

### **2.3.3 Good practice**

There is little evidence on good practice examples in tackling UDW in Poland. In terms of the 'curative' actions, one could consider the possibility to register a childcare assistant with the social security institution (as described in point 1.3.1) as this brought about increased protection of this significant group of workers, the majority of whom were previously employed in UDW.

In terms of the other actions, the promotional campaigns of the National Labour Inspectorate could be considered. One of such examples is the 'Before you undertake work' (Zanim podejmiesz pracę) campaign. The campaign aims to disseminate knowledge about labour law among workers, students and employers. The campaign comprised activities such as telephone duty of inspectors (inspectors were available to take calls from the public and respond to questions on issues of labour law, etc), radio broadcasts, and information on web portals. In 2014, two editions of the campaign were organised<sup>314</sup>. Also EU funded projects aimed at legality of employment of foreigners, in cooperation with International Organisation for Migration and Ministry of Internal Affairs have been undertaken (e.g. 'Migrants' rights in practice /'Prawa migrantów w praktyce'; 'Migrant Info'), including operation of the helpline with information on legal employment in Poland.

### **2.3.4 Challenges and barriers**

One of the biggest challenges is the economic character of UDW, which is hard to change without significant improvement of the labour market conditions, along with reducing key barriers of legal employment – which are high social security contributions and other

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<sup>311</sup> Article 98 item 1 point 1 and 2 of the act of 13 October on Social Security System.

<sup>312</sup> Article 119 item 2 of the Act on the Promotion of Employment and Labour Market Institutions

<sup>313</sup> Act of 20 April 2004 on employment promotion and labour market institutions (Journal of Laws of 2004, No 99, item 1001, with amendments).

<sup>314</sup> Internet: [www.prawawpracy.pl](http://www.prawawpracy.pl).

non-wage costs, bureaucracy and administrative procedures. As noted above, a large part of UDW takes place in households / is provided on behalf of individuals. The high (but lowering) level of social acceptance of UDW, especially performed for households, makes penalising measures ineffective in combating this kind of UDW. Also, lack of understanding of the consequences of UDW for both worker and the employer plays significant role. The changes stipulated as the result of the project initiated by the Ministry of Labour in 2007 still remain valid<sup>315</sup>, including: (1) introduction of the financial incentives that would diminish the motivation of the employees to undertake undeclared work (e.g. diminishing the tax wedge, tax burden and social security contributions), (2) liquidation of administrative burden (e.g. simplifying procedures of employment, cooperation with the labour market institutions); (3) increasing coordination of actions among public institutions (e.g. through sharing of information), (4) introduction of individual help to unregistered employees (thus helping them to leave the shadow economy and supporting those at risk of entering UDW), (5) organising preventive informative and educational campaigns.

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<sup>315</sup> The reasons for undeclared work, its scale, nature and social consequences. As part of the orders were carried out simultaneously and independently two research projects: ( 1 ) a draft of the Institute of Labour and Social Affairs ( ILSS ) and the Public Opinion Research Centre ( CBOS ); ( 2 ) the project Center for Social and Economic Research ( CASE ), and Millward Brown SMG / KRC. *(Przyczyny pracy nierejestrowanej, jej skala, charakter i skutki społeczne. W ramach zlecenia prowadzone były równocześnie i niezależnie dwa projekty badawcze: (1) projekt Instytutu Pracy i Spraw Socjalnych (IPiSS) oraz Centrum Badania Opinii Społecznej (CBOS); (2) projekt Centrum Analiz Społeczno-Ekonomicznych (CASE) oraz Millward-Brown SMG/KRC).*

## Factsheet on Undeclared Work – PORTUGAL (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work in Portugal

The Labour Code (Law 7/2009 and its later revisions) does not contain a definition of undeclared work. The Law 107/2009 that approves the procedural regime regarding administrative infraction proceedings in the area of work relations and social security stipulates that the subject of these proceedings are violations of norms of the labour law or laws of the social security (Article 2-1). The law specifies in Article 2-2 that in the case of 'the provision of services in an apparently autonomous form that have [in fact] the characteristic conditions of a work contract [bogus self-employment] and that may cause losses for the worker or for the state', or in the case of non-declaration of a worker for social security purposes, then any of the two competent bodies (Authority for Working Conditions / ACT or Institute of Social Security / ISS) is allowed to initiate the infraction proceedings. The revision of the regime regarding administrative infraction proceedings by Law 63/2013 created a specific procedure for the prosecution of bogus self-employment (Articles 2-3 and 15-A).

The Report of the ACT for 2015<sup>316</sup> presents in its section regarding 'undeclared or irregular work' the following more specific **definition of undeclared work** and names its negative consequences: 'Work that is totally or partially not declared to the Labour and Social Security Administration by companies of the informal sector or belonging to the structured economy and phenomena like the dissimulation of a work contract using figures like bogus self-employment, paid false traineeships or simulated voluntary services ... contribute to social segmentation (by creating groups of workers separated from social security) and to financial insufficiencies of public revenue, being at the same time a grave factor for unfair competition harming companies that follow the rules'.

The definitions of undeclared work given in the above cited legislation and in the ACT-report can be seen as a **common denominator for all organisations with an interest in undeclared work**, but each one of them will focus its approach towards specific aspects related to its core business (Labour Inspection: violation of labour law; Social Security and tax authorities: fraud and evasion).

#### 2.1.2 Characteristics of undeclared work in Portugal

The undeclared work in Portugal can be divided into two **major categories**: fully undeclared work and partly undeclared work (the latter subdivided into two categories: Substatement of remuneration and disguised employment).

The results of the ACT's inspecting activity (2016) demonstrate that in 2015 the most frequent forms of detected irregularities were two forms of undeclared work: the non-declaration of workers (86%) and the dissimulation of work relations (14%).

Dornelas et al.<sup>317</sup> conclude that undeclared work tends to affect in the first place those workers whose jobs are most distant from the 'typical protected employment'. According to the same authors, undeclared work is (also) a component of unpaid work in the formal economy (i.e. unpaid overtime). They point out that in Portugal, in contrast to most other EU-countries, hourly wages paid for undeclared work tend to be higher than wages

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<sup>316</sup> ACT (2016) Atividade de inspeção do trabalho: relatório 2015 / Autoridade para as Condições do Trabalho; Lisboa: ACT, 2016; Internet: [http://www.act.gov.pt/\(pt-PT\)/SobreACT/DocumentosOrientadores/RelatorioActividades/Documents/Relatorio%20Atividade%20Inspetiva%202015.pdf](http://www.act.gov.pt/(pt-PT)/SobreACT/DocumentosOrientadores/RelatorioActividades/Documents/Relatorio%20Atividade%20Inspetiva%202015.pdf)

<sup>317</sup> Dornelas, António (2010), "O trabalho não declarado é invisível?", in Dornelas, António, Luísa Oliveira, Luísa Veloso e Maria das Dores Guerreiro (orgs.), Portugal Invisível, Lisboa, Editora Mundos Sociais, pp. 95-107

for regular work, and that undeclared work occurs mostly in the context of work relations in the formal economy.

The ACT's National Campaign against undeclared work covered all **sectors of the economy**, with a clear priority for (1) construction, (2) hotel and restaurants, (3) retail trade and (4) agriculture and forestry<sup>318</sup>. In its inspecting activity with regard to vulnerable groups, the ACT focused its efforts on the same sectors and in addition on performing arts (p. 121).

In relation to **specific groups**, Dornelas et al<sup>319</sup> identify the unemployed and illegal immigrants as the groups with the highest probability of doing undeclared work (57% and 50%, respectively), followed by self-employed workers (25%) and part-time workers (16%).

No data could be found in relation to the distribution of undeclared work by **employer size**.

Based on the data of the Eurobarometer 2007, Dornelas et al<sup>320</sup> identify the following **motivations for undeclared** work with most mentions: (1) It is not worthwhile to declare a seasonal job (PT: 44%; EU: 23%); (2) Both parties have an advantage (PT: 31%; EU: 47%); (3) Could not get a declared job (PT: 18%; EU: 16%).

### 2.1.3 Estimated scale of undeclared work

At the launch of the ACT's 'National Campaign against undeclared work' in July 2014 the organisers presented the results of a study on the 'Non Registered Economy in Portugal' which is based on macro-economic calculations and which covers (1) the illegal economy, (2) the hidden economy, (3) the informal economy, (4) the production for one's own consumption and (5) production that is only partly hidden due to statistical deficiencies. The aggregate data presented by Gonçalves and Afonso (2014)<sup>321</sup> show a steady growth of the size of the 'Non Registered Economy in Portugal' in relation to the 'official GDP' from 9.23 % in 1970 to 26.74 % in 2012. These data give an outline of the dimension of undeclared work as a factor in the economy and the losses of tax revenue and social security contributions resulting from it.

In the course of this investigation no credible estimates of the scale of undeclared work could be found.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing undeclared work

The **government authorities with responsibilities for combating undeclared work** and the shadow economy are:

- The Authority for Working Conditions (*Autoridade para as Condições do Trabalho / ACT*)
- The Institute of Social Security (*Instituto de Segurança Social / ISS*)
- The Tax and Customs Authority (*Autoridade Tributária / AT*)
- Foreigners and Border Service (*Serviço de Estrangeiros e Fronteiras / SEF*)

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<sup>318</sup> ACT (2016), op. cit

<sup>319</sup> Dornelas, António, et al. (2011) Emprego, Contratação Colectiva de Trabalho e Protecção da Mobilidade Profissional em Portugal, Lisboa / Gabinete de Estratégia e Planeamento (GEP), Ministério do Trabalho e da Solidariedade Social (MTSS); Internet: <http://www.gep.msess.gov.pt/edicoes/outras/ecctpmpp.pdf>

<sup>320</sup> Ibid.

<sup>321</sup> Nuno Gonçalves e Óscar Afonso (2014) Economia Não Registada em Portugal [Powerpoint Presentation at Launch Seminar of ACT's Campaign against UDW on 15.07.2014], Internet: [http://www.act.gov.pt/%28pt-PT%29/Campanhas/Campanhasrealizadas/Trabalho%20N%C3%A3o%20Declarado/Documents/Oscar%20Afonso\\_TND.pdf](http://www.act.gov.pt/%28pt-PT%29/Campanhas/Campanhasrealizadas/Trabalho%20N%C3%A3o%20Declarado/Documents/Oscar%20Afonso_TND.pdf)

The ACT's National Campaign against undeclared work involved three public entities (the High Commissioner for Migrations, the national PES and the Foreigners and Border Service) and the social partners' organisations with representation on the national body for tripartite concertation (four employers' confederations and two trade union confederations).

Due to its **focus on the enforcement of regulations regarding the labour market**, the **ACT** is the institution *par excellence* to deal with undeclared work in the narrow sense of the term. The other entities with responsibilities in the area have by nature different focuses. The ISS is particularly interested in combating 'contributive' evasion (and recovering lost contributions), the AT concentrates its efforts on combating tax evasion and on the recovery of lost tax revenue, and for the ACM the main objective is to assist migrants to integrate into society and labour market, etc.

### 2.2.2 Characteristics of the responsible organisations

The **Authority for Working Conditions (ACT)** has the responsibility to monitor and enforce the compliance with legal norms regarding labour relations and health and safety at the workplace and to promote the prevention of occupational risks<sup>322</sup>. The activity of the ACT covers all sectors of the economy, but for health and safety inspection activities in public administration ACT is now expecting for especial regulation of the Law of Work in Public Functions (Law 35/2014). The fight against undeclared work can be seen as a central part of the core business of the ACT.

The total number of staff of the ACT in 2015 was 804 (2014: 770). The number of labour inspectors has been constantly decreasing from 384 in 2010 to 307 in 2015<sup>323</sup>. The first national budget submitted by the new government elected in November 2015 (for the budget year 2016) stipulates that an additional number of 80 labour inspectors will be hired. According to the ACT's website ([www.act.pt](http://www.act.pt)) the authority has its HQ in Lisbon and 33 local offices in all parts of mainland Portugal. It is part of the Ministry of Labour and Social Affairs (MTSSS) and covers the totality of mainland Portugal where approximately 95% of the population live. The autonomous regions of Azores and Madeira have their own services for labour inspection.

In 2015, the ACT carried out 39,306 inspections that covered 234,643 employees.

The **Institute of Social Security (ISS)** is responsible for the management of the contributions to, and of the benefits from, public social security (schemes regarding illness, parenthood, unemployment, families, social benefit, pensions, and others). This responsibility includes preventing and combating fraud with regard to the payments to the beneficiaries, and combating fraud and evasion regarding the payment of contributions to the social security. This latter type of action against fraud is directly related to undeclared work. The ISS' inspecting activity is directed against evasion of social contributions and against the falsification of contributive careers (in order to obtain higher pensions)<sup>324</sup>.

The total number of staff of the ISS was 8,285 in 2014 (2013: 9 172). The Institute is part of the Ministry of Labour and Social Affairs (MTSSS) and covers the territory of mainland Portugal. Its central services are complemented by regional centres in all 18 district capitals on mainland Portugal. The ISS covers 4.2 million beneficiaries; 3.3 million of them are salaried workers (2014).

The **Tax and Customs Authority (AT)** is responsible for the collection of taxes and customs. (Ministerial Order 198-A/2012, <https://dre.tretas.org/dre/301915/>). Its total staff was 10,762 in 2014 (2013: 11 341). The AT is a Directorate-General of the Ministry

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<sup>322</sup> ACT (2016), op. cit

<sup>323</sup> Ibid.

<sup>324</sup> ISS (2015) Relatório de Atividades 2014, online: [http://www.seg-social.pt/documents/10152/14494812/RA2014\\_v1.0\\_Final/4c991822-994d-42f8-a15d-424338558672?version=1.0](http://www.seg-social.pt/documents/10152/14494812/RA2014_v1.0_Final/4c991822-994d-42f8-a15d-424338558672?version=1.0)



of Finance, with Central Services in the capital Lisbon and decentralised services in the areas of taxes (21 centres and 343 local offices) and customs (15 centres and 24 local delegations). It covers all individual and collective persons who are subject to tax or customs in the total national territory (mainland and autonomous regions).

The **Foreigners and Borders Service** (briefly referred to as SEF), is a security service, organized hierarchically depending on the Minister of Internal Affairs, with administrative autonomy, that, in the context of internal security policy, has the mission to control the movement of persons across borders, the residence and activities of foreigners in the national territory, as well as to study, promote, coordinate and implement the measures and actions related to those activities and with migratory movements<sup>325</sup>.

### 2.2.3 Cooperation and collaboration between authorities and cross-border authorities

The **ACT's** 'Referential Framework for the Inspecting Activity'<sup>326</sup> states that the Inspector General of Labour 'proposes when necessary' to the head of the Authority requests for the support of other entities, namely experts for giving their opinion, police forces for protecting the inspectors and supporting the preservation of evidence, other public bodies with inspecting responsibilities (**namely the ISS, the AT, the SEF and others**), other public services for gathering essential information, the Institute of Insurances of Portugal for activities related to work accidents, and the Institute of Forensic Medicine. This support is requested on the basis of 'reciprocity'.

The **ACT notifies systematically** other entities about infringements revealed by its inspecting activities. In its report in 2015, the Authority registered a total of 851 notifications to other bodies (ISS, AT and others<sup>327</sup>). These notifications are regulated by law. Notifications with regard to unpaid contributions to the social security (info from ACT to ISS) are mandatory<sup>328</sup>. The ISS, on the other hand, informs the ACT about issues that are relevant for its activity (e.g. in relation to the posting of workers in other EU-MS, see ACT 2016<sup>329</sup>).

The **AT's** 'Strategic Plan for the Combat against Tax and Customs Evasion and Fraud 2015-2017' (further cited as "Strategic Plan 2015-2017") states that its inspecting activity shall continue to be based on a cooperation strategy with common 'preventive and prospective actions' with other entities, namely the police and other entities, amongst them the ACT, the ISS and the SEF<sup>330</sup>. The **AT** refers in its "Strategic Plan 2015-2017" that it had intensified during the years before its cooperation with the ACT, ISS and other entities<sup>331</sup>.

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<sup>325</sup> As stipulated in the paragraph 1 of article 1 of the organic law of the Foreigners and Borders Service, approved by Decree-Law No. 252/2000, of 16 October (however changed by Decree-Laws Nos. 290-A/2001, of 17 November, 121/2008, of 11 July, and 240/2012, of 6 November).

<sup>326</sup> ACT (2015) Referencial da atividade inspetiva / Autoridade para as Condições do Trabalho; Lisboa: ACT, 2015; Internet: <http://www.act.gov.pt/%28pt-PT%29/crc/PublicacoesElectronicas/Documents/Referencial%20da%20atividade%20inspetiva.pdf>

<sup>327</sup> ACT (2016) Atividade de inspeção do trabalho: relatório 2015 / Autoridade para as Condições do Trabalho; Lisboa: ACT, 2016; Internet: [http://www.act.gov.pt/\(pt-PT\)/SobreACT/DocumentosOrientadores/RelatorioActividades/Documents/Relatorio%20Atividade%20Inspetiva%202015.pdf](http://www.act.gov.pt/(pt-PT)/SobreACT/DocumentosOrientadores/RelatorioActividades/Documents/Relatorio%20Atividade%20Inspetiva%202015.pdf)

<sup>328</sup> Ibid.

