

CHAPTER 5

INFORMAL EMPLOYMENT: SURVEY METHODS OF MEASUREMENT AND NATIONAL POLICY REVIEWS

**Annexes 1 and 2 to "Informal Employment and Promoting the Transition to a Salaried Economy",
Chapter 5 of the OECD *Employment Outlook 2004*.**

ANNEX 1. SURVEY METHODS FOR ESTIMATING INFORMAL EMPLOYMENT

The Rockwool Foundation survey design (Pedersen, 2003) which was implemented in Denmark, Norway, Sweden, Germany and Great Britain draws on extensive experience with similar earlier surveys. It includes prompts describing different types of work and payment, and allows a relatively precise identification of work that is in legal terms taxable. Surveys were conducted only by highly-respected data-collection institutes (national statistical institutes, except in Germany) and samples were based on population registers, or a household sample frame weighted to ensure representativity at the individual level. Survey response rates did not differ from the usual surveys conducted by the institutes, and the specific item non-response rate (in relation to the question about black activities) was low. The results (Table 5.2 of the main text) show that a fairly high proportion of respondents reported doing some black work over the past year: up to 20% overall, and always above 10% for age groups below 40. This suggests that surveys are able to elicit responses concerning a large proportion of undeclared work. Owing to the relatively low average hours reported (which is not surprising, insofar as most black work was reported by people who also held a regular job), the shares of “black” hours in total hours are fairly low, although they reach 4% in Denmark and Norway. An earlier international comparison using surveys that did not use the same questionnaire, but with an attempt at adjusting for differences in definition, suggested that the “shadow economy” in the 1980s was 4-6% in Norway, Holland and Germany but 17% in Spain (Table 5.3 of the main text).

A number of biases may affect survey findings of this kind:

- The sample frame probably does not include migrants without a work permit, who usually will not be registered at an address, nor people living and working from an address different from their official one (in the United Kingdom benefit authorities have been given powers to prevent the automatic redirection of mail to another address: Darling, 1999).
- Although *item* non-response was low, about a third of the people approached did not complete the survey at all, and since lack of time is commonly cited as a reason for non-participation, those working long hours are likely to be over-represented among non-respondents.
- For unemployed workers, “the questionnaire method can have a particular weakness – it cannot be ruled out that the unemployed in particular are not totally honest in the questions in black activities ... since the unemployed cheat twice over, *i.e.* both with regard to tax and unemployment benefit” (Pedersen, 2003): again, this type of underreporting may arise where undeclared hours worked are long.
- Response patterns in southern Europe may be different from those in the north, with more established habits of concealment of income and suspicion of officialdom. Thus, the proportion of unemployed reporting receipt of unemployment benefits in the EU Labour Force Survey in the 1990s was only about half the level implied by administrative statistics for benefits in Portugal, and a third in Greece (OECD, 1998, Table 4.2), whereas discrepancies of this kind in other EU countries seem to be smaller.

To tackle some of the biases, in addition to conducting surveys that explicitly ask respondents about their own undeclared work, it is possible to survey “key observers” asking them to estimate undeclared activity. It is also possible to engage in quasi-anthropological research:

“A survey was conducted by Tommaso Di Nardo, Rafaela Caldarelli and Maria Izzo (2000) on a long, residential street in San Giuseppe Vesuviano. The town is the ‘capital’ of a semi-underground textile and clothing manufacturing district in the province of Naples. The street chosen was neither wealthy nor poor; it was intermediate, as was the local “irregularity” rate. The standard method was that of the census survey, but conducted three times for the same universe in a period of a few months: once by an interviewer not known to the local area; once by an interviewer who was known, using the indirect method of contacting ‘key observers’; and once by a known interviewer using the direct, door-to-door survey method, but establishing trust with the respondents and exploiting (fortuitously) her particular personal situation: she had to finish her thesis and she was pregnant Where the standard method produced a result of 31.1% and that of the “informed persons” one of 35.8%, the surprisingly effective ‘Caldarelli method’ got 43.7%, or more than 40% higher than the traditional approach. Is this figure too high? ‘Not at all,’ answered a trade unionist (one of the ‘key observers’) in the course of a public debate; ‘it is still lower than the reality’. Probably these three responses do not reflect only decreasing reticence. They presumably also reflect the differing degrees of concealability, irregularity, precariousness and the relative importance (individual and for the household) of unreported work ...” (Meldolesi, 2003).