<sup>329</sup> Ibid

<sup>330</sup> AT, Autoridade Tributária e Aduaneira 2014, Internet: [http://info.portaldasfinancas.gov.pt/NR/rdonlyres/714DD895-8D4C-4EF3-9ED0-DB71CC4989E9/0/RA\\_AT\\_2014e.pdf](http://info.portaldasfinancas.gov.pt/NR/rdonlyres/714DD895-8D4C-4EF3-9ED0-DB71CC4989E9/0/RA_AT_2014e.pdf)

<sup>331</sup> The AT's "Strategic Plan 2015-2017" states in the report of the results of the previous Plan (2012-2014) as one achieved goal: "Invigorate significantly common preventive and prospective actions in cooperation with other entities, namely" the criminal investigation

The ACT's systematic notifications to other bodies (in the first place the ISS and the AT; see above) can be qualified as an important element of **data exchange** in the area of undeclared work.

The AT's 'Strategic Plan for the Combat against Tax and Customs Evasion and Fraud 2015-2017' indicates that this Authority has made (at least since 2012) a systematic effort to improve the capacity of its internal and external exchange of data and information. One concrete measure amongst the Strategic Plan's priorities for 2015-2017 is the implementation and automatization of the detection of discrepancies between the amounts of money and numbers of workers given by employers to the Social Security and to the AT<sup>332</sup>.

The ACT's **notifications to the ISS, the AT and other entities** registered in its Report of Activity 2015 are the result of the Authority's systematic cooperation with other bodies. These notifications (851 to the ISS, AT and others; 141 to the prosecutor's office) represented 2% and 0.5% of the number of the total number of inspections, respectively.

There are also indicators of an active involvement of the ISS and AT in the exchange of information.

In its Report of Activities 2015 the ACT registers an **exchange of information with other EU-Member States** within the Internal Market Information System (IMI). In 2015, 143 requests from other MS were answered by the ACT, most of them from France (71) and Belgium (47). In the same year the ACT answered a further 140 information requests by foreign liaison services in Portugal.

The AT's Strategic Plan 2015-2017 includes the objective to intensify international cooperation (pp. 32 and 64) and stipulates that its software for data-export will be updated in order to guarantee its compatibility with the present model in the OECD.

## 2.3 Policy Focus and Measures

### 2.3.1 Policy approach

**The Programme of the Government** (2015-2019) names as one of its three top-priorities the aim to 'Promote employment, combat job insecurity'. In relation to the effort to reduce job insecurity the programme commits itself to combat 'abusive and illegal use of fixed-term contracts, bogus self-employment, temporary agency work, partly or totally undeclared work and abuses and illegal practices in the use of employment measures' (p. 24).

In addition to the inspecting activities of the three key players in the combat against undeclared work (ACT, ISS and AT), the ACT launched in 2014 a National Campaign against undeclared work that aimed at raising general awareness in society and of social partners about undeclared work. Numerous national, regional and local employer associations and trade unions were actively involved in the implementation of the enabling and preventive activities of the Campaign.

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department (PJ), the inspection of the regional centres of the ISS, the customs brigade of the GNR (BR-GNR), the Authority of Food and Economic Security (ASAE), the ACT, the SEF and the constabulary (PSP). The report does not present more specific information regarding this cooperation.

<sup>332</sup> AT, Autoridade Tributária e Aduaneira 2014, Internet: [http://info.portaldasfinancas.gov.pt/NR/rdonlyres/714DD895-8D4C-4EF3-9ED0-DB71CC4989E9/0/RA\\_AT\\_2014e.pdf](http://info.portaldasfinancas.gov.pt/NR/rdonlyres/714DD895-8D4C-4EF3-9ED0-DB71CC4989E9/0/RA_AT_2014e.pdf)

The chapter on the 'Prevention and combat against contributive fraud and evasion' in the ISS' Report on Activities 2014<sup>333</sup> registers only the results of the Institute's inspecting activity. It does not include any reference to enabling or preventive action.

The AT's strategy, on the other hand, demonstrates a strong concern with the necessity for preventive action<sup>334</sup>.

Migrants are particularly vulnerable to undeclared work and are therefore a specific target for preventive and deterring action. The High Commissioner for Migrations (ACM) plays a central role in this relation. The ACM coordinates a broad network of local services for the insertion of migrants into the labour market which is an important contribution for the prevention of undeclared work amongst migrants. The prevention of and combat against undeclared work are important aims of the government's Strategic Plan for Migrations 2015-2010 (explicitly) and of the III National Plan of Prevention and Combat against Human Trafficking 2014-2017 (implicitly).

### **2.3.2 Measures to tackle undeclared work**

#### **Government measures in place to tackle undeclared work: Measures to promote and extend decent work to all:**

- Measures to simplify and facilitate compliance with labour, fiscal and social security laws.
- Measures to reduce context costs, through simplification, reducing bureaucracy and dematerialization of the fulfillment of legal obligations and administrative formalities and simplification of access and exercise of economic activities.
- Measures to facilitate detection, sanction and dissuasion of undeclared work practices.

#### **The Role of the Portuguese Labour Inspectorate (ACT) in tackling undeclared work**

- The ACT is the major player in the fight against undeclared in Portugal. The ACT's approach is based on two strands: (1) Deterrence and (2) enabling compliance
- No data beyond the results of the ACT's and ISS' inspecting activities were available for use in this report.

### **2.3.3 Good practice in the MS:**

- Systematic notification of other entities (ISS, AT, SEF and others) by ACT.
- ACT's National Campaign against undeclared work (2014-2015) with a strong preventive aspect and based on the active involvement of social partners and other public entities (ACM, SEF).
- ACM's support to migrants' insertion into the labour market.

### **2.3.4 Challenges and barriers**

The main challenges in addressing undeclared work in Portugal include:

- Lack of a strategic nationwide plan focused on combating the phenomenon of undeclared work.
- The absence of a system for the regular and systematic assessment of the phenomenon.
- Insufficient international cooperation in the fight against undeclared work.

In response to these challenges, the ACT's National Campaign 2014-2015 gave an important impulse to the involvement of social partners and to awareness raising with

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<sup>333</sup> ISS (2015), op. cit.

<sup>334</sup> AT, Autoridade Tributária e Aduaneira 2014, Internet: [http://info.portaldasfinancas.gov.pt/NR/rdonlyres/714DD895-8D4C-4EF3-9ED0-DB71CC4989E9/0/RA\\_AT\\_2014e.pdf](http://info.portaldasfinancas.gov.pt/NR/rdonlyres/714DD895-8D4C-4EF3-9ED0-DB71CC4989E9/0/RA_AT_2014e.pdf)

regard to undeclared work. This positive experience should be transformed into continuous practice. The new government is going to increase the number of labour inspectors, thus opening the way to an increased inspecting activity of the ACT.

The key remaining challenges to overcome in order to enhance the effectiveness of the efforts to combat undeclared work, include:

- Simplifying compliance and implementation, in conjunction with the social partners;
- Formulation of a national strategic plan against undeclared work, the creation of a structure of coordination (national and international) and the creation of a system of evaluation and monitoring; and
- Intensify international cooperation, notably through the European Platform to Tackle UDW.

## Factsheet on Undeclared Work – ROMANIA (July 2016)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

The definition used by the National Institute for Statistics does not refer specifically to undeclared work but to the non-observed economy. It states that this is the total of activities that are in principal falling within the boundaries of production of the national accounts system but that are not directly classified as such (i.e. non-observed). The Labour Force Survey (LFS) or AMIGO data as published on the National Institute of Statistics website includes the number of salaried employees (RO: *salariați*), which also includes persons working in the informal sector as well as persons working on the black market although no definition of those is given specifically. It is presumed therefore that internationally applied definitions are in use. The definition used by the Labour Inspectorate, which is the main state body entrusted with combating undeclared work, is work that is undertaken without observing the provisions of the labour legislation, in most cases without a labour contract, permit or license as the case may be. If such work is undertaken by a larger number of persons it may constitute criminal offence (i.e. more than five). Provisions regarding this are included in the Labour Code<sup>335</sup> (Law. No.53/2003 with subsequent amendments,), title XI (Legal responsibility) chapters IV/ and V (as of the latest version of the Labour Code,-2015).

As said above, the legal definition is used by the Labour Inspectorate - the state body with the explicit legal mandate for the prevention and combating of undeclared work, as well as by other bodies of the state (e.g. the National Agency for Fiscal Administration - ANAF) when working to combat the phenomenon. Social partners and enterprises also make use of the legal definition as used also by the Labour Inspectorate which is subordinated to the Romanian Ministry of Labour. The National Institute for Statistics makes use of the definition generally accepted at European level. Several other definitions, are used by various academics.

#### 2.1.2 Characteristics of undeclared work

A variety of types of undeclared work co-exist at the moment. 'Envelope wages' is considered to be the most frequent with employers opting for the payment of the statutory minimum salary while giving the rest as envelope payments, mainly to avoid social insurance contribution payments. As the minimum salary has been increased successively, even twice a year since 2012 this practice has become ever more expensive. However it is to be noted that some employers are resorting now to artificial reductions of working hours so as to pay practically the sums as formal payments while leaving the rest in the form of envelope wages. Another form that is widespread in the health services are 'informal payments' made by patients to doctors nurses and other medical personnel. Work without a contract is less and less present due to better and more targeted controls of the labour inspectorates but it is still the case in construction, restaurants, retail commerce and agriculture<sup>336</sup>.

In regard to the main broad sectors where undeclared work is found, most cases of undeclared work occur in industrial type activities, followed by activities of warehousing,

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<sup>335</sup> The labour Code (Law no.53/2003 with subsequent amendments) does not include per se a definition of UDW. However, articles contained in the chapter imply a definition of it.

<sup>336</sup> According to a recent study performed by the National Scientific Research Institute in the field of Labour and Social Protection and published at „editura UNIVERSITARA”, Bucharest 2015, under the title: Assessments of Undeclared Work Dimension; Micro and macro economic approaches' (RO: *Evaluari ale dimensiunii muncii nedeclarate; abrodari micri si macroeconomice*), Ed.Universitara, Bucharest-RO, 2015 (Larisa Stanila-coordinator, Maria Denisa Vasiliescu, Amalia Christescu, Madallina Ecaterina Pppescu, driana AnaMaria Davidescu and Catalin Ghinararu;

transportation and commerce as well as hotels and restaurants. Construction has somehow reduced its size as a result of the crisis on the one side but also as a result of more and targeted control, Undeclared work in agriculture has also been brought somehow under control after the adoption in 2011 of the daily labourer's law (Legea Zilierilor, Law no.52/2011).. Linked to construction are the small home repairs and other such services. As said above, informal payments, as a peculiar form of undeclared work, are present on a wide basis in health provision and public education. More recently and with the development and diversification of activities of the national economy, undeclared work has penetrated also in enterprises providing services other than the retail, and involving work on short-term contracts where the turnover of staff is high. In most cases these temporary, or determined duration, contract workers are subjected to various forms of undeclared work.

In most cases undeclared work is prevalent in small and medium sized enterprises. There are forms of undeclared work present also in large enterprises but this is less frequent as these generally have collective labour agreements (mandatory according to the Romanian Labour Code for enterprises hiring more than 21 workers) and forms of unionisation or other types of employee representation.

The main motivation for undeclared work is the avoidance of taxation and especially of social contributions which are deemed as still too high by most employers. Another motivation, especially for 'informal payments' in public health and education are low salaries which make personnel in these sector prone to engaging in such practices. Cultural motivations and deeply rooted lack of trust in the state and its institutions also motivate such practices. A lower price for services, especially for home repairs and small construction services is yet another powerful determinant which maybe also linked to the lack of jobs, low salaries and generally low level of incomes.

### **2.1.3 Estimated scale of undeclared work**

It is generally considered that, overall, the 'shadow' or 'informal economy' would make for around 29 %<sup>337</sup> of the GDP according to various methodologies used for its quantification. According to various estimates around 1.3 to 1.4 million individuals engage in such activities. Figures for 2010-11, based on the comparison between the results of the Labour Force Survey (AMIGO) and the labour cost survey, both run by the National Institute of Statistics show a certain drop to figures of below 1 million for 2010-11. The highest concentration seem to be industry or industrial activities with around 385 000 persons for 2011, followed by commerce, transport, hotels and warehousing with around 355 000. As a result of the crisis the construction sector looks now smaller in this respect with only between 110 000 and 120 000 workers. A new concentration pole appeared in IT industries and communications recently.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

The main national authority entrusted with the prevention and combating of undeclared work is the Labour Inspectorate, as of 2015 the Labour and Social Inspectorate, subordinated to the Ministry of Labour. The Labour Inspectorate has the full and explicit legal mandate for the enforcement of both employment and labour legislation in general ('labour relations' matters) as well as of health and safety at work legislation. The Labour Inspectorate is organised in accordance with Law no.108/1999 (republished last as of 2012, Romanian Official Journal/*Monitorul Oficial al Romaniei* no.290/03.05.2012). Its attributes on undeclared work are stated in article 6, section 'A', letter 'e' of the previously mentioned act of law. On aspects of tax evasion, the main responsibility rests with the National Fiscal Administration Agency (ANAF) subordinated to the Ministry of

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<sup>337</sup> Fr.Schneider, (2012), The Shadow Economy and Work in the shadow; What do we (not) know?, IZA, Discussion paper no.6423

Public Finances. The Labour Inspectorate is also the main source of regular administrative data and reporting on undeclared work, its prevention and combat.

The Labour Inspectorate specifically tackles cases of undeclared work under their various forms. For cases where tax evasion is implied the National Agency for Fiscal Administration is also involved. For cases where the recourse to undeclared work is accompanied by fraud with regard to social benefits, the Social Inspection is also involved (together with the Labour Inspectorate these are two organisations subordinated to the Ministry of Labour and which as of 2015 work jointly). The National Agency for Employment may also be involved where undeclared work is accompanied by fraud with regard to the unemployment benefit or the improper use of the various subsidies provided to employers as active employment measures. The support of National Police or the National inspectorate of the Gendarmerie are involved when and where deemed necessary. Where cases of undeclared work are linked to illegal immigration or the trafficking of persons the support of the Romanian General Inspectorate for Immigration as well as that of the Frontier Police may be also provided.

### **2.2.2 Characteristics of the responsible organisations**

All of the organisations described above are national.

The Labour Inspectorate is a national organisation subordinated to the Ministry of Labour and which has 42 county branches (RO: judet), including in this number the branch for the Municipality of the capital city of Bucharest. The wider remit of the Labour Inspectorate covers the whole field of application of the labour legislation as well as of the health and safety at work regulations.

The National Fiscal Administration has a territorial organization, with regional divisions. It is subordinated to the Ministry of Public Finances. Within its broader remit fall not only the collection of all state budget taxes and social contributions, but also combating fiscal and contribution fraud.

Police and Gendarmerie operate under the authority of the Ministry of Interior as does the Frontier Police and the Romanian Office for Immigration.

The Labour Inspectorate also carries out controls and inspection with the Consumer Protection Office, which also classifies as national government and which has a national network of branch offices.

The National Agency for Employment is the Romanian PES. It has 42 county offices.

The General Inspectorate for Immigration is also a national organization subordinated to the Ministry of Interior.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The Labour Inspectorate as the main organisation responsible for the prevention and combating of the undeclared work has concluded several 'cooperation protocols' with the organisations cited above. By law it is authorised to also request and receive, if needed, the support of Police and eventually of the Gendarmerie if this is deemed necessary. In cases of undeclared work involving trafficking of persons or illegal immigration it has the right to request the support of the Frontier Police and of the Romanian Office for Immigration. Case by case when campaigns are organised it may work, basing on inter-institutional protocols with the ANAF and other designated state bodies such as also the Office for the Protection of Consumers and the Social Inspectorate. It has also a cooperation protocol with the Special Telecommunications Service.

In regard to data exchange between these organisations, the Labour Inspectorate operates and maintains REVISAL, or the national electronic register of the employees, where all employers are obliged by law to input data on the labour contracts concluded, as well as all of changes occurring. Data are shared regularly with the ANAF, the Social Inspectorate, the National Agency for Employment as well as other state bodies if

necessary. Information is also exchanged with the National Health Insurance House and the National Pension House. The single numerical personal code of all individuals aged 14 and above allows for accurate registration of all employees and of all of their employment contracts under the labour law. Employers also have their single registration codes.

Most of the campaigns directed by the Labour Inspectorate for the targeted prevention and combating of undeclared work are carried out in cooperation with the other state bodies already mentioned using both the general inter-institutional cooperation protocols as well as ad-hoc cooperation arrangements for each and every action. In 2011 an integrated mechanism for the prevention and combating of undeclared work was created via a government decision. The main body of evidence is constituted by the number of controls performed by the Labour Inspectorate as well as by the number of cases identified and the volume of fines and sanctions applied. Since the modification of the Labour Code in 2011 which included a toughening of sanctions against undeclared work, including criminalisation of what has been deemed to be a 'significant resort to it', the number of employers found as using undeclared work and sanctioned for it has decreased from more than 9 000 in 2011 to around 3000 in 2015.

In regard to cooperation and collaboration with other Member States, the Labour Inspectorate regularly cooperates with similar bodies in practically all of the Member States including for the development of good practices using also EU funds in the frame of EU co-financed projects.

Data exchanges between the Labour Inspectorate and other similar bodies also takes place on a case by case basis. The Labour Inspectorate also works with other national specialised authorities for the protection of the rights of Romanian workers abroad. For these purposes, it acts in conjunction with the offices of the labour attaché of the Ministry of Labour.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Tackling undeclared work has always been considered a priority in Romania given the dimensions of the phenomena as well as its social and economic implications. Measures have always included both an enabling as well as deterring approach. In milder cases the Labour inspectors have refrained from applying fines and generally offer options for rather more preventive or enabling type measures, while resorting to fines and other measures only if preventive measures failed or if cases were serious, involving large numbers of persons as well as significant fiscal evasion and fraud. The measures have become more deterring in their character as of 2011 with the changes to the Labour Code (applied as of 1 May 2011) when undeclared work above a certain level (more than five workers simultaneously without a labour contract) has become equal to a criminal offence and as such liable for prosecution.

Also notable are the successive rounds of VAT reductions implemented starting in 2013, which included first a targeted reduction of VAT for bread and bakery products from 24 % to 9 %, then extended to meat products and then generalised to all of the alimentary products as of mid-2015. This has been followed by a general reduction of VAT from 24 % to 20 % as of 2016. Social security contributions have been also reduced by 5 pp as of the last quarter of 2014.

### **2.3.2 Measures to tackle undeclared work**

The backbone of the ensemble of measures taken for the prevention and combating of undeclared work relies on inspections and controls. These are carried out regularly as well as in the form of campaigns directed towards those sectors where either there is a regular prevalence or where seasonally such prevalence tends to occur. Also the Labour Inspectorate responds to individual complaints from the public with regard to breaches of either labour law or of the regulations regarding health and safety at work.



Apart from this the Labour Inspectorate runs information campaigns that warn against the perils of undeclared work and the disadvantages and risks associated with it. It runs such initiatives both with other state bodies involved as well as in cooperation with employers and unions, schools and universities. The Labour Inspectorate has worked so as to enhance the system of electronic registration of all labour contracts via the REVISAL system. It has worked with the National House of Pensions as well as in cooperation with the National Labour Research Institute as to create a national database for all data previously contained in the so-called labour booklets (RO: *Carnet de Munca*) and ensure that scanned copies of all of these booklets (in total around 9 million out of which more than 7 million have been scanned finally) were stored into a national database maintained by the National House of Pensions. As such, the paper record of the labour booklet has been removed from use as of 31 December 2010.

A certain effectiveness of the measures is visible in practice. As said in the previous paragraphs, undeclared work has been on the fall as of 2010-11, which means after the introduction of tougher sanctions as part of the Labour Code as well as after electronic registration has become the sole mean of registration of labour relations. A significant role may also be attributed to the daily labourer's law, passed in 2011.

### **2.3.3 Good practice**

Definitely here stands the introduction of the single salary employees register, the REVISAL system, as well as the process by which the paper records have been removed from use and replaced with a database created at national level for the storage of all information previously contained by those (i.e.; previous to 2010). The introduction of criminal charges for what may be deemed as significant recourse to undeclared work also may be counted as good practice.

### **2.3.4 Challenges and barriers**

The main challenges are related basically to the deeply rooted mistrust of the state and its bodies and staff by the general public as well as by employers and employees equally. State civil servants are viewed as corrupt and abusive, as well as self-serving rather than acting in the general interest of the public and the tax payer. This makes resorting to undeclared work very common and not necessarily socially unacceptable. It is also viewed as the only response possible, at times, to poverty, lack of jobs and low-income which affect large sections of the population in Romania and which may be considered as the main rationality behind the significant recourse to undeclared work.

These challenges and barriers are being addressed in the following ways:

- by enhanced cooperation between the various state bodies as well as by the introduction of more electronic instruments of contract registration;
- through several rounds of fiscal and contribution relaxation; and
- through a toughening of penalties for situations where undeclared work is considered as 'significant' (criminalisation of the recourse to undeclared work).

The key remaining challenges to be addressed regarding undeclared work are as follows:

- A still pervasive culture of mistrust in the state and its agents;
- Far too much reliance on the punitive aspects of the legislation with less weight given to enabling, education and preventive actions. Severity should be applied with caution and only where strictly the case and not with largesse;
- The persistent lack of jobs and employment opportunities, especially in rural areas but also in small cities; and
- Low incomes of the majority of households which encourages undeclared work in all of its forms.

## Factsheet on Undeclared Work – SLOVAKIA (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

The term "undeclared work" is not defined in Slovak legislation. The most relevant legal reference is provided by the Act on illicit work and illicit employment (Act No. 82/2005 Coll.). The law defines illicit work as *dependent work performed by a natural person for a legal entity or sole proprietor, where (i) there is no labour-law or state-civil-service-law relation established between the two parties pursuant to special regulation<sup>338</sup>, or (ii) the natural person is a third country national employed in conflict with respective provisions<sup>339</sup>*. At the same time, the law determines illicit employment as *employment of a natural person by a legal entity or sole proprietor who makes use of dependent work of (i) a natural person with whom there is no labour-law or state-civil-service-law relation established, (ii) a natural person with whom a labour-law or state-civil-service-law relation is established but the employer has not complied with his/her obligation to notify the Social Insurance Agency<sup>340</sup>, (iii) a third country national employed in conflict with provisions on employment of third country nationals and asylum seekers and/or staying in the territory of the Slovak Republic in conflict with legal provisions regulating the stay of foreigners.*<sup>341</sup>

A key aspect in defining (and proving) illicit work and illicit employment is the performance of dependent work, which is defined as *work carried out in a relation where the employer is superior and the employee is subordinate, and in which the employee carries out work personally for the employer, according to the employer's instructions, in the employer's name, during working time set by the employer [Article 1(2) of the Labour Code]*. The Labour Code further stipulates that dependent work may be carried out only in an employment relationship or a similar labour-law relation and cannot be carried out in a contractual civil-law or a commercial-law relation. The definition of dependent work has been tightened since 1 January 2013 by way of reducing the number of defining attributes with the aim of preventing the substitution of labour-law relations with other forms of contractual relations (e.g. work carried out based on a trade licence).

Public administration authorities involved in the fight against undeclared work follow the same definition of illicit work/illicit employment. Academic and research institutions, dealing with the phenomena of undeclared work and the shadow economy, also make use of modified definitions and/or refer to definitions used by international organisations (e.g. the EC definition of undeclared work). Examples include the terms "unregistered work" and "hidden economy".<sup>342</sup>

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<sup>338</sup> Labour Code (Act No. 311/2001 Coll.) and the Act on state civil service (Act No. 400/2009 Coll.)

<sup>339</sup> Article 21 of the Act on employment services (Act No. 5/2004 Coll.)

<sup>340</sup> The main duty of employers is to register employees for social insurance at the Social Insurance Agency the day before commencing work at latest.

<sup>341</sup> Illicit work is not considered work performed for a natural person who is an entrepreneur by his/her direct relative, sibling or spouse who has pension insurance, who is a recipient of a pension or is a student under the age of 26 (the same applies to illicit employment).

<sup>342</sup> Unregistered (or black) work is defined as work performed by an individual for remuneration, from which taxes or contributions for social and health insurance have not been paid (by the employer or the worker). Hidden (or shadow) economy is defined as the sum of activities, producing goods (products and services), which have not been captured by way of official registration (e.g. statistics, tax system, accounting, etc.). Hidden economy includes activities in the formal sector, the non-formal sector, and illegal activities (Infostat (2014): Hidden economy (August 2014) – survey report. Centre of social research at Infostat).

### 2.1.2 Characteristics of undeclared work

According to labour inspection statistics, evasion of social security contributions in a formal employment relationship is the most prevalent form of undeclared work in Slovakia, followed by false self-employment and/or absence of a labour-law contract. Available national surveys imply that the most significant manifestations of undeclared work include partial cash-in-hand payments received by dependent employees and false (involuntary) self-employment.<sup>343</sup> Foreign research confirms that only a small share of employees are working fully informally in Slovakia, yet a large share of the workforce tends to have undeclared and/or under-reported income.<sup>344</sup> Illicit work carried out by immigrant workers is considered a relatively minor problem.

Recent surveys confirm that undeclared work is concentrated mainly in the construction sector, hotels and restaurants, agriculture, and other services. While the traditional areas of undeclared work tend to keep (construction) or somewhat lose (agriculture) their notorious positions, the incidence of undeclared work in various services sectors (e.g. catering, retail trade, sport and leisure time services) appears to have relatively increased over the past decade.<sup>345</sup> Survey findings generally correspond with labour inspection data. Control authorities are, by law, focusing their activities on 'high-risk' sectors (construction, retail/wholesale, hotels and restaurants).

Undeclared work is most prevalent in micro and small enterprises employing nine or less people, as suggested by both inspections and surveys. Large enterprises appear to be much less involved in undeclared activities. Surveys further indicate that undeclared work concerns mainly occasional and seasonal jobs, and is carried out more often by unemployed persons than those with an existing paid job or the self-employed.<sup>346</sup>

High levels of social security contributions and taxes (contributing to high labour costs in relation to productivity) and administrative burdens are considered the traditional drivers of undeclared work for employers. The abundant supply of undeclared labour seems to be another important incentive. Three main motives lead workers to participate in undeclared work – survival concerns, efforts to increase income, and the need to pay off debts.<sup>347</sup>

### 2.1.3 Estimated scale of undeclared work

According to a representative survey carried out by Infostat in 2014, 18.1 % of respondents stated to have carried out some form of 'black work' in 2013 (21.4% of men and 15.2 % of women), of which 7.4 % worked illicitly in their main job and 10.7 % in their second job. The share of positive answers has not changed much compared to 2007 when a similar survey was undertaken by Infostat (18.5 %), however, the relative share of women participating in undeclared work has increased since then (25.2 % of men and 12.4 % of women in 2007), which is in line with the supposed rise of undeclared work in the services sector. When applied to the economically active population, 492 400 persons have engaged in undeclared work in 2013, spending a total

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<sup>343</sup> Bednarik, Rastislav (2014): Undeclared work in Slovakia. Survey of opinions and attitudes of public administration representatives, Institute for Labour and Family Research, Bratislava. Internet: [http://www.ceit.sk/IVPR/images/IVPR/vyskum/2014/Bednarik/2170\\_bednarik.pdf](http://www.ceit.sk/IVPR/images/IVPR/vyskum/2014/Bednarik/2170_bednarik.pdf)

<sup>344</sup> IFP (2014): Unemployment in Slovakia. Economic analysis - Policy paper 30, Institute for Financial Policy, Bratislava. Internet: [https://www.finance.gov.sk/en/Components/CategoryDocuments/s\\_LoadDocument.aspx?categoryId=698&documentId=605](https://www.finance.gov.sk/en/Components/CategoryDocuments/s_LoadDocument.aspx?categoryId=698&documentId=605)

<sup>345</sup> Bednarik, 2014; and Infostat (2014): Hidden economy (August 2014) – survey report. Centre of social research at Infostat

<sup>346</sup> Infostat, 2014; Bednarik, 2014.

<sup>347</sup> Infostat, 2014; Bednarik, 2014.

of 139 453 000 hours on illicit work (3.6 % of total hours worked in the economy; 3.4 % in 2006).<sup>348</sup>

In 2016, control authorities (labour inspectorates and labour offices) carried out 25,931 inspections of illicit work in 23,416 enterprises and inspected 60,349 workers. Inspectors detected 1,311 employers (5.6% of all controlled employers; 7.1% in 2015) who illicitly employed 2,924 persons (4.8% of all controlled persons; 4.8% in 2015). Controls have been conducted mainly in small businesses with up to nine employees, where the highest number of violations have been detected. Among the illicitly employed, 81 persons were EU nationals and 220 were third-country nationals (7.5% of all cases; 1.7% in 2015), all of whom had a valid residence permit. A total of 1,139 fines were issued in 2016, amounting to EUR 4,144,800.<sup>349</sup>

There are no recent national estimates of the size of the shadow economy. A non-representative survey carried out by the Institute for Labour and Family Research among representatives of relevant public authorities estimated the size of the hidden economy at 21.4 % of GDP in 2014, an increase compared to 18.3 % of GDP estimated in a similar survey in 2007.<sup>350</sup> According to international studies (Schneider, 2013), the size of the shadow economy in Slovakia has been moderately decreasing in recent years and reached 15.0 % of GDP in 2013<sup>351</sup>.

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing Undeclared Work

The Ministry of Labour, Social Affairs and Family is the central state administration body responsible for the design and implementation of policies addressing undeclared work. Other ministries with important competences in developing policies that help to prevent and deter undeclared work include the Ministry of Finance (area of taxes, fees and customs), Ministry of Economy (business environment regulation), and the Ministry of Interior (small entrepreneurship, entry and stay of foreigners).

The Ministry of Labour manages and controls the National Labour Inspectorate (NLI) and the Central Office of Labour, Social Affairs and Family. The regional labour inspectorates and the territorial labour offices, including the Central Office, are the main authorities in charge of supervising observance of legal provisions governing the ban on illicit work and illicit employment. They closely cooperate with the Social Insurance Agency which oversees employer and self-employed registration and contribution obligations. Although not primarily focused on detecting undeclared work, Tax Offices pay attention to possible incidence of illicit work when performing tax controls. Control activities focused on illicit employment are to a limited extent performed also by Trade Licensing Offices. Inspection authorities collaborate furthermore with the Police Force, health insurance agencies, and self-governing authorities (towns and municipalities).

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<sup>348</sup> Hajnovicova, Viera (2014): Processing of results of a survey on the informal sector in 2014. Infostat, Bratislava

<sup>349</sup> Source: NLI (2014, 2015). Information on the amount of so-called additional payments, i.e. outstanding wage that has to be paid to the illicitly employed person and the amount of outstanding and/or recovered payments to tax, social security and health insurance authorities by the penalised employers is not readily available. NLI (2014): Informative report on detection of illicit work and illicit employment. National Labour Inspectorate, Kosice. Internet: <http://www.nip.sk/?t=46&s=128&ins=nip>; and NLI (2015): Informative report on detection of illicit work and illicit employment. National Labour Inspectorate, Kosice. Internet: <http://www.nip.sk/?t=46&s=128&ins=nip>

<sup>350</sup> Bednarik, 2014.

<sup>351</sup> Schneider, Friedrich (2013): The shadow economy in Europe, 2013. A.T. Kearney, Johannes Kepler University in Linz, Visa Europe. Internet: [https://www.atkearney.com/financial-institutions/featured-article/-/asset\\_publisher/j8IucAqMqEhB/content/the-shadow-economy-in-europe-2013/10192](https://www.atkearney.com/financial-institutions/featured-article/-/asset_publisher/j8IucAqMqEhB/content/the-shadow-economy-in-europe-2013/10192)

## 2.2.2 Characteristics of the responsible organisations

The **National Labour Inspectorate (NLI)** is a budgetary organisation of the Ministry of Labour with nationwide competence that oversees tasks concerning labour inspection and manages and supervises regional labour inspectorates. The NLI is the main partner for relevant inspection authorities in other EU and EEA Member States.

**Labour inspectorates** are charged with the performance of labour inspections, including supervision over the adherence to legal provisions regulating the ban on illicit work and illicit employment.<sup>352</sup> Inspectorates are located in eight regional centres and currently employ almost 500 workers, of which approximately 330 are labour inspectors (including NLI). Since 1 October 2013, specialised departments have been set up at each labour inspectorate to improve control of illicit work and employment. These units (called KOBRA) have special working time organisation and conduct controls also during the night, weekends and holidays. There are altogether 36 inspectors in the KOBRA units who have carried out 12,493 controls in 2016 and detected 883 employers (7.1% of all controlled employers) who illicitly employed 2,042 persons (7.4% of controlled natural persons).

The **Central Office of Labour, Social Affairs and Family (COLSAF)** is a budgetary organisation subordinate to the Ministry of Labour with main competence in the area of social affairs and employment services. COLSAF manages, coordinates and controls the operation of 46 territorial offices of labour, social affairs and family (labour offices). The Central Office and the labour offices are authorised to control adherence to legal regulations governing the prohibition of illicit work/employment. Execution of controls comprises, however, a minor part of activities performed by labour office staff. In 2016, approximately 130 inspectors conducted 2,559 controls and disclosed 83 employers (3.2% of controlled employers) who illicitly employed 168 persons (3% of controlled natural persons).

The **Social Insurance Agency (SIA)** is a public law institution responsible for the administration of social insurance. SIA controls adherence to legal provisions laid down in the Act on social insurance (Act No.461/2003 Coll.), including the registration and reporting obligations of employers and the self-employed. Pursuant to the Act on illicit work and illicit employment, the failure to register an employee for social insurance before he/she commences work is considered illicit employment. SIA shall not penalise detected violations if they had been penalised already by the labour inspectorate or labour office. In 2015, approximately 240 supervisors carried out 17,427 controls on compliance with social insurance regulation (14,604 in 2014). SIA has 36 local branches and three detached units.

**Tax offices** are financial administration bodies managed by the Financial Directorate within the competence of the Ministry of Finance. As part of local enquiries and tax audits, tax administrators consider also indications of illicit employment and illicit work, and inform respective control authorities (labour inspectorates and labour offices) accordingly.

**Trade Licensing (District) Offices** execute state administration in the area of entrepreneurship operated on the basis of a trade. Offices located in eight regional centres are authorised to control the observance of tax, fee and contribution duties and illicit employment by the self-employed. In actual effect, however, trade offices have provided assistance to inspection bodies in only 15 and 18 controls in 2014 and 2015, respectively.

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<sup>352</sup> In 2014, controls focused on illicit work/employment made up 38.2% of all inspections carried out by labour inspectorates. Violations of the ban on illicit work and employment are detected also within the scope of inspections primarily focused on observance of labour-law regulations, occupational health and safety regulations, or social legislation in transportation.

**Police Force**, in particular the **Bureau of Border and Alien Police and the regional directorates of the Police Force**, assist labour inspectorates and labour offices in controls of illicit work and illicit employment (315 and 82 joint controls in 2016, respectively).