This example argues that information from broad national surveys such as the labour force survey should be “rebenchmarked”, using more intensive investigation techniques to check biases in small subsamples, before using them as input to the national accounts for example.

Surveys of firms also can give insights into tax evasion and related problems. According to the EBRD/World Bank Business Environment and Enterprise Performance Survey implemented in 26 countries of Central and Eastern Europe and the Commonwealth of Independent States in 2002, firms in Poland and the Czech Republic hid an average of less than 10% of their sales from tax authorities, and less than 10% of them bribed tax authorities. Tax underreporting and bribery percentages were slightly higher in Hungary and the Slovak Republic but they were often over 20% or 30% in CIS and Balkan countries (Fries *et al.*, 2003).

ANNEX 2. SOME NATIONAL REVIEWS OF POLICY TOWARDS INFORMAL EMPLOYMENT

This Annex briefly summarises the recommendations made in official national reviews with a policy focus, such as studies by the tax or labour administration, the national audit office, a parliamentary commission, or other committee created at political level. “Background” factors which encourage formality – reasonable tax rates and employment regulation, good educational attainment of the labour force, absence of corruption among government officials, social norms and the democratic legitimacy of government – are seen as values in themselves, and reviews do not give a written description of these dimensions of the strategy. The focus in national reviews is on potential changes in legislation and administration.

A private body, the Centre for International Private Enterprise, also offers a detailed set of recommendations for government, with a focus on processes to improve the quality of regulation. Recommendations include: encourage participatory policymaking; enact and enforce freedom-of-information laws; streamline legal codes; strengthen property rights systems; institute corporate governance; match laws and regulations with institutional capacity, and entrepreneurs' capacity to comply; strengthen administrative and enforcement capacity of government agencies; and improve infrastructure. Kuchta-Helbling (2002) sets out these recommendations, also describing many relevant national experiences.

European Union

The “Commission Communication on Undeclared Work” (EC, 1998) which, apart from defining and describing undeclared work, called for a comprehensive strategy centred around two approaches:

- Interpreting undeclared work as a situation in which individuals or firms take advantage of the system, policy should be oriented towards sanctions and awareness-raising.
- Interpreting undeclared work as the outcome of inappropriate legislation, action should concentrate on simplification of procedures, reduction of taxation on labour, etc. The Communication also foresaw co-operation between EU states to improve co-operation and information exchange.

In 2003, the EU moved from 15 guidelines to only 10 employment guidelines, of which the ninth concerns undeclared work:

- a) Simplification of the business environment by the removal of excessive bureaucracy, especially when dealing with startups and small enterprises.
- b) Strengthening of incentives to declare work by mostly reducing labour taxation and eliminating poverty traps.
- c) Improvement in sanctions by reinforcing surveillance and enhancing co-operation among labour inspection-dedicated institutes.
- d) Raising social awareness about the problem by informing public opinion on the consequences of undeclared work on the social security system and, more in general, on social cohesion.

- e) Improvement in gauging the amount of undeclared work in Member States so as to better formulate the policies aimed at combating this work.

A Council resolution (EU, 2003) recently committed EU member states to preventive actions and sanctions, and to making necessary efforts to measure the extent of the problem and progress achieved.

Several EU countries have created permanent bodies specifically responsible for coordinating measures against undeclared and illegal work across the different departments that are directly involved. In France, the Interministerial Delegation for the Struggle against Illegal Work (DILTI) is responsible for seven categories of illegal work, including illegal trade and placement of workers, and illegal cumulation of work (*e.g.* private work for profit by a civil servant). DILTI (2002) provides links to advice to enterprises and self-employed workers, legislation, statistics and studies. France also has a central agency of social security organisations (ACOSS) which issues an annual report on research into and detection of illegal work (ACOSS, 2003). In Italy, the National Committee for Surfacing of Irregular Work (www.emersionelavorononregolare.it) as well as many provincial commissions have been created.