### **2.2.3 Cooperation and collaboration between authorities within Slovakia and cross-border authorities**

In general, authorities involved in fighting undeclared work are obliged to cooperate and provide necessary information within the scope of their competence. At ministerial level, cooperation takes place mainly through inter-resort consultations on legislation and policies. Cooperation between state authorities directly involved in combating undeclared work is running basically at two levels – cooperative execution of controls and sharing of information.

Labour inspectorates and labour offices conduct joint inspections in the form of planned activities or ad hoc inspections and special campaigns. On specific occasions, inspectors and representatives from other relevant authorities join the control bodies (Social Insurance Agency, trade licensing offices, health insurance companies, tax offices, police). Police Forces are obliged to provide necessary cooperation and protection for inspections on request of the control bodies if threats to life or health of inspectors or obstruction of controls are anticipated.

Labour inspectorates and labour offices (including the Central Labour Office) have access to the electronic database of the Social Insurance Agency and may investigate data needed for controls. The control bodies are obliged to notify the Social Insurance Agency, the Central Labour Office and the respective labour office and/or labour inspectorate, tax office, and in cases relating to third country nationals also the Police Force, of all detected cases of illicit work and illicit employment. Control bodies shall also inform the respective trade licensing office about cases of repeated violation of the ban on illicit employment; this shall lead to the cancellation of the trade license. The National Labour Inspectorate maintains a central publicly available list of natural persons and legal entities that have violated the ban on illicit employment over the past five years. Control authorities are obliged to notify law enforcement bodies of any facts that indicate the commission of a crime.<sup>353</sup>

There are no available assessments of the effectiveness of cooperation between authorities.

As from 18 June 2016, a new law on cross-border cooperation in the posting of employees to perform work (Act No.351/2015) entered into force, which stipulates new competences for the National Labour Inspectorate and labour inspectorates in cross-border cooperation with respective authorities in the EU/EEA Member States. The law also amends the Act on illicit work and illicit employment, in that it shall penalise equally employers for accepting services supplied by another employer through an illicitly employed person(s) as if that employer had illicitly employed own workers.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Undeclared work is addressed by a mix of preventative and repressive policies in Slovakia. Preventative policies are pursued to improve the legal and administrative framework to make it more favourable for the declaration of economic activity and employment. The deterrence policy approach builds on strengthening detection and sanctions for violations. Even though there are no distinct trends in recent policy developments that would indicate favouring one or the other policy approach, the acting

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<sup>353</sup> Article 251a of the Criminal Code (Act No.300/2005 Coll.) specifies "unlawful employment" of third country nationals whose stay in the territory of Slovakia is in conflict with the law (illegal immigrants) as a criminal act that may be punished with a prison sentence of up to 3 years.

political representation but also the society in general tend to consider punitive policies as more effective in fighting illicit work than preventative measures. Nevertheless, in combination with reinforced controls and sanctions, a number of promising reforms have been implemented in recent years which strengthen incentives to declare work on both the demand and supply sides.

### 2.3.2 Measures to tackle UDW

The following table provides an overview of the main measures in place to tackle undeclared work. It also contains information on preventative measures which pursue more general objectives rather than just reducing motivations to engage in undeclared work.

Deterrence		Prevention	
Control activities	Inspection capacities of labour inspectorates were reinforced in 2013 -2014 which resulted in a substantial increase of performed controls and detected violations	Tax-favoured work agreements for students	Income up to EUR 200 monthly from work agreements for students is freed from social contributions
KOBRA units	Special units set up at labour inspectorates operate also beyond regular working hours  inspection results point to a higher rate of detected violations	Start-up support	Start-up support is available to self-employed through the ALMP scheme  Support to SMEs through different support schemes
Joint controls	Cooperation and coordination of controls is a standard practice and is considered important due to the different manifestations of undeclared work and scope of activity of participating authorities	Hiring incentives	Various wage subsidies are available for employers through the ALMP scheme and special ESF funded projects
Information and data sharing	Control authorities have access to social insurance data of the Social Insurance Agency  Control authorities notify other relevant authorities (e.g. tax offices, Social Insurance Agency) about detected cases of undeclared work	Administrative burden reduction	Points of single contact set up at every Trade Licensing Office  Electronic registration and reporting to commercial registers, tax and social security authorities  Simplified accounting rules for micro enterprises
List of employers violating the prohibition of illicit employment	National Labour Inspectorate maintains a publicly accessible list of employers who have infringed the ban on illicit employment in the past 5 years  Social Insurance Agency publishes a list of debtors	Child tax bonus and child care allowance	A tax bonus is granted to employed parents of dependent children (EUR 21.41 monthly)  Working parents may apply for a child care benefit (EUR 280 monthly) to co-finance childcare for children up to 3 years of age
Penalties and other sanctions	Employers who illicitly employed persons are fined with EUR 2 000 – 200 000 (the minimum fine is EUR 5 000 if two and more persons were illicitly employed)  Administrative sanctions include, for example, cancellation of trade license, license of temporary work agency, no access to EU funds and public tenders for a period of 5 years, etc.  Illicit workers may be fined with EUR 331, removed from the	Measures to support formal employment of long-term unemployed	Temporary in-work benefits may be provided to welfare recipients who take up a low-wage job  A temporary social contribution relief is available for employers who hire long-term unemployed  A health contribution allowance for low-wage workers and their employers to offset increase of labour costs associated with minimum wage increase

	register of job seekers and obliged to return received unemployment benefits (if relevant)		A workfare scheme requires welfare recipients to carry out at least 32 hours of activation work per month to be eligible for the basic subsistence benefit
Public hotline	Telephone link and e-mail for (anonymous) reporting on suspected cases of undeclared work and social system misuse (labour inspectorates, labour offices, Social Insurance Agency)	Awareness raising and counselling services (NLI, labour offices)	National Labour Inspectorate and labour offices organise awareness raising campaigns about the negative implications of undeclared work
Registration duties	Employers are obliged to register employees at the Social Insurance Agency before they start work		

### 2.3.3 Good practice

There is not sufficient supporting evidence to highlight individual measures as good practice. Available data suggest that on the 'deterrence' side, the operation of the KOBRA units within labour inspectorates has improved the success rate in detecting undeclared work. On the 'prevention' side, in-work benefits appear to have effectively increased incentives for inactive and long-term unemployed persons (who are over-represented among illicit workers) to take up low-paid work in the formal sector.

### 2.3.4 Challenges and barriers

There are several challenges which need to be tackled with regard to undeclared work in Slovakia:

- *High prevalence of under-declared income.* Available evidence suggests that although having a formal contract, employers and workers fail to declare the actual income in order to evade tax and social security obligations.<sup>354</sup> Inspectors find it difficult to detect under-reporting (cash-in-hand) when employers and workers co-operate in order to circumvent regulations.
- *Preferential tax treatment of the self-employed.* Recent tax reforms (2012-2013) have partly reduced distortions in the tax regimes for different categories of labour, but the tax regime for the self-employed remains preferential in relation to dependent employees. Hereby we refer mainly to the opportunities to adjust the tax base (e.g. by including part of personal consumption into business costs) or to defer registration and payments for social security, through which the self-employed can effectively decrease their tax and contribution obligations. One of the effects is a supposedly high occurrence of bogus self-employment, which is, despite recently tightened definition of dependent work, difficult to prove.
- *Lack of job opportunities in the formal sector for the low-skilled.* There is a relatively small group of low-skilled and unqualified labour in Slovakia, but they perform very poorly in the labour market. Given the very few opportunities in the formal sector, work in the informal or semi-formal sector is often the only opportunity for these groups (especially the Roma) to raise income. Although not a panacea, further reduction of non-wage labour costs on low-paid work could help to increase the motivation of employers to hire such labour.
- *Unclear policy/strategy regarding prevention.* There seems to be some ambiguity in the government's approach to creating an environment encouraging individuals and businesses to declare activities. On one hand, measures to reduce the tax wedge on low-paid work are being pursued while at the same time the minimum wage has substantially increased. Similarly, reduction of administrative burdens is promoted, while at the same time new

<sup>354</sup> IFP, 2014.



duties are imposed or extended (e.g. occupational health service) which are particularly burdensome for small businesses. Selective state aid and tax concessions are provided to large companies, while SMEs have hardly any access to such support.

Additional challenges stem from the widespread acceptance of illicit and unlawful behaviour in the society, weak law enforcement, limited capacity of inspection/control authorities, some remaining work disincentives in the tax-benefit system, and an unnecessary regulatory burden on businesses.

#### **Additional References**

Ad-Hoc Query on inspections to control the employment of irregular migrants. European Commission, European Migration Network, June 2015. Internet; [http://ec.europa.eu/dgs/home-affairs/what-we-do/networks/european\\_migration\\_network/reports/docs/ad-hoc-queries/ad-hoc-queries-2015.703\\_inspections\\_to\\_control\\_the\\_employment\\_of\\_irregular\\_migrants\\_wider\\_diss.pdf](http://ec.europa.eu/dgs/home-affairs/what-we-do/networks/european_migration_network/reports/docs/ad-hoc-queries/ad-hoc-queries-2015.703_inspections_to_control_the_employment_of_irregular_migrants_wider_diss.pdf)

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[http://ec.europa.eu/public\\_opinion/archives/ebs/ebs\\_402\\_en.pdf](http://ec.europa.eu/public_opinion/archives/ebs/ebs_402_en.pdf)

## **Factsheet on Undeclared Work – SLOVENIA (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

The relatively recently adopted and implemented (from 18 August 2014) Prevention of Undeclared Work and Employment Act (ZPDZC-1) differentiates between undeclared work and undeclared employment.<sup>355</sup> Both forms are prohibited in Slovenia.

Article 3 of the Act states that the pursuit of activities or work shall be deemed undeclared work when:

- A legal person or a foreign legal entity that is a legal person pursues an activity not defined in its constituent instrument or has no statutory documents relating to fulfilment of the conditions for performing the activities defined in its constituent instrument;
- A self-employed person or a foreign legal entity that is a self-employed person pursues an activity not recorded in the register of companies or has no statutory documents relating to fulfilment of the conditions for performing that activity;
- A legal person, a foreign legal entity or a self-employed person pursues an activity despite a ban on carrying out such activity;
- A foreign legal entity pursues an activity in the Republic of Slovenia and does not have a registered subsidiary there or does not hold a relevant statutory permit;
- A legal entity established in an EU Member State or the European Economic Area or Swiss Confederation fails to carry out service activities in accordance with the act governing services in the internal market; and
- An individual who is not registered or notified as provided by this or any other act pursues an activity or work.
- Similarly, Article 5 of the Act states that undeclared employment shall be deemed to occur when an employer:
  - Allows an individual to work but fails to conclude an employment contract with him and does not register him for compulsory social insurance schemes or deregisters him from compulsory social insurance schemes during employment;
  - Allows an individual to work but fails to conclude a civil law contract on the basis of which work can be carried out or does not register him for compulsory social insurance schemes;
  - Fails to conclude a contract with a retired person for temporary or occasional work in accordance with the act governing the labour market;
  - Allows a school pupil or student to work in contravention of the regulations governing temporary or occasional work of pupils and students; OR
  - Illegally employs a third-country national.

However, there are several forms of work and activities, which are not defined as undeclared work or employment, such as neighbourly help and humanitarian work. These are further elaborated in Article 7.

In the law, there are also two definitions of activities related to undeclared work, which are also prohibited – facilitation of undeclared work (Article 4) and illicit advertising (Article 6).

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<sup>355</sup> The Government of the Republic of Slovenia (Vlada Republike Slovenije), 2014. Prevention of Undeclared Work and Employment Act (Zakon o preprečevanju dela in zaposlovanja na črno (ZPDZC-1)).

Internet: <https://www.uradni-list.si/1/content?id=117354>

All organisations with an interest in UDW and UDE within Slovenia follow the same definitions.

### **2.1.2 Characteristics of undeclared work**

The most frequent forms of undeclared work are:

- When employers provide work to individuals with whom no employment or civil-law contract has been concluded;
- Employers who have failed to enter employees into relevant social insurance, and where employers de-register employees from social insurance while they still work for them; and
- Violations in the employment of foreign persons.

According to the report of the Government Commission for detecting and preventing undeclared work and undeclared employment for 2016<sup>356</sup>, the main sectors where undeclared employment is found are: construction, transportation, accommodation and food service activities.

No information on the employer size distribution of undeclared work were available.

According to Nastav (2009)<sup>357</sup> Slovenia does not deviate significantly from other countries in terms of the causes for the development and persistence of the shadow economy. The main reason for the shadow economy to exist is financial gains for working (or consuming) in it. That is why the shadow economy in Slovenia can in many cases be the only way out of difficult living conditions. Thus, it encompasses the characteristics of the social economy (the one that strives for survival and not sheer profit-making). Amongst the main causes for the shadow economy to be present in Slovenia are also high administration barriers (procedures, work of institutions) and tax load, which altogether push production into the shadow economy. Besides, social security fraud is a significant characteristic of the shadow economy in Slovenia.

### **2.1.3 Estimated scale of undeclared work**

According to the data presented in the Report on Effects of Prevention of Undeclared Work and Undeclared Employment for the year 2014 prepared by the Government Commission for detecting and preventing undeclared work and undeclared employment (2015), the share of undeclared employment is almost negligible – 0.006% of all employed persons in Slovenia. According to the Statistical Office of Slovenia, the share of shadow economy in 2010 was 8.3 % of Slovenian GDP.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing Undeclared Work:**

In Slovenia, there are several authorities with responsibilities for identifying, tackling and/or preventing UDW. With the new law in 2014, the main responsibility for tackling undeclared work was transferred to the Financial Administration of the Republic of Slovenia (FURS), which is in charge of undeclared employment (Article 5) and undeclared work regarding the supervision of individuals – tinkers (šušmarji). The Labour Inspectorate, MIRS and Inspectorate of the Republic of Slovenia for

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<sup>356</sup> The Government of the Republic of Slovenia, Report on Activities and Effects of Prevention of Undeclared Work and Undeclared Employment for the year 2016 prepared by the Government Commission for detecting and preventing undeclared work and undeclared employment.

<sup>357</sup> Nastav Bojan. 2009. The grey economy in Slovenia. Measurement, causes and consequences. Doctoral dissertation, Faculty of Economics, UL Ljubljana (Siva ekonomija v Sloveniji. Merjenje, vzroki in posledice. Doktorska disertacija, Ekonomska fakulteta, UL Ljubljana). Internet: [http://www.protisiviekonomiji.si/fileadmin/dokumenti/si/projekti/2013/siva\\_ekonomija/bojan\\_nastav\\_-\\_doktorska.pdf](http://www.protisiviekonomiji.si/fileadmin/dokumenti/si/projekti/2013/siva_ekonomija/bojan_nastav_-_doktorska.pdf)

Infrastructure have responsibility for certain forms of undeclared work, as stated below:

- Labour Inspectorate: part of illicit advertising;
- MIRS: undeclared work (with the exception of tinkers); facilitation of undeclared work of legal persons and part of illicit advertising; and
- Inspectorate of the Republic of Slovenia for Infrastructure: undeclared work, facilitation of undeclared work and illicit advertising, focus is on the supervision of the activities of passenger and goods transport in the road, especially activities of taxi services.

Other supervisory authorities are responsible for violations of the provisions of this Act related to the fulfilment of specific conditions for performing activities in the areas of agriculture and the environment, forestry, energy and spatial planning, health, education and sport and the interior.

The Government Commission for detecting and preventing undeclared work and undeclared employment has special role – more on its characteristics and activities is given below.

### **2.2.2 Characteristics of the responsible organisations**

- Government Commission for detecting and preventing undeclared work and undeclared employment: for the determination, coordination and monitoring of the areas of prevention of undeclared work and undeclared employment the Commission is appointed by the Government of the Republic of Slovenia. The Commission is composed of a representative of the ministry responsible for the field of prevention of undeclared work and employment (Ministry of Labour, Family, Social Affairs and Equal Opportunities), of the Ministry of Economy, Ministry of Finance, Ministry of Justice, Ministry of Internal Affairs, representatives of the supervisory authorities under ZPDZC-1, employers' and trade unions' representatives.
- Financial Administration of the Republic of Slovenia: at the end of 2016 there were 166 members of mobile units and 250 financial inspectors which also carry out inspections in the area of undeclared work and employment. The main tasks of the Financial Administration of the Republic of Slovenia are: assessment, calculation and collection of taxes and duties; customs clearance of goods; financial supervision and investigation; gaming supervision; cash controls on entering or leaving the EU; and more; since 18 August 2014 it is also responsible for inspections and control of undeclared work and employment in Slovenia.
- Labour Inspectorate of Slovenia: 42 labour inspectors at the end of 2016; until 18 August 2014 were responsible for inspections of undeclared work and employment; the Labour Inspectorate oversees the implementation of laws, other regulations, collective agreements and general documents regulating employment, wages and other receipts from employment, the employment of workers at home and abroad, cooperation of workers in management, strikes and occupational safety, unless otherwise provided by regulations. The main areas of inspections are: Employment relationships, Occupational Safety and Health and Social Protection.
- MIRS: is an inspection office, operating within the Ministry of Economic Development and Technology. Market inspectors carry out surveillance of execution of several legislative acts, which specify market relations. They are responsible for areas such as consumer protection, trade and craft, tourism and catering, protection of copyrights and some others. At the moment there are 100 inspectors.

The rest of the authorities (inspectorates) are responsible for specific areas.