Australia

ATO (1998) examined the cash economy as a practical issue of policies to improve tax compliance, making 33 recommendations. In addition to a number of recommendations in the areas of research, communication and co-operation with other authorities and the taxpaying public, and staff training, a large block of recommendations focused on promoting better record-keeping by cash businesses. (Following an earlier first report, the number of field staff engaged in cash economy initiatives had by 1998 been increased from 300 to 900 officers, implementing an approach called "real time reviews", which involves frequent yet irregular visits to cash businesses to ensure that they maintain essential records.) Some of the main measures were to help and educate new businesses offering advice on registration and tax matters; to introduce record-keeping requirements that vary by industry; to consider imposing on-the-spot fines and/or more onerous record-keeping requirements on taxpayers with a poor compliance record or (a practice already existing in Japan) to allow compliant taxpayers to use a simplified tax return form. Additional strategies include benchmarking financial ratios by industry, and supporting industry self-regulation which will be concerned *inter alia* with unfair competition related to tax evasion.

ATO (2003) claims considerable success from this strategy over recent years, and provides a revised list of 38 recommendations. One new area discussed following changes to the tax system is the registration of businesses and transactions for GST (general sales tax, equivalent to VAT in EU countries) and registration of businesses and transactions using the Australian Business Number (ABN). There is now a legal requirement on businesses to withhold 48.5% tax on payments to other businesses which do not provide an ABN. Eleven of the recommendations focus on business-to-consumer dealings, including problems of moonlighting and customers who ask not to pay GST.

Sweden

The Swedish National Audit body in 1998 (RRV, 1998) found that the problem was a very complex one (Jönsson, 2002) and proposed a large national programme based on three components:

- Influence attitudes: this included an information campaign, simplification of the regulatory framework and self-regulation in the business sector.
- Increase the risk of detection: this included centralization of information, increased resources for tax authorities and measures against benefit fraud.

- Create incentives to declare income: this had eight subheadings, mainly highlighting that pension entitlements create an incentive for declaration, and that high effective marginal tax rates for social security benefits, labour law, complex tax regulations, etc. create an incentive for evasion. Two specific recommendations are for a review of business aid schemes because they make many entrepreneurs, who consider that these schemes give an unfair advantage to their competitors, less willing to comply with the rules; and the extension to other sectors of tax rebates based on invoices for construction work, since this gives individuals an incentive to demand invoices and receipts, which is otherwise lacking, even for purchasers who do not explicitly intend to facilitate tax evasion.

Switzerland

A national council for the struggle against black-market work was created in 1999. Its report (SECO, 2000) recommended repressive measures as the main strategy: “Given that the route of reduced incentives offers limited prospects, it is difficult to struggle against black-market work other through *repressive measures (inspections and sanctions)*. In this regard, it is worth recognising that repression is in effect a type of reduction in incentives for undeclared activities, insofar as it aims to make, in the calculation done by the employer or employee, the risk of loss (financial or other, through prison sentences) greater than the prospective profit.” Specific measures include the improved exchange of administrative information, measures against false self-employment, and increases in sanctions. However in the case of domestic services purchased directly by households, it was recognized that checks are difficult to implement and an approach based on incentives (creating service cheques, as in France) was recommended.