### **2.2.3 Cooperation and collaboration between authorities within Slovenia and cross-border authorities**

According to the new Prevention of Undeclared Work and Employment Act (ZPDZC-1), the Financial Administration of the Republic of Slovenia (FURS) has (from 18 August 2014) exclusive competences and new powers of control over undeclared work and employment of individuals. It is also responsible for controlling unauthorised advertising of undeclared work and employment of individuals.

Since there are also other authorities involved, the Slovenian government appointed a special commission, in which all the involved authorities are cooperating. The tasks of the Commission are as follows:

- Coordinate the work of the supervisory authorities related to the prevention of undeclared work and employment;
- Propose to the Government of the Republic of Slovenia measures for more efficient prevention and detection of undeclared work and employment;
- Report on the implementation and effects of this Act to the Economic and Social Council, the Government of the Republic of Slovenia and the Inspection Board of the Republic of Slovenia by the end of June for the previous calendar year;
- Give initiatives to amend regulations within the limits of its competence;
- Identify annually the activities it considers prone to illegal employment of third-country nationals and draft an inspection plan; and
- Draw up a report on the inspections referred to in the preceding indent carried out in a calendar year and inform the European Commission of their results by the end of June for the previous calendar year.

If UDW and UDE are detected by other authorities that are not specifically stated in the law, these authorities have the obligation, to draw up a report on the findings and submit it to the competent supervisory authority.

According to the reports from different authorities involved in the activities of identifying, tackling and/or preventing UDW, the mechanisms for cooperation between them is relatively effective.

There is no specific information on cooperation and collaboration with other Member States.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The Financial Administration of the Republic of Slovenia is the main authority responsible for the supervision of undeclared work and employment. System supervision over taxpayers is provided on the basis of the annual plan. Criteria on the basis of which audits are performed are defined on the basis of risk analysis, received reports and random selection. Supervision over undeclared work and employment is directed into activities which are detected as risky and into implementation of activities in individual industries where this type of audits has not been performed yet. We would like to emphasize the following activities: accommodation and food service activities, construction, transport of passengers, trade, bakeries, taxi drivers and various service activities. Financial penalties are prescribed for violations. The most severe violations are processed within the criminal procedure.

Within the policy for managing undeclared work and employment the significant emphasis is placed also on preventive activities, with which taxpayers are encouraged to register and legalise performing of work and activities and to raise tax awareness. Also in cases of violations in connection with undeclared work and employment offenders are encouraged to eliminate them already during supervision, which results in the primary purpose of supervision, i.e. legalisation of employment, performing of work or activities.

## **2.3.2 Measures to tackle UDW**

### ***Preventive measures***

Taxpayers are with preventive measures encouraged to register and legalize the performed work and activities and to raise tax awareness. Also in cases of violations related to undeclared work and employment the offenders are encouraged to eliminate them already during supervision, with which they achieve the primary purpose of supervision, i.e. legalization of employment, performing of work or activities. Joint actions of supervisory authorities have also a preventive effect on prevention of grey economy, which includes also undeclared work and employment. Other preventive measures include also extensive informing via the website and the media, informing takes place about negative consequences in connection with rights from the obligatory health insurance, compensation for sick leave, deprivation of rights related to the employment relationship, deprivation of severance pay, pay for annual leave, reimbursement for meals during work and commuting, at losing jobs there is no entitlement to unemployment benefit, the work performed is not included into the period of employment nor pensionable service and earnings.

### ***Introduction of fiscal cash registers and influence on undeclared work and employment***

In 2016 fiscal cash registers were introduced in Slovenia. On the basis of data on fiscally verified invoices and data about individuals (cashier, operator), who have issued the invoice, cases of undeclared employment may be established.

Introduction of fiscal cash registers has several positive effects. One of them is evident also on the base of increased entries into the social security insurance, which has resulted in increased payments of social security contributions and personal income tax on income from employment. A part of these entries is a consequence of the fact that the Slovene Financial Administration supervises also undeclared work and employment with the assistance of data within fiscal tax registers because the invoice shall include the data about the invoice issuer – cashier.

As an indirect effect we may take also data into consideration about persons, who have entered into the social security system for the first time. In the first ten months of 2016 there were 46,836 persons registered for the first time at 15,311 employers at taxpayers, who use fiscal cash registers. Out of this number there are 24,569 newly registered persons, who issue invoices (cashiers).

### ***Penalties and sanctions***

The ZPDZC-1 states fines for undeclared work from EUR 2,000 to EUR 26,000 for legal persons and sole traders and from EUR 1,000 to EUR 7,000 for individuals – moonlighters.

Undeclared employment shall be fined from EUR 5,000 to EUR 26,000 for employers, who are not individuals, when they employ illegally. The fine from EUR 500 to EUR 2,500 is also prescribed for individuals, to whom employers enable work without conclusion of employment contracts or other civil-law contracts, on the basis of which work may be performed. If the work is performed on the basis of the civil-law contract, the fine prescribed for individuals is from EUR 100 to EUR 2,500 in cases when they don't have contracts on the spot where they perform the work all the time.

Additional obligations, which shall be fulfilled in cases of violations established in supervision, are prescribed for employers, who enable work to individuals, with whom they have no concluded employment contract:

- They shall conclude full-time employment contracts for an indefinite period of time with these persons and register them in social insurance and
- They shall pay all obligations related to the employment relationship for the period of the whole undeclared employment. If it is not possible to establish the

period of employment, it shall be deemed on the basis of law that the person has been in undeclared employment for three months.

In cases when the supervisory authorities establish undeclared employment of citizens from third countries, additional sanctions or limitations are prescribed for employers, to whom fines are finally imposed for these offences, as follows:

- They shall be excluded from the procedures of public procurement or the right to public funds is limited to them, including funds of the European Union, for the period of five years after the offence decision is final (employers with the negative reference); and
- They shall return public funds, including funds from the European Union, paid in the period of twelve months before preparation of the first record of the supervisory authority until the imposed fine for the offence is final.

Deportation conducted by the Police is envisaged as the secondary sanction for citizens of third countries illegally employed in the Republic of Slovenia, which means that this person is illegally located on the territory of the Republic of Slovenia.

The ZPDZC-1 defines also joint and several liability for the main contractor and intermediary sub-contractors in cases if employers, who have illegally employed persons, are subcontractors. In these cases the main contractor and all intermediary subcontractors are jointly and severely liable for possible outstanding liabilities related to the employment relationship for the time of undeclared employment if they have known that employers have illegally employed those persons.

At supervision over undeclared work and employment the measure is also applied for prohibition of performing of activities and sealing the business premises, which is one of the most severe measures, used by the supervisory authority in cases when this is absolutely necessary due to prevention of further violations, failure to comply with prior prohibitions, due to health hazard and also other circumstances.

In cases of the most severe violations the Slovene Financial Administration shall submit criminal charges due to suspicion of criminal acts of undeclared employment in accordance with Article 199 of the Penal Code (Official Journal of the RS, No. 50/12 – Official consolidated version, 6/16 – corr., 54/15 and 38/16), which is submitted when suspects in conflict with regulations employ two or more workers and they fail to enter them into the appropriate insurance or they employ several foreign persons or persons without citizenship without proper permits for work. Severe penalties are envisaged in cases of, for example, especially exploitative work conditions or exploitation of victims of human trafficking.

### **2.3.3 Good practice**

One of the most important examples of good practice is improved cooperation between many authorities responsible for identifying, tackling and/or preventing UDW. This was emphasised by the majority of those authorities in their reports. The implementation of the new legislation and the transfer of major responsibilities for identifying and/or preventing UDW to Financial Administration of Slovenia (FURS) enabled utilisation of FURS's mobile units in identifying and preventing UDW and UDE. It also increased the effectiveness of the inspections and control in the field.

Preventive activities or raising awareness at people through various media have an important role in prevention of undeclared work and employment.

### **2.3.4 Challenges and barriers**

The majority of authorities that perform inspections report that they are understaffed.

Another important challenge is the attitude of the Slovenian population about the acceptance of illegal activities and perception of how widespread they are in the Slovenian society. According to the Eurobarometer 402 (Eurobarometer 402, 2014), the level of risk of being detected in Slovenia is the lowest among all EU countries – only

14% of Slovenian respondents said that there is high risk of being detected by tax or social security institutions in the case of not declaring income.<sup>358</sup>

In this part public awareness activities shall be continued about the consequences of undeclared work and employment and about activities of supervisory authorities.

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<sup>358</sup> EU Commission (2014), Undeclared Work in the European Union, Eurobarometer Special Survey 402, Internet: [http://ec.europa.eu/public\\_opinion/archives/ebs/ebs\\_402\\_en.pdf](http://ec.europa.eu/public_opinion/archives/ebs/ebs_402_en.pdf)



## Factsheet on Undeclared Work – SPAIN (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

There is **not a legal definition of undeclared work** in Spain comparable to the EU's (COM(98) 219) or OECD's. The law states the obligation for employers to register job contracts with Social Security and pay the corresponding monthly Social Security contributions; there is an obligation for self-employed to register with Social Security as well; and for workers to declare to the Tax Agency (*Agencia Tributaria*) their work incomes. Thus, *de facto* undeclared work in Spain is defined as the payment or reception of a monetary remuneration without declaring it to the Treasury, or making the compulsory registration and payment with Social Security. Self-employed workers must register with Social Security when they carry out a 'usual' activity as professionals, with Supreme Court case law determining on several occasions the extent and meaning of 'usual'. Alternatively, an activity would be considered as 'usual' if it provides the self-employed worker more than the annual amount of the minimum wage.

#### 2.1.2 Characteristics of undeclared work

The **main types of undeclared work in Spain** are (Foundation, 1 May, 2011)<sup>359</sup>: companies or workers not registered with Social Security; foreign workers without a working permit; workers who work while receiving unemployment or other social benefits; full-time jobs declared as part-time jobs; envelope wages; and unpaid or non-declared extra hours. In addition, other forms of work that, although declared, do not fully comply with labour regulations, are: illegal application of employment incentives (rebates to Social Security contributions when hiring certain collectives); and illegal use of certain types of working contracts, such as volunteering or traineeships.

There is a clear **sectoral concentration of undeclared work**. According to the Labour and Social Security Inspectorate (*Inspección de Trabajo y Seguridad Social*), more than 80% of undeclared work detected in 2015 was found in four economic sectors: hospitality and restaurants (34.4%); services (25.2%), of which: professional services (12.4%); education, healthcare, sport and free time services (10.4%). Retail trade (13.1%) and construction (7.5%). Agriculture accounts for 6.5% of cases.

Other sources of information showed that in household services, involving mostly women, over one-third of workers could be unregistered<sup>360</sup>. Other economic sectors with a high presence of undeclared work carried out at homes are the textile and the ICT sectors (Foundation, 1 May, 2011). The transport sector is also highlighted as having a high presence of undeclared work. Finally, according to Eurobarometer (2014), 33% of the goods and services purchased where the consumer had a good reason to believe that they included undeclared work were repairs or renovations at homes, car repairs (27%), and domestic activities (cleaning of houses, 11%).

Although undeclared work has been found **in companies of all sizes**, it has been reported to be more frequent in SMEs. In addition, a positive correlation has been found between the percentage of self-employed in the economy and the size of the shadow economy<sup>361</sup>.

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<sup>359</sup> Foundation 1 May (2011) (CCOO Trade Union). '*El trabajo no declarado en España*' (Undeclared Work in Spain).

<sup>360</sup> Comparing the 650 000 persons employed, according to the LFS 2014, only 420 000 persons registered in the Special Regime for Household workers.

<sup>361</sup> Gestha (Trade Union of economists of the Treasury) and Jordi Sardà (University Rovira i Virgili) (2014). '*La economía sumergida pasa factura. El avance del fraude en España durante la crisis*' (The costs of the shadow economy. The growth of fraud in Spain during crisis).

**As for the main motivators for undeclared work**, in the case of low-qualified self-employed workers, the inability to afford taxes and Social Security contributions plays a key role. The bureaucratic complexity is another motivation among self-employed workers. In contrast, in the case of high qualified self-employed workers the motivation for tax evasion can be considered as more relevant. However, several studies show no conclusive evidence to consider the overall tax level as a cause of the shadow economy<sup>362</sup>. Other motivations are the reduction of administrative and bureaucratic costs; the possibility to evade regulations (health, safety, urbanism, etc.); the need for higher organisational and productive flexibility, including higher geographical mobility; or lower labour unitary costs<sup>363</sup>. **From the employees' side**, according to Eurobarometer (2014)<sup>364</sup>, the main reasons for not declaring work included, the lack of regular jobs in the labour market (45% of respondents); salaries in regular business being too low (23%); and the lack of controls (28%). From the **consumers' side**, the price is one key motivator for 59% of respondents when asked 'what made you buy it undeclared instead of buying it in the regular market?' (Eurobarometer (2013), a figure similar to EU 27, at 60%, and 5pp higher than in 2007). The second reason argued was to help someone in need (27%), 17pp higher than in 2007. Finally, the **economic crisis** has also been observed as a factor<sup>365</sup>; in the period before the crisis (2004-2007) the figures for the shadow economy are lower than for the period 2008-2011. However, there is a counter argument to this motivation: undeclared workers do not bear dismissal costs, so that companies would have dismissed first undeclared rather than formal workers to adjust to the reduction of demand caused by the crisis, and thus reduce the overall weight of undeclared work. Indeed, according to the method based on the comparison between LFS and adjusted Social Security registration figures, undeclared work would have diminished by 313,000 persons between 2008 and 2014<sup>366</sup>.

### 2.1.3 Estimated scale of undeclared work

There is not a consensus on the estimated scale of undeclared work in Spain and the available estimates differ widely. The first estimate was made by Ruesga (1984), with a figure of undeclared work for 1980 between 9.3% and 11.3% of the active population<sup>367</sup>. With a similar, although adjusted methodology<sup>368</sup>, undeclared work in Spain would have reached 561,400 workers, 3.2% of total employment, in Q2/2014<sup>369</sup> (218,400 Spanish and 343,000 foreign workers).

Gestha and Sardà (2014)<sup>370</sup> estimate the shadow economy at 23.1% of GDP in 2012 combining several sources<sup>371</sup>, stating a wide geographical dispersion behind these

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<sup>362</sup> Randstad study (2014) shows a correlation of  $R^2 = 0,1373$  between the shadow economy and corporate tax level across OECD countries. Gestha and Sardà (2014) arrive at a similar conclusion.

<sup>363</sup> Santos M. Ruesga, '*Economía sumergida y fraude fiscal*'. Actualidad Tributaria, 30 septiembre 1994. Quoted by Foundation 1 May (2011).

<sup>364</sup> Special Eurobarometer 402 (2014). Undeclared Work in the European Union.

<sup>365</sup> Gestha and Sardà, 2014, op. cit.

<sup>366</sup> Calculation based on figures from INE. Labour Statistics Working Group. 'Comparison between employment statistical magnitudes according to LFS and affiliation data. Q2/2014'. May 2015.

<sup>367</sup> Ruesga, B. (1984), '*Economía oculta y mercado de trabajo: Aproximación al caso español*', Información Comercial Española. Revista de Economía, nº 607 (marzo).

<sup>368</sup> Based on the gap between the employment figures of the LFS and the affiliation to social security. The INE estimates take due account of the weight of certain groups (such as papal clergy or civil servants that are registered in a mutuality).

<sup>369</sup> Source: INE. Labour Statistics Working Group. 'Comparison between employment statistical magnitudes according to LFS and affiliation data. Q2/2014'. May 2015.

<sup>370</sup> Op. cit.

<sup>371</sup> Arrazola et al. (2011); Schneider, Büehn y Montenegro (2010); B a F. Schneider (2011); Schneider, AT Kerney, by VISA (2013) 'The Shadow Economy in Europe'; Pickhardt, M. and J. Sardà (2011). 'Evolution and Causes of the Spanish Underground Economy', Mimeo; Ruesga,

figures. The study of FUNCAS (2011), assuming the same productivity for undeclared work as for the formal economy, and based on LFS values and three models for the estimation of the shadow economy (monetary, energy and MIMIC), estimates around 4 million undeclared work jobs in the period 2005-2008<sup>372</sup>. On its side, the study of the Foundation of Financial Studies on the Shadow Economy in Spain (2013)<sup>373</sup> estimates a figure of around 1 million undeclared jobs based on the estimate of the shadow economy linked to undeclared work made by Gestha and Sardà<sup>374</sup> (EUR 82,500 million) and a productivity per worker of EUR 61,200 (EC, 2012).

## 2.2 Institutional Framework

### 2.2.1 Responsibilities for addressing undeclared work

In Spain undeclared work involves two frauds, one in terms of Social Security contributions and another in terms of taxes. Thus the key authorities with responsibilities for identifying and tackling undeclared work are: the Labour and Social Security Inspectorate (*Inspección de trabajo y seguridad social*); the Social Security Treasury (*Tesorería General de la seguridad social*), responsible for collecting the Social Security contributions; and the Tax Agency (*Agencia Tributaria*).

### 2.2.2 Characteristics of the responsible organisations

The **Labour and Social Security Inspectorate** belongs to the Ministry of Employment and Social Security (MEYSS) and is a national body. The body had 960 inspectors and 840 sub-inspectors in 2015 (adding 1,800 workers), plus 1,231 additional administrative workers. This figure has remained almost constant since 2009 (1,798 inspectors and sub-inspectors), despite the increase in undeclared work observed by some organisations<sup>375</sup>.