United Kingdom

In the United Kingdom, only limited resources have been devoted to policy analysis of the informal economy *per se*, although recent years have seen increased efforts at detecting benefit fraud, including non-declaration of earnings. On the basis of a few months' work – but drawing on the experience of officials across all the relevant government departments – Grabiner (2000) made a series of recommendations:

- Making it easier to join the legitimate economy: this includes a confidential telephone line to advise people on how they can put their affairs in order, and increased help for people who set up as self-employed.
- Prevention: this includes a requirement on people to tell the Inland Revenue as soon as they start up in business, and better controls on obtaining false identify documents and National Insurance numbers.
- Detection: this includes administrative co-operation and data sharing, ways of using information from private sector sources (*e.g.* concerning where people live and their bank accounts), and giving investigators powers to make reverse searches of the telephone directory to find the addresses of people who advertise business with only a telephone number.
- Punishment: measures in relation to benefit fraud include making greater use of warnings to employers who are suspected of colluding with fraudulent benefit claims that they risk detailed investigation and prosecution; in cases of suspected working, requiring people to attend the Jobcentre more frequently and at unpredictable times; and in case of repeated fraud, removing the right to benefit for a period.
- Advertising, to change public attitudes.

BIBLIOGRAPHY

- ACOSS (2003), *Lutte contre le travail illégal: bilan 2002* (www.acoss.fr – publications - études).
- ATO (Australian Tax Office) (1998), *Improving Tax Compliance in the Cash Economy, Second Report of the Cash Economy Task Force*, Canberra (<http://ctsi.anu.edu.au/publications.html>).
- ATO (2003), *The Cash Economy under the New Tax System, Third Report of the Cash Economy Task Force*, Canberra (www.ato.gov.au/content/downloads/N9544CEbookfinal.pdf).
- Darling, A. (1999), *A New Contract for Welfare: Safeguarding Social Security*, Green Paper (Cm 4276) (www.dwp.gov.uk/publications/dss/1999/fraud/index.asp).
- DILTI (Délégation interministérielle à la lutte contre le travail illégal) (2002), *Plaquette de présentation de la DILTI* (www.travail.gouv.fr/ministere/dilti.html).
- EC (1998), “Communication of the Commission on Undeclared Work”, COM(1998)219 (http://europa.eu.int/comm/employment_social/empl_esf/docs/com98-219_en.pdf).
- EU (2003), “Council Resolution on Transforming Undeclared Work into Regular Employment”, *Official Journal*, 29 October, C 260 (<http://europa.eu.int/eur-lex/en/archive/index.html>).
- Fries, S., T. Lysenko and S. Polanec (2003), “The 2002 Business Environment and Enterprise Performance Survey: Results from a Survey of 6,100 firms”, EBRD Working Paper No. 84 (www.ebrd.com/pubs/find/index.htm).
- Grabiner, Lord (2000), *The Informal Economy*, HM Treasury Public Enquiry Unit, HMSO (www.hm-treasury.gov.uk/documents/taxation_work_and_welfare/tax_index.cfm – other tax issues).
- Jönsson, H. (2002), “Undeclared Work in Sweden – Results and Recommendations” (www.academyavignon.net/undwork.htm).
- Kuchta-Helbling, C. (2002), “Barriers to Participation: the Informal Sector in Developing and Transition Countries”, paper for the conference on Unofficial Activities in Transition Countries: Ten Years of Experience, Zagreb (www.ijf.hr/UE_2002/program.html).
- Meldolesi, L. (2003), “Policy for the Regulation of the Underground Economy and Employment”, *Review of Economic Conditions in Italy*, No I, January-April (www.emersionelavorononregolare.it/catania/index.php).
- OECD (1998), *The Public Employment Service: Greece, Ireland, Portugal*, Paris.
- Pedersen, S. (2003), *The Shadow Economy in Germany, Great Britain and Scandinavia: A Measurement based on Questionnaire Surveys*, Rockwool Foundation Research Unit Study No. 10, Copenhagen.

RRV (Riksrevisionsverket) (1998), *Illicit Work in Sweden: A Report on a Welfare State Dilemma*, report RRV 1998:61 (www.riksrevisionen.se/ – publikationer – Riksdagens revisorer).

SECO (2000), *Rapport du groupe de travail federal sur la lutte contre le travail au noir* (www.seco-admin.ch/themen/arbeit/recht/schwarzarbeit_recht/?lang=fr).