The total number of business units<sup>376</sup> registered with the Social Security in 2015 was 1,463,553 (excluding agriculture and domestic service regimes). This figure involves a ratio of 1.544 business units per inspector and 1.746 units per sub-inspector. In the same year, 371,887 business units of 304,413 companies were inspected, unveiling 87,068 infractions.

The amount of fines proposed by this body reached more than EUR 310 million. Regarding undeclared work, 193,562 inspections were carried out in 2015, unveiling 86,113 undeclared jobs (a figure 21.7% higher than in 2010)<sup>377</sup>.

The **Social Security Treasury** is a national body managed by the MEYSS, the main role of which is to collect social security contributions at the national level. Thus the (lack of) registration of working activities in this body determines the border between declared and non-declared work in many cases. The body has 12,066 workers (December 2014) and a network of 203 administrative offices, 53 attention offices and 277 Units of Collection (*Unidades de Recaudación Ejecutiva*)<sup>378</sup>.

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S.M. y Carbajo, D. (2013). 'El "Tax Gap" en España: definición, estimaciones y medidas dinámicas para su reducción'. Mimeo.

<sup>372</sup> Funcas (2011). *La Economía Sumergida en España* (The Shadow Economy in Spain). María Arrazola, José de Hevia, Ignacio Mauleón, and Raúl Sánchez.

<sup>373</sup> Foundation of Financial Studies (2013). *La Economía Sumergida en España* (The Shadow Economy in Spain). Alfredo Jiménez Fernández, Ramiro Martínez-Pardo del Valle.

<sup>374</sup> Op. cit.

<sup>375</sup> Gestha and Sardà, 2014, op. cit.

<sup>376</sup> One company may have more than one business units (*centros de trabajo*), usually in several localities or regions.

<sup>377</sup> 2014 Annual Report. Inspection of Work and Social Security (*Memoria 2014 Inspección de Trabajo y Seguridad Social*). MEYSS.

<sup>378</sup> Memory of Activities of the Treasury of Social Security 2014.

The **Agencia Tributaria** holds the main function of collecting taxes across the country, with the exception of the Basque Region and Navarre, which have their own tax agencies. It is managed by the Ministry of the Treasury and Public Administration, and has 25,742 workers distributed across 193 public attention offices, 31 offices of customs and special taxes, and 17 councils of territorial coordination<sup>379</sup>.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

There has been constant cooperation between the Tax Agency and the social security over the years. The 2005 Plan of Prevention of Fiscal Fraud<sup>380</sup> already involved data exchange between both bodies about hiring/dismissal of workers by companies and salaries paid. Later, the renewal of this plan (2008) included other cooperation models such as the exchange of data with the registry of subcontracting companies of the MEYSS and the coordination of actions with the Treasury of social security to tackle the shadow economy. In addition, the 2010 Comprehensive Plan for the Prevention and Correction of Fiscal, Labour and against the social security Fraud (*Plan Integral de Prevención y Corrección del Fraude Fiscal, Laboral y a la Seguridad Social*) guided the cooperation between the Tax Agency, the Social Security Treasury and the Labour and Social Security Inspectorate. This cooperation is based on information exchange, shared training, the creation of permanent coordination channels<sup>381</sup> and joint actions, focusing on certain economic sectors and on the prevention of common practices in undeclared work, such as unpaid or non-declared extra hours, subcontracting, seasonal agrarian work, undeclared transport workers, extreme low-cost retail shops, full-time jobs under part-time contracts and fraud related to employment incentives. The plan also includes cooperation with Regional Governments and with the tax agencies of the Basque Region and Navarre<sup>382</sup>. Finally, the most recent Plan to fight irregular work and social security fraud (*Plan de lucha contra el empleo irregular y el fraude a la Seguridad Social*), of 2012, adds strengthened institutional cooperation between Social Security bodies, the Tax Agency, the Ministry of the Interior, the Fund for Salaries' Guarantee, the General Council of the Judiciary, the General Council of Notaries and the Real Estate Registers College. It has also set up an anonymous denouncement box on the MEYSS webpage.

There are other interesting fields of cooperation between bodies. According to the Law 23/2015 (Art 22.17), the Labour and Social Security Inspectorate can adopt several actions when the inspection finishes, such as reporting to the national PES to promote guidance and skill training of the workers found in undeclared or irregular work situations. In addition, there is a cooperation agreement between the Ministry of the Interior and the MEYSS (30 April 2013) to manage the support of police bodies to certain inspections performed by the Labour and Social Security Inspectorate. Police Forces supported 19,609 of the 193,562 inspections targeting undeclared work in 2015. According to the MEYSS, thanks to the mentioned Plan, 252,822 irregular jobs were detected in 2012-2014 with an impact of EUR 11.3 billion<sup>383</sup>.

The Labour and Social Security Inspectorate participates in working groups of the Senior Labour Inspectors Committee of the EU, so that the direct contact is frequent. The Spanish body has bilateral agreements with similar organisations in Portugal, Romania, France and Poland. Every year there is a meeting between the Portuguese and the

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<sup>379</sup> Source: Agencia Tributaria.

<sup>380</sup> Source: Agencia Tributaria

([http://www.agenciatributaria.es/AEAT.internet/Inicio/La\\_Agencia\\_Tributaria/Planificacion/Plan\\_de\\_Prevencion\\_del\\_Fraude\\_Fiscal/Plan\\_de\\_Prevencion\\_del\\_Fraude\\_Fiscal.shtml](http://www.agenciatributaria.es/AEAT.internet/Inicio/La_Agencia_Tributaria/Planificacion/Plan_de_Prevencion_del_Fraude_Fiscal/Plan_de_Prevencion_del_Fraude_Fiscal.shtml))

<sup>381</sup> *Mesa para la Prevención y Corrección del Fraude Fiscal y a la Seguridad Social* (Working group for Prevention and Correction of Fiscal Fraud).

<sup>382</sup> In Spain there is a national tax agency (*Agencia Tributaria*) plus four regional departments, in the three Basque Country provinces and in the Navarre region.

<sup>383</sup> Source: La Moncloa (press release 13 March 2015):

<http://www.lamoncloa.gob.es/consejodeministros/Paginas/enlaces/130315enlacetrabajo.aspx>

Spanish Inspectorate bodies to strengthen cross-border cooperation and to plan coordinated actions regarding undeclared work.

## 2.3 Policy Focus and Measures

### 2.3.1 Policy approach

The policy approach in Spain to tackle undeclared work has been traditionally one of deterrence, implemented through inspections by the mentioned bodies. Over the last years though, certain measures suggest a gradual growth of a complementary enabling/preventative approach. An example of these measures are the employment incentives (rebates to Social Security contributions for some collectives) and the significant reduction of Social Security contributions for self-employed workers<sup>384</sup>. Other examples can be found in the already mentioned Comprehensive Plan for the Prevention and Correction of Fiscal, Labour and Social Security Fraud of 2010, that includes an awareness campaign about the effects of fiscal fraud; collaboration agreements with business associations, which involve the provision of information by these organisations on a voluntary basis. The plan also includes the facilitation of bureaucratic procedures through ICT (fully operative), also to reach persons in remote areas.

### 2.3.2 Measures to tackle undeclared work

**The Plan to fight undeclared work and Social Security Fraud** (*Plan de lucha contra el empleo irregular y el fraude a la Seguridad Social, 2012-2013*) includes the mentioned improved coordination among different public bodies; reorganisation and increase of human resources of the Labour and Social Security Inspectorate<sup>385</sup>; new inspection campaigns in sensitive sectors; follow-up of undeclared work cases and areas; and several law modifications. Among these is the Law 13/2012 of 26 December, on the fight against irregular employment and Social Security fraud, and the Organic Law 1/2015, that modifies the Penal Code (Organic Law 10/1995). They include the extension of the prescription period of crimes against Social Security from 5 to 10 years; the request of paying the evaded amounts to skip penal responsibilities; tighter controls to prevent the reception of unemployment benefit while working; and an increase of fines.

In addition, an **online mailbox** has been created (August 2013) to receive anonymous reports about undeclared work or shadow economy situations: up to December 2016, it had registered 195,912 communications and led to 31,631 inspections, of which 23,750 were finalised. The creation of an **Office Against Fraud** has also been announced (Law 23/2015, July), although not yet created.

Finally, as a curative measure, on May 2011, a Royal Decree (5/2011) granted an **amnesty for undeclared workers**, allowing employers to register any undeclared employee until 31 July 2011 with no penalty and backdated Social Security contributions. The decree also increased substantially the sanctions from 31 July 2011 onwards<sup>386</sup>.

Since the approval of the Plan to fight undeclared work and Social Security fraud, 252,822 undeclared jobs have been detected (2012-2014). This, together with other irregularities detected, has provided an additional EUR 11.3 billion to the Treasury during the three mentioned years<sup>387</sup>. Regarding the Labour and Social Security Inspectorate actions, as mentioned above, the body accounted for 1,800 inspectors and

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<sup>384</sup> These reductions reach 80 % during the first six months, 50 % for the six following ones and 30 % for the last six months.

<sup>385</sup> The plan states to increase the staff in 50 inspectors and 63 sub-inspectors, which involves a growth of about 5 %.

<sup>386</sup> Eurofound (2013): Tackling undeclared work in 27 European Union Member States and Norway. Approaches and measures since 2008

<sup>387</sup> Source: La Moncloa (press release 13 March 2015):

<http://www.lamoncloa.gob.es/consejodeministros/Paginas/enlaces/130315enlacetrabajo.aspx>

sub-inspectors in 2015, who performed 193,562 undeclared work inspections and identifying 87,068 undeclared jobs.

### 2.3.3 Good practice

The reduction in Social Security contributions for new self-employed workers can be considered a good practice of a preventative approach, since the measure facilitates a smooth transition into self-employment and the beginning of entrepreneurial activities in the formal economy. This has been strengthened by another measure that can be considered as a good practice as well: the allowance to receive 100% of the contributive unemployment benefit for unemployed workers that shift to self-employment. Particular stronger entrepreneurship incentives had been approved for young people, which have now been extended to all self-employed (Law 31/2015).

### 2.3.4 Challenges and barriers

One key challenge is to achieve **a clear definition of undeclared work at the legal level**. At present, part-time self-employment is not foreseen and the minimum amount of contributions to pay is set at EUR 267.04 every month (regardless the income achieved that month), which reaches 35% of the minimum wage (EUR 764.40 per month, 12 months a year). Thus this system involves an evident barrier for part-time or low income self-employed workers. There is a current debate among several political parties to reform the Social Security fees for low-income self-employed workers.

In addition, there are **challenges in specific sectors**. Another important challenge remains in the **domestic service** and the care provision sector, where over one-third of employees may be undeclared. In addition, there is a social awareness challenge in this sector, as, according to Eurobarometer (2014), in Spain 18% of the population finds it fairly acceptable and 8% total acceptable to do undeclared work for household work. The **agriculture** sector gathers an important share of undeclared work among irregular immigrants, which is difficult to combat due to their unwillingness to denounce it.

There is a need to **increase the resources of the Labour and Social Security Inspectorate**. Moreover, according to Eurobarometer (2014), 58% of respondents in Spain consider the risk of being detected in undeclared work as 'small'.

## Factsheet on Undeclared Work – SWEDEN (September 2017)

### 2.1 Nature and Estimated Scale of Undeclared Work

#### 2.1.1 Definition of undeclared work

The term “undeclared work” (UDW) is defined as “any paid activities that are lawful as regards their nature but not declared to the public authorities”.<sup>388</sup> In Sweden the term “svartarbete” (“black work”) is also used frequently, and should be interpreted as a synonym to UDW.

Key organisations with an interest in UDW in Sweden, namely the Swedish National Audit Office (*Riksrevisionen*) and the Swedish Tax Agency (*Skatteverket*), use UDW as a concept distinct from tax avoidance of income from unlawful activities such as smuggling, prostitution and trafficking/trade in stolen goods.

#### 2.1.2 Characteristics of undeclared work

The Swedish Tax Agency divides UDW (or black work) into two broad categories: (1) Undeclared income from employment and (2) undeclared income from self-employment.<sup>389</sup> The form of undeclared payment in these two categories can be separated into four distinct groups:

- Employees receiving undeclared pay in money or in kind from employers
- Self-employed individuals obtaining undeclared compensation for work or sales of goods
- Employers paying the employee’s private expenses (goods, travel, loan of equipment) and not recording it as a taxable salary benefit
- The firm’s business account being loaded with private expenses that reduce taxable profits.

In a survey conducted by the Swedish Tax Agency (2006), UDW was most frequently found in the sectors covering fishing, agriculture, forestry, restaurants, hairdressers, taxis, car servicing, and cleaning of business premises and other personal services. In these sectors UDW was estimated to be above 15 per cent of total income. The sectors where the income from UDW was between 5 and 15 per cent of total income included education and health care (excluding the public sector), construction industry, rental and company services, road transport of goods, grocery stores, other wholesale and retail, and hotel, camping sites, etc. Because of the large size of these sectors, the greatest amount of income from UDW in absolute figures were found in rental and company service companies, retail stores and in the construction industry.<sup>390</sup>

Income from UDW in registered companies was estimated by the tax authority to be EUR 7.9 billion, where the main sectors were company service (EUR 1.5 billion), retail stores (EUR 0.9 billion) and the construction industry (EUR 0.7 billion).<sup>391</sup> Income from registered and unregistered companies that cannot be tax audited were estimated to EUR 0.6 billion. Based on a survey by the Swedish Tax agency in 2005, 30% of this income originated from work in restaurants, 13% from sales, cashiers and shop, and

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<sup>388</sup> Anxo, D. (2007), Update of thematic article on “undeclared Work” Sweden, European Employment Observatory, May 2007,

Storrie, D. (2004), Undeclared work in Sweden, in *European Employment Observatory Review, Autumn 2004*, Fighting the immeasurable? Addressing the phenomenon of undeclared work in the European Union, Employment and Social affairs, European Commission, Brussels.

<sup>389</sup> The Swedish Tax Agency (2006), Purchasing and performing undeclared work in Sweden, Part 1: Results from various studies, Report 2006:4B

<sup>390</sup> op. cit.

<sup>391</sup> op. cit.

8% from construction, painting, demolition etc.<sup>392</sup> Furthermore, households' purchase of UDW was estimated to EUR 1.1 billion (EUR 0.6 billion from work on homes and EUR 0.5 billion on other household work than on homes). Some UDW can be derived from purchase of goods (EUR 0.3 billion), where beverages (13.5%), agricultural products (15.5%) and building materials (3.3%) constituted the largest shares. The Swedish Tax Agency estimated that there was EUR 2.8 – 3.3 billion of income from UDW with unknown origin.

According to the same report by the Swedish Tax Agency,, 85 per cent of the income from UDW originated from small companies with annual wage costs of less than SEK 1 million (EUR 110,000), 11 per cent from limited companies with total wages between SEK 1 and 5 million (EUR 110,000 – 560,000), and larger limited companies and other sectors accounted for 4 per cent.

The main motivators for undeclared work in Sweden varied by individual. A survey by the Swedish National Audit Office found that students, self-employed and blue-collar workers are performing most of the UDW.<sup>393</sup> Students have a strong incentive to hide their extra earnings as their public subsidised study-loans are conditioned on a low income from work. As expected, self-employed and blue-collar workers have a significant higher share of UDW than white-collar workers, as incomes from UDW are mainly found in construction and other services.

A common type of UDW is where self-employed individuals obtain undeclared compensation for work performed in households, to avoid the tax wedges created by the households' payroll taxation.

Increasing labour migration also creates a substantial risk of UDW, in particular in the construction sector. The Swedish National Council for Crime Prevention (*Bråttförebyggande rådet - Brå*) states that UDW is common among subcontractors in the construction sector, where employers avoid paying social security contributions and payroll taxes, and false invoices hide payments in cash.

### **2.1.3 Estimated scale of undeclared work**

An indirect method to measure UDW is the use of Discrepancy methods, where Statistics Sweden estimates Gross Domestic Product (GDP) based on total consumption, investment and exports. The difference between this calculation of GDP and the calculation of GDP which is based on the total reported national incomes provides an estimate of how much of the national incomes that are not reported in the tax declarations of households and firms. This difference provides an overall picture on the total amount of UDW, which is estimated to be around 5 per cent of the Swedish GDP.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

The Swedish Tax Agency (*Skatteverket*) is the central government authority that administers the Swedish tax system. It is accountable to the government, but operates as an autonomous public authority. If a taxation crime is detected, the case will be transferred to The Swedish Economic Crime Authority (*Ekobrottsmyndigheten*) which has the exclusive mandate to investigate and prosecute tax and bookkeeping crimes. The Social Insurance Agency (*Försäkringskassan*) controls the rights to obtain social benefits and reports suspected UDW amongst people receiving social benefits. The work against crimes is supported by the Swedish National Council for Crime Prevention (*Brottsförebyggande rådet - Brå*) which also is responsible for the official crime statistics.

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<sup>392</sup> The estimations were based on 2,232 telephone interviews of a random selection of individuals 18-74 years old. (The Swedish Tax Authority, 2006)

<sup>393</sup> The Swedish National Audit Office (1998), *Illicit work in Sweden, a report on a welfare state dilemma*, Riksrevisionsverket RRV 1998:61, Stockholm



Branch organisations and trade unions in various sectors of the economy, in particular construction, also have a role to play and co-operate with the authorities to raise awareness of UDW.

The Swedish Work Environment Authority (*Arbetsmiljöverket*) is an authority mandated by the government and the Swedish Parliament to control laws about the work environment and working hours are followed by companies and organisations.

The Swedish National Audit Office (*Riksrevisionen*) is part of the central control power of the Swedish Parliament (*Riksdagen*). The authority ensures that the Parliament receives a coordinated and independent audit of the state finances, and is the only body that can audit the entire state finances.

Specific responsibilities held by each organisation regarding UDW are set out below. The Minister of Finance decides on the political priorities regarding the taxation system and delegates authority to individual agencies. The government thus set out the tasks and goals for the agencies, as well as their budgets and how the resources are allocated between different activities. It should, however, be noted that the Swedish constitution does not allow ministers in the Swedish government to intervene in an agency's decisions in specific matters relating to the application of the law or the due exercise of its authority.

The Swedish Tax Agency audits the tax declarations of both private individuals and legal entities, and analyses and reports to the government on the function and performance of the Swedish Taxation system. A large part of the received knowledge about UDW in Sweden is produced by the Swedish Tax Agency.

The Swedish Economic Crime Authority investigates and prosecutes tax crime and bookkeeping crime. The authority also takes the initiative in promoting cooperation between authorities, and proposes changes in statutes to make the fight against economic crime easier and more effective.

The Swedish National Council for Crime Prevention is a government agency that works to reduce crime and increase safety in society by producing data and disseminating knowledge on crime and crime prevention. The agency also produces the official crime statistics, evaluates reforms, conducts research to develop new knowledge and supports local crime prevention work.

The Social Insurance Agency administers the Swedish social insurance system and pays social benefits to families with children, and to people with sicknesses and disabilities. They also control the person's entitlements to social benefits.

The Swedish Work Environment Authority is in charge of monitoring whether the provisions in the Work Environment Act are respected. The Swedish Work Environment Authority produces legally binding provisions, inspects workplaces and disseminate information about work environment regulations.

The Swedish National Audit Office is tasked with controlling and evaluating how government policies, including those to decrease UDW, have been executed and to evaluate the results. The authority publish reports that are publicly available and which critically and independently analyse the performance of the government bodies.

### **2.2.2 Characteristics of the responsible organisations**

The Swedish Tax Agency has 10,370 employees distributed across seven regional offices, and administers matters pertaining to public records, property tax and estate inventories. They also undertake criminal investigations and issue ID cards. During 2014, the authority conducted 5,792 inspections of staff registers, 13,799 inspections of cash registers, and conducted 23,583 other company visits.<sup>394</sup>

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<sup>394</sup> Annual data from the Tax Statistical Yearbook of Sweden

The Swedish Economic Crime Authority is organised into ten public prosecution offices and five regional police operational units. The police operational units deal with criminal intelligence, investigation and reconnaissance as well as the analysis of crimes within the IT sector. Approximately 560 people work at the agency, comprising approximately 100 prosecutors, 70 civilian investigators, 60 administrators and 230 police officers. In 2015, the number of reported crimes related to tax regulation was 14,458 (where 29% lead to prosecution). Fraud against social insurance and unemployment benefits was reported 8,726 times (46% prosecution of fraud against social insurance and 33% prosecution of fraud against unemployment benefits). Accounting offences were reported 14,641 times (48% prosecution).<sup>395</sup>

The Swedish National Council for Crime Prevention is situated in Stockholm with approximately 100 employees including criminologists and lawyers, statisticians and software developers.

The Social Insurance Agency, with approximately 13,400 employees, is one of the largest Swedish government agencies. The agency has the mandate to investigate, decide and pay grants and social insurance benefits. The agency is organised into 60 local insurance centres and 20 regional centres.

During 2015 the Swedish Work Environment Authority inspected more than 13 500 work places. They are based in 11 offices across Sweden, with a central head-office based in Stockholm, and have almost 550 employees.

The Swedish National Audit Office was formed in 2003 after a constitutional change to establish a coherent audit authority for the parliament. The agency has around 340 employees.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

The Swedish Economic Crime Authority targets its preventive work mainly on three groups: school children, entrepreneurs and new groups in the labor market, and often participates in events and conferences that involve these groups. The cooperation has also involved branch organisations and trade unions in various sectors of the economy, in particular the construction sector.

The Construction Industry in Collaboration (*Byggbranschen i Samverkan*), a joint organisation featuring employers and trade unions in the construction sector, are running a project "Clean Construction Industry". The target groups for this project are students / teachers in secondary schools' vocational programmes, college and universities, as well as the industry and the public. This campaign aims to change attitudes towards UDW in the construction sector. The Swedish Economic Crime Authority and the Swedish Tax agency have contributed to this project by participating in a film designed to combat illegal work in the construction industry.<sup>396</sup>

In terms of data exchange between agencies, the Swedish Economic Crime authority, in cooperation with other authorities (Åklagarmyndigheten, Rikspolisstyrelsen, Tullverket, Skattemyndigheten, and Kronofogdemyndigheten) has formed a joint-national authority specialist function on exchanging information related to economic crime (*Myndighetsgemensam nationell specialistfunktion för brottsutbytesfrågor*). However, there is no available evidence of the effectiveness of cooperation around information exchange.

For the period 2015-2018, the Government has instructed the Swedish Work Environment Authority to increase its monitoring and control of companies that are violating health and safety regulations to gain competitive advantage. This mandate

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<sup>395</sup> The Swedish National Council for Crime Prevention (*Bråttförebyggande rådet - Brå*), annual data.

<sup>396</sup> Available at [www.renbyggbransch.nu/ny-film-sa-far-vi-en-ren-byggbransch\\_\\_70](http://www.renbyggbransch.nu/ny-film-sa-far-vi-en-ren-byggbransch__70)

also includes increased collaboration with other Swedish agencies, as well as consultations with the social partners, in order to develop information campaigns specifically targeted at sectors and companies with high rates of UDW.

The Swedish Work Environment Authority will also be Sweden's representative at the EU forums on undeclared work. The authority has been involved in a collaborative project funded by the Commission regarding the exchange of experience of the implementation of the Posting of Workers Directive. It is hoped that this, as well as other future collaborations, should increase knowledge on UDW in the communities, and how UDW is dangerous for both individuals and the society as a whole. In terms of cooperation and collaboration between other Member States, the Swedish Council for the protection of the European Union's financial interests, also known as the SEFI Council, is responsible for coordinating measures in Sweden to combat fraud and other improper use of EU-related funds.

The European Anti-Fraud Office, OLAF, work to protect the EU's financial interests against unlawful activities. The Office may carry out administrative investigations in EU member states and also in countries outside the EU, as well as internal investigations within EU institutions and bodies. OLAF investigates EU fraud, prepares legislation to protect the Community's financial interests and represents the European Commission in anti-fraud matters.

The Swedish Economic Crime Authority is part of the Advisory Committee for the Coordination of Fraud Prevention (COCOLAF) along with the Ministry of Finance and, like Swedish Customs, is the Swedish contact authority for OLAF. The Swedish Economic Crime Authority has national responsibility for cases of fraud if the act relates to the EU's financial interests and the improper use of subsidies.

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

Concerted efforts to raise social awareness of UDW have been undertaken through joint information campaigns by the tax authorities and the Economic Crime Authority (*Ekobrottsmyndigheten*). This co-operation has also involved branch organisations and trade unions in various sectors of the economy, in particular the construction sector.

In recent years, greater attention has been paid to the incentive structure of the labour market in explaining the relative deficit of employment growth in Sweden, in particular in personal services. Social transfers, taxes and non-labour costs may, either separately or jointly, raise barriers and disincentives affecting the growth of service activities, in particular personal services. It has been argued that a high tax wedge restricts consumer demand for household related services, limiting job creation, favouring UDW and leading to inefficient resource allocation within the household and in the whole economy.

One central measure in this context is the "ROT" tax deduction, introduced between April 2004 and June 2005 to address the issue of UDW related to the repair of dwellings. The tax deduction applied to those who build or repair their dwelling. A further step was taken in 2007, when the government announced a tax deduction for household related services ("RUT"), related to, for example, cleaning, care of children, elderly and disabled individuals, and gardening. The tax deduction allows a reduction of 50% of labour cost up to a ceiling of 50,000 SEK per year and household.

A regulation on reversed charges of value added tax (VAT) for the construction sector was introduced in 2007, with the explicit aim of reducing tax evasion. In Sweden VAT is normally paid by the seller of commodities and services and included as a part of the market price. From 1 July 2007 reverse VAT was introduced in the construction sector to impede fraud where buyers of services make a deduction of VAT, but where the seller does not pay the VAT to the State. The seller is often a subcontractor that supplies untaxed labour by charging labour costs as a cost of material.

The Government has also emphasised the need for reforms stimulating and facilitating entrepreneurship and business development. This is especially regarding SMEs for which the present rules and regulations, including those related to the tax system, are described as too complicated and present significant obstacles to the creation and development of small scale firms.

Concerning preventive actions against UDW, from 1 January 2007, employers in high-risk sectors (restaurants and hairdressers) are required to keep a register of their staff. From April 1, 2013 laundries, and from 1 January 2016 the construction industry, are also included. As of 1 January 2010, businesses selling goods and services in return for cash payments must have a certified cash register. Statistics from the Swedish Tax Agency do, however, show that the reported VAT for restaurants rose by 7% and 11% in the hairdressing industry in 2010.<sup>397</sup>

### **2.3.2 Measures to tackle UDW**

The current regulations regarding tax deductions from services related to building and repair of dwellings (ROT) and household services (RUT) was changed 1 January 2016. The current ROT allows 30 per cent of labour costs to be deducted from taxation to a maximum of SEK 50,000 per year, while the RUT deduction allows 50 per cent of the labour costs to be tax deductible to a maximum of SEK 25,000 per year (For persons 65 years or older, the maximum amount is SEK 50,000). Furthermore, the sum of tax deductions in ROT and RUT cannot exceed SEK 50,000 per year. The supplier of services directly deducts labour costs on the bill to the customer, and then applies for a payment to the tax authority.

The tax deduction of services in the household (RUT) and building and repair of dwelling (ROT) is estimated to have reduced the purchase of UDW in cleaning services by 11 – 12 per cent<sup>398</sup>. (This could be an underestimation, since it is based on a survey where buyers of “white” services answer that they have previously bought “black” services. As pointed out in the report, households that did not buy cleaning services before, could have hired “black” services if there was no RUT).

The Swedish Tax Agency attempted to establish the degree of price sensitivity for renovation work by asking ROT buyers how they would have behaved if the tax deduction was not in place. 56% said they would have bought the service to the same extent, 21% would have done the job themselves, 19% had let the work to be undone, 9% would have used help from friends and relatives and only 6% would have bought black work.<sup>399</sup> There are obviously major methodological problems associated with this type of research, but the responses suggest that a large part of the services purchased with the ROT-deduction would not have come about without the tax deduction.

### **2.3.3 Good practice**

The Swedish policies to reduce households’ incentives to use UDW seem to have been successful:

- High tax wedges and low risks of detection have established a norm among Swedish households to use UDW in home repair and renovation. The introduction of the tax deduction for the labour costs for repair and renovation (ROT) has decreased the use of UDW and benefited the employment rate in the conventional (white) sector.

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<sup>397</sup> Eurofound (2013), Tackling undeclared work in 27 European Union Member States and Norway: Approaches and measures since 2008, Eurofound, Dublin.

<sup>398</sup> The Swedish Tax Agency (2011), “Om RUT och ROT och VITT och SVART”, Rapport 2011:1

<sup>399</sup> The Swedish Tax Agency (2011), “Om RUT och ROT och VITT och SVART”, Rapport 2011:1

- By extending the tax deduction to the sector of other household services (RUT), the use of UDW has further diminished and supported the creation of jobs in the household service sector.

#### **2.3.4 Challenges and barriers**

A part of the market for UDW features very low prices and is performed by illegal immigrants, so in this market segment there are other incentives than tax evasion. The illegal immigrants include three different categories of people: (1) Persons who come to Sweden as asylum seekers, but do not leave the country after a deportation notice; (2) Persons who come to Sweden with tourist or student visas and remain in the country after their visa has expired; and (3) Persons whose entry and stay in the country is completely unknown to the authorities. These people are usually living hidden in Sweden and are without social protection and access to medical care. Consequently, they are dependent on UDW, often with extremely low wages and poor working conditions. Qualitative studies based on interviews with illegal immigrants suggest that salaries can vary between SEK 20 and 74 (EUR 2 and 8) per hour, significantly lower than other groups participating in 'black labour'. The Swedish Tax Authority concluded that there could be at least 10 – 20,000 illegal immigrants in Sweden, with the majority earning their livelihood by UDW. A simple calculation results in an undeclared income of about SEK 0.7 – 1.4 billion (EUR 78 – 156 million) per year. As a comparison, total UDW is estimated to around SEK 200 billion (EUR 23 billion) per year (5 per cent of GDP).<sup>400</sup>

Steps taken to address these challenges include, in April 2016, government proposals to invest over SEK 500 million (EUR 56 million) in measures to help immigrants better integrate into Swedish society. Resources are also added to improve the skills mapping and validation of foreign qualifications to employment agencies, so employers can more easily get a picture of the individual's knowledge. A new fast track system for newly arrived entrepreneurs has also been launched.

Outstanding challenges include the influence of criminal activities related to UDW. UDW is often found in labour-intensive industries such as building, cleaning, catering and transport, and several authorities have paid attention to criminal actors within these industries and procurement by organised criminal networks. The Swedish Economic Crime Authority points out that there is a high and continued risk that foreign labour and vulnerable people are increasingly used as UDW by these criminal networks.<sup>401</sup>

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<sup>400</sup> op. cit.

<sup>401</sup> The Swedish Economic Crime Authority (2014), "Ekobrottsmyndighetens lägesbild 2014", September 2014, Ekobrottskansliet, EBM A-2014/0435

## **Factsheet on Undeclared Work – UNITED KINGDOM (September 2017)**

### **2.1 Nature and Estimated Scale of Undeclared Work**

#### **2.1.1 Definition of undeclared work**

In the United Kingdom, undeclared work (UDW) is associated with the 'shadow economy' or 'hidden economy', and the terminology often depends on the focus of the different interest groups (as described in Section 1.2.1 below). Her Majesty's Revenue & Customs (HMRC) refers to the hidden economy as a: 'source of income earned from the sale of good or services, which have not been declared for tax purposes'<sup>402</sup>. Therefore, from the national perspective the perceived damage caused by UDW is a combination of financial and welfare considerations. In the case of the former, the gross losses are usually the focus of attention, without much attention paid to the net losses. While UDW may lead to lower income tax receipts, the cash payments received by workers in the shadow economy are likely to be ploughed back into the economy generating VAT and other taxes down the line. Similarly, those receiving illicit pay may mean that they are less reliant on welfare payments.

The UK is acknowledged to have one of the lowest rates of UDW in the EU and has had considerable success in reducing the tax gaps and HMRC and the Department for Work and Pensions (DWP) have also been successful in tackling fraud and error in benefit payments. Also, the UK has been innovative in its approach to tackling all forms of worker exploitation and is at the forefront of legislative change, for example introducing a Modern Slavery Act in 2015, the first of its type in Europe.

#### **2.1.2 Characteristics of undeclared work**

In the UK the key activities that contribute most to the extent of UDW are:

- Second job holders where the secondary activity is hidden;
- Those workers and businesses fully hidden in the shadow economy; and
- Illegal migrants working in the shadow economy.

A significant proportion (there is no reliable measure of its scale) of UDW is done by those already working in the formal economy. HMRC has identified self-employed as a key group where undeclared transactions take place, especially where the main method of payment is cash. This is partly to do with the self-assessment tax system that applies to this group, where an annual self-declaration is required. For employees, the biggest tax take, income tax, is paid through the PAYE (Pay-As-You-Earn) system where tax due is deducted at source by the employer.

HMRC investigations<sup>403</sup> show that the self-employed are the most likely group to be operating in the hidden economy, especially where cash payments are the norm (in sectors such as construction, personal services and retail). The rapid growth in Internet trading has posed new problems of regulation for the government in the form of undeclared transactions (often on internet auction sites) which may avoid VAT, as well as sellers choosing to not register leading to the possible avoidance of Income Tax and Corporation Tax. The legislators face the dilemma of tightening controls but without restricting entrepreneurial zeal in the hope that small businesses will grow into bigger ones.

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<sup>402</sup> Her Majesty's Revenue & Customs (2013) *Tackling the hidden economy*  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/190076/HMRC\\_Issue\\_briefing\\_-\\_Tackling\\_the\\_hidden\\_economy.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/190076/HMRC_Issue_briefing_-_Tackling_the_hidden_economy.pdf)

<sup>403</sup> National Audit Office (NAO) (2008) *Tackling the hidden economy*  
<https://www.nao.org.uk/wp-content/uploads/2008/04/0708341.pdf>

According to the Eurobarometer Survey<sup>404</sup> conducted in 2013 across the EU, in the UK around 8 per cent of paid for goods and services transactions are undeclared, the majority of which are between family, colleagues and acquaintances (50% of all transactions), relatives (10%) and other private persons/households (16%). This means that only just over one quarter of transactions were with businesses.

In terms of the supply side, according to the Eurobarometer survey only around 3% of all those in employment provided undeclared paid for goods and services (to varying degrees). This is somewhat below an estimate for 2005 from HMRC in a National Audit Office (NAO) report<sup>405</sup> which suggested that there were around 2 million 'ghost and moonlighters', which equates to around 7% of all employment.

In terms of fraud and error in benefits and tax credits payments, according to government sources<sup>406</sup> the level was 'unacceptably high'. In the ten years up to 2013-14, fraud and error over-payments were around 3% of the total on average per year, with under-payments at around 1% (though the agencies appear to calculate the figures on different bases)<sup>407</sup>.

As for the shadow economy employing vulnerable workers such as illegal migrants, the main sectors of employment are agriculture, horticulture, food processing/packaging, event catering and construction. Workers are often provided by third party 'gangmasters' on a job-by-job basis making it difficult for the regulatory agencies to keep track other than by physical inspection.

The evidence suggests that the principal motivation for UDW is financial gain, though this can be seen from different perspectives. For second job holders, the opportunity to avoid paying tax on a share of their income is the principal driver. For some it is the aim of suppressing levels of income to meet thresholds for welfare support. For those working wholly in the shadow economy the same incentives dominate but are clearly more of a driver to stay out of the regular economy. Here the government has tried to offer incentives for hidden workers to join the regular labour market, and the National Minimum Wage (NMW) and the increased National Living Wage (from April 2016) are partly aimed at making regular work attractive. For unscrupulous employers the financial incentives to operate in the shadow economy can be great, with savings in tax, national insurance, sick and holiday pay, pensions and other statutory requirements, not least paying below the NMW which often means exploiting vulnerable groups such as illegal migrants.

### **2.1.3 Estimated scale of undeclared work**

There is no one reliable official source of data on the extent of UDW in the UK. A report by the National Audit Office (NAO)<sup>408</sup> points out that HMRC has sought to estimate the extent of taxation losses due to the hidden economy but has so far failed to provide robust estimates.

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<sup>404</sup> European Commission (2014) *Undeclared work in the European Union* (Special Eurobarometer 402) [http://ec.europa.eu/public\\_opinion/archives/ebs/ebs\\_402\\_en.pdf](http://ec.europa.eu/public_opinion/archives/ebs/ebs_402_en.pdf)

<sup>405</sup> National Audit Office (NAO) (2008) *Tackling the hidden economy* <https://www.nao.org.uk/wp-content/uploads/2008/04/0708341.pdf>

<sup>406</sup> Department for Work and Pensions (2015) *Fraud and error in the benefit system: 2014/2015 biannual national statistics, Great Britain* [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/473968/fraud-and-error-stats-release-fy-2014-15.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/473968/fraud-and-error-stats-release-fy-2014-15.pdf)

<sup>407</sup> National Audit Office (2015) *Understanding fraud and error in benefits and tax credits: A primer* <https://www.nao.org.uk/wp-content/uploads/2015/09/Understanding-fraud-and-error-a-primer.pdf>

<sup>408</sup> National Audit Office (2008) *Tackling the hidden economy* <https://www.nao.org.uk/wp-content/uploads/2008/04/0708341.pdf>

HMRC publishes an annual report on Measuring Tax Gaps<sup>409</sup> which breaks down the total tax gap by behaviour and distinguishes between the hidden economy, evasion, avoidance, errors (including criminal attacks), legal interpretation, non-payment and failure to take reasonable care. For the tax year 2014-15 the tax gap was slightly smaller in percentage terms at 6.5 per cent compared to 6.9 per cent in 2013-14, though in monetary terms it remained largely unchanged at GBP 36bn (EUR 44bn). Over the longer term, the trend has been for a reducing tax gap from 8.3 per cent in 2005-06 to the latest figure of 6.5 per cent. The largest component of the tax gap comprises Income Tax, National Insurance Contributions and Capital Gains Tax which combined make up around 43 per cent of the total. Another 39 per cent is accounted for by VAT.

More broadly various estimates of the scale of UDW have been produced, normally around the following three approaches:

- Direct procedures at a micro level aimed at determining the size of the shadow economy at one point in time (as used by the Eurobarometer survey, for example);
- Indirect procedures that make use of macroeconomic indicators in order to proxy the development of the shadow economy over time; and
- Statistical models that estimate the shadow economy as an unobserved variable.

The direct procedure was used in the 2014 Eurobarometer survey and suggested that around 8% of paid for goods and services were undeclared in the UK, which was at the lower end of the spectrum among all EU Member States.

Using statistical methods, and specifically the MIMIC approach, combined with estimates of the absolute size of the shadow economy using the currency demand approach, a recent Institute for Economic Affairs (IEA) report<sup>410</sup> estimated the size of the UK shadow economy in 2012 at 10.3% of official GDP<sup>411</sup>. This had fallen from 12.5% in 2003, though the reasons for this are likely to be varied and include success with enforcement by HMRC, BEIS and DWP, though the reliability of the statistics may call into question the robustness of the estimates so derived.

## **2.2 Institutional Framework**

### **2.2.1 Responsibilities for addressing undeclared work**

The principal government departments or agencies with a direct role in some form of UDW or the hidden economy in the UK are as follows:

- Her Majesty's Revenue and Customs (HMRC) – regarding the loss of revenue from UDW including losses of Income Tax, Value Added Tax (VAT), Capital Gains Tax and Corporation Tax.
- Department for Work and Pensions (DWP) – chiefly benefit and tax credit fraud, and lack of compliance with labour law (including health and safety (working with the independent Health & Safety Executive), working time, etc.).
- Department for Business, Energy and Industrial Strategy (BEIS) – regarding labour market regulation and control of employment agencies and businesses

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<sup>409</sup> Her Majesty's Revenue & Customs (2015) *Measuring tax gaps 2016 edition – tax gap estimates for 2014-15*

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/561312/HMRC-measuring-tax-gaps-2016.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/561312/HMRC-measuring-tax-gaps-2016.pdf)

<sup>410</sup> Institute of Economic Affairs (2013) *The Shadow Economy*

<http://www.iea.org.uk/sites/default/files/publications/files/IEA%20Shadow%20Economy%20web%20rev%207.6.13.pdf>

<sup>411</sup> The analysis calls into question whether the shadow economy should be calculated as a proportion of just the official GDP or the official GDP plus the shadow economy element. If the latter, this would render a smaller figure.



through the Employment Agency Standards Inspectorate (EAS), enforcement of the National Minimum Wage (NMW) (with HMRC).

- Home Office (HO) – regarding illegal working, worker exploitation, licensing of gangmasters in high risk sectors, modern slavery and human trafficking (through the Gangmaster and Labour Abuse Authority (GLAA)).

The concerns over UDW are shared across the four home nations of the UK, and in the key areas of departmental responsibility listed above, the UK government has reserved powers (i.e. not devolved to the home nations). However, as part of the post-independence vote settlement, Scotland has been given a 'fiscal framework' that allows the Scottish Government control over certain parts of VAT receipts and, from April 2017, full devolution of income tax rates and thresholds.

At a local level, there is also a strong interest in tackling UDW and key players include local authorities and their role in collecting council taxes, curbing abuse of social housing, social support frameworks, etc. The social partners have a strong interest in preventing UDW, particularly the trade unions in efforts to tighten working labour market legislation and its enforcement.

### **2.2.2 Characteristics of the responsible organisations**

Information on the resources dedicated to tackling UDW are difficult to estimate, partly because many functions are subsumed within a range of activities carried out by the various departments, agencies and their staff. For example, in the DWP, Jobcentre Plus staff are aware of the need for vigilance in detecting benefit fraud, while police forces are trained to identify illegal working, exploitation of workers and human trafficking. There has been a significant increase in funding at HMRC to tackle the hidden economy which, through the Budget and additional internal deployments, will increase the total workforce (including managers and support) to over 1,000 staff.

HMRC is also developing new and innovative ways to extend its compliance activity, for example through 'Virtual Street Sweeps' to increase detection rates. Cooperation with other government agencies is also developing to tackle the social consequences of illegal working and the hidden economy.

### **2.2.3 Cooperation and collaboration between authorities and cross-border authorities**

In terms of cooperation and collaboration between responsible authorities, little precise information is available except for statements by various departments/agencies that there is increased sharing of information (e.g. to tackle tax evasion).

## **2.3 Policy Focus and Measures**

### **2.3.1 Policy approach**

The policy approach adopted in the UK takes a number of forms constructed around the different departmental interests. So, for example, HMRC's approach to tackling the hidden economy is aligned with the department's overarching approach to compliance using the 'promote, prevent, respond' strategy for non-compliance, where the stated aim is to:

- Promote compliance by designing it into systems and processes;
- Prevent non-compliance at or near the time of filing; and
- Respond to non-compliance through well-designed delivery.

For DWP and BEIS, it is more about tightening the legislative framework to prevent breaches, along with improved enforcement mechanisms and for the Home Office Immigration Enforcement, the emphasis is on preventing worker exploitation through modern slavery and trafficking.

### 2.3.2 Measures to tackle UDW

A number of recent key legislative milestones directly or indirectly address the hidden economy and UDW as follows:

- **The Gangmasters (licensing) Act 2004** – this legislation followed concern over the exploitation of workers in agriculture, forestry, horticulture, shellfish gathering and food processing and packaging industries<sup>412</sup> by labour providers known as ‘gangmasters’. It provided for a Gangmasters Licensing Authority (GLA) (now the Gangmasters and Labour Abuse Authority (GLAA) which regulates labour providers and employment agencies and sets out eight standards covering areas including: pay and tax matters; prevention of forced labour and mistreatment of workers; working conditions; and sub-contracting and using other labour providers. A team of compliance officers are in place to enforce the licensing requirements, including random checks.
- **The Modern Slavery Act 2015** – which aims to provide support and protection for victims of slavery and trafficking, strengthening the legal position regarding the following:
  - Increasing the maximum sentence for the most serious offenders from 14 years to life imprisonment;
  - Ensuring perpetrators convicted face the toughest asset confiscation regime;
  - Consolidating the simplifying existing modern slavery offences into one Act;
  - Introducing Slavery and Trafficking Prevention Orders and Slavery and Trafficking Risk Orders to restrict the activity of individuals posing a risk of causing harm;
  - Strengthening law enforcement powers at sea to close loopholes which can prevent the police and the Home Office Immigration Enforcement from being able to act on board vessels at sea.

The Act has established an Independent Anti-Slavery Commissioner tasked with ensuring the legislation is used and in practice is fit for purpose.

More recently, in the Immigration Act 2016, the government has introduced measures to tackle illegal working and worker exploitation, which focus on the following:

- Establishing a statutory **Director of Labour Market Enforcement** to set priorities for the enforcement bodies across the spectrum of non-compliance, from criminal exploitation to payroll errors. In addition to the provisions of the Immigration Act 2016, employing an illegal worker has been a criminal offence since the Immigration, Asylum and Nationality Act 2006;
- Creating a new regime of labour market enforcement undertakings and orders to secure compliance with the offence of aggravated breach of labour market legislation;
- Increasing intelligence and data sharing between the existing enforcement bodies and others to strengthen the targeting of enforcement; and
- Reforming the Gangmasters Licensing Authority to become the Gangmasters and Labour Abuse Authority with stronger powers to deal with labour exploitation across the economy.

For the tax authority (HMRC) the approach is to change the behaviour of those in the hidden economy. This means supporting business start-ups with guidance and tools to ensure they remain legitimate; making compliance easier to help people pay the tax they owe; improving the identification of those outside the tax system including

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<sup>412</sup> The main trade union for the building trades, UCATT, has been campaigning for the inclusion of the construction sector within the Gangmasters Licensing Authority.

increased sharing of information between agencies; and taking a tougher approach to businesses failing to come forward.

In April 2016 the government strengthened its policy on the enforcement of the NMW by increasing the level of fines that can be imposed on employers for NMW breaches from 100 per cent to 200 per cent of the arrears owed to the worker affected. Employers can also be publically named in a government press notice<sup>413</sup> which can cause reputational damage to the employer and so act as a deterrent to other employers.

Data on performance is internal in terms of specific performance indicators, but each year the Comptroller and Auditor General issues a report via the National Audit Office (NAO)<sup>414</sup>. This assesses the work of HMRC on collecting tax and on its success on the 'compliance yield' which measures the effectiveness of HMRC's enforcement and compliance activities. HMRC's funding and delivery commitments for 2015-16 were set out in the 2015 Spending Review, and the latest report sets out its success in tackling, *inter alia*, fraud and error working with the DWP on various benefit payments. DWP statistics indicate that between 2014/15 and 2015/16 the rate of DWP-funded benefits overpayments has increased slightly to 1.9% of expenditure from its lowest recorded rate of 1.8% in 2014/15. It amounts to £3.3bn of overpayments (EUR 3.79bn). By type of benefit the largest overpayment was in Housing Benefit (6 per cent of the total of this benefit) followed by Pension Credit (5.3 per cent), Jobseeker's Allowance (4.3 per cent) and Employment & Support Allowance (3.1 per cent)<sup>415</sup>. However, of the GBP 3.3bn (EUR 3.79bn) of overpayments, GBP 1.9bn (EUR 2.18bn) was attributed to fraud, GBP 0.9bn (EUR 1.03bn) to claimant error and the remainder the result of official error.

### 2.3.3 Good practice

The UK recognises the need for a regulatory framework with sufficient weight to act as a disincentive for UDW, but there is also a recognition that incentives may also be effective. This means reducing regulations for businesses in employing workers and keeping employment costs low, but also incentivising individuals to seek work (or convert to work) in the regular labour market attracted by a higher National Living Wage and other financial incentives such as workplace pensions. In this regard the government agencies have focused on efforts to raise awareness of the benefits of joining the formal economy, including highlighting:

- Responsibility to register as self-employed;
- The value of increased business credibility when legitimate;
- More help available for getting tax affairs in order;
- Encourage take up of voluntary disclosure schemes;
- What happens to those detected – emphasising this may not necessarily lead to criminal prosecution;
- Publicise the cases where prosecution has taken place (as a deterrent); and
- Change the attitudes of those employers using labour in the hidden economy.

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<sup>413</sup> Department for Business, Innovation and Skills (2015) *Policy on HMRC enforcement, prosecution and naming employers who break the National Minimum Wage law* [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/429737/bis\\_15\\_299\\_NMW\\_hm\\_revenue\\_and\\_customs\\_enforcement\\_prosecutions\\_and\\_naming\\_employers\\_who\\_break\\_national\\_minimum\\_wage\\_law\\_May\\_2015\\_\\_2\\_.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/429737/bis_15_299_NMW_hm_revenue_and_customs_enforcement_prosecutions_and_naming_employers_who_break_national_minimum_wage_law_May_2015__2_.pdf)

<sup>414</sup> The latest is: National Audit Office (2015) *HMRC 2015-16 Accounts: Report by the Comptroller and Auditor General* <https://www.nao.org.uk/report/her-majestys-revenue-customs-annual-report-and-accounts-2015-16/>

<sup>415</sup> Department for Work and Pensions (2016) *Fraud and error in the benefit system: 2015/16 Final Estimates, Great Britain* [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/575407/fraud-and-error-stats-release-2015-16-final-estimates.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/575407/fraud-and-error-stats-release-2015-16-final-estimates.pdf)

This represents an approach that attempts to use the power of publicity to bring UDW into the formal economy, though with sufficient legislative weight and enforcement expertise should serious breaches of taxation or labour law be discovered.

#### **2.3.4 Challenges and barriers**

A degree of UDW is inevitable in all countries and it is likely that a significant part of it will remain undetected partly because of its fragmented nature and the fact that it often represents transactions between people known to each other (such as friends or relatives).

For the UK, it is the view of the author that significant challenges lie in controlling the abuse of labour and in particular the casual employment of illegal migrant workers or workers from within the EU who are exploited. This is likely to require more resources in terms of enforcement officers and better intelligence networks and while good progress has been made, more could be done to eradicate this activity. Government actions, such as those in the Immigration Act 2016 that have reformed the Gangmasters Licensing Authority into the 'Gangmasters and Labour Abuse Authority', demonstrate the current thinking on enforcement, though whether extra (and adequate) resources will be given to this remains to be seen.

#### **2.3.5 Addressing the challenges**

In terms of the loss of taxation, the approach in the UK of attempting to regularise those involved in UDW through publicity and persuasion is used alongside legislation, and to a great extent this has worked. It is highly unlikely that all UDW can be eliminated and so the challenge is to minimise it, and overall the extent of UDW in the UK is comparatively low. Furthermore, the rollout of Universal Credit is expected to reduce the extent of benefit fraud and error because of its simpler approach to both the application for, and payment of, benefits. It also links with the HMRC database, enabling tax records to be cross-referenced with benefit claims (and payments), with the potential to further reduce the incidence of erroneous payments.

The abuse of labour is best tackled directly and here the UK has embarked on setting out a legislative framework (see 1.3.2) that ensures all forms of worker exploitation are subject to penalty. However, uncovering incidences of non-compliance tends to require intensive physical resources and intelligence with the associated cost implications.

#### **2.3.6 Key remaining challenges to be addressed**

One of the key challenges facing the UK in terms of UDW and the shadow economy is to see through the recent legislative changes into operational effectiveness. The Modern Slavery Act, for example, is the first of its kind in Europe and is aimed at demonstrating the country's commitment to seek out and prosecute slavery and trafficking, as well as providing for the protection of victims and their treatment once released (such as the payment of reparations, health and welfare support, etc.). The use and effectiveness of this new legislation should be closely monitored, helped by the Independent Anti-Slavery Commissioner who will oversee the workings of the legislation.

The other new measures introduced in the Immigration Act 2016 on tackling the exploitation of workers and illegal working are also in some ways innovative and need to be monitored closely. The Director of Labour Market Enforcement is a bold attempt at bringing together the work of the existing enforcement agencies to coordinate resources and response. There is a requirement to produce an annual labour market enforcement strategy which will inform the operational priorities for the individual enforcement bodies to enhance the joint operations that already take place. Key to this will be the sharing of information and legislative gateways are being put in place to facilitate this.

