



European Employment Observatory Review: **Spring 2007**



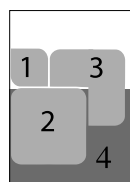
European Employment Observatory Review: Spring 2007

European Commission
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OVERVIEW OF SYSDÉM EXPERTS' NATIONAL UPDATE ARTICLES ON UNDECLARED WORK IN THE EUROPEAN UNION SUBMITTED MAY 2007

1. INTRODUCTION AND BACKGROUND

This Review provides an update, for the EU-27, to the report on undeclared work that was published in the EEO Review: Autumn 2004

www.eu-employment-observatory.net/en/reviews

The Review concentrates on the following aspects:

- changes in the prevalence of undeclared work;
- the impact of minimum wages;
- the impact of the taxation and social security regimes; and
- measures aimed at tackling undeclared work.

The Review is based on articles submitted by the SYSDÉM experts, as part of the work of the European Employment Observatory, in Spring 2007. The original articles are available in English on the EEO website www.eu-employment-observatory.net/en/reviews

An appendix to this Review summarises the national articles by country.

Forthcoming European Commission Communication on Undeclared Work (Autumn 2007)

These articles have contributed to the recent debate about the prevalence and persistence of undeclared work led by the European Commission, the results of which are forthcoming in the *2007 Commission Communication on Undeclared Work*.

Tackling undeclared work is integrated into the European Employment Strategy, Guideline 21 under the broad ob-

jective of Improving the Adaptability of Workers and Enterprises (Council Decision of 12 July 2005 on Guidelines for the employment for the Member States):

Europe needs to improve its capacity to anticipate, trigger and absorb economic and social change. This requires employment-friendly labour costs, modern forms of work organisation and well-functioning labour markets allowing more flexibility combined with employment security to meet the needs of companies and workers. This should also contribute to preventing the emergence of segmented labour markets and reducing undeclared work.

Previous European Commission Communication (1989)

The 1989 Communication launched a debate on the causes of undeclared work and the policy options for combating it. The debate focused on two main concerns. First, a discussion was needed to identify correctly the causes and extent of the problem. Second, the aim was to regard combating undeclared work as part of the overall employment strategy (COM (98) – 219).

Previous European Commission Research (2004)

The background to the European Commission's concerns about undeclared work in the enlarged EU is manifest in the 1998 Commission *Communication on Undeclared Work* (COM (98) 219 final) and the study *Undeclared Work in an Enlarged European Union*, Renooy et al., 2004. (See http://europa.eu.int/comm/employment_social/employment_analysis/work/undecl_work_final_en.pdf).

The principal aims of the research were to clarify definitions, measurement methods, estimated size, good practices and the gender dimension of undeclared work. In summary the study concluded that the information on the size and structure of undeclared work collected through reliable methods was sparse.

For the EU-15 the conclusion was that undeclared work in most Member States was rather modest in extent with

estimates far below 5% of GDP, the exceptions being southern European countries like Italy and Greece.

Participation in undeclared work was dominated by men between 25 and 45 years of age, generally skilled workers and often with a regular job. The sector with a highest incidence of informal work across the EU was the construction sector followed by agriculture (in Germany), hotel and restaurant sectors and personal and domestic services.

For the new Member States and the then (2004) candidate countries, regarding the estimated scale of undeclared work, the range was from 8% to 22% of GDP. The Czech Republic, Estonia and Slovakia were in the lowest band; Bulgaria and Romania were in the highest band; and Poland, Slovenia, Hungary, Lithuania and Latvia were in the middle band. The following were interesting characteristics of undeclared work in Central and Eastern European countries:

- the importance of retailing and the hotel and restaurant sectors;
- the presence of a subsistence economy with a focus on agriculture, more typical of developing countries;
- the relative high importance of professional services;
- the relative low incidence of the informal economy in manufacturing.

One of the most important factors in combating undeclared work in these countries was reported as the general success and stability of economic development, political stability, integration in Western markets (including the presence of foreign capital) and the liberalisation of foreign trade.

Women participated less in undeclared work than men overall in the Member States and candidate countries. However the working conditions of women in undeclared work overall were less favourable than those of men. Women tended to be employed in less autonomous jobs, earned less and were motivated to work informally by economic necessity. Men tended to earn extra cash on the side through undeclared work.

2. THE PREVALENCE OF UNDECLARED WORK

The 2004 European Employment Observatory Review indicated that the prevalence of undeclared work ranged from 1.5% to 30% of GDP, with the greatest prevalence amongst the (then) candidate countries and the new Member States.¹ This pattern has not changed, although it needs to be acknowledged that new official data (i.e. since 2004) are only available for a small number of countries.

Table 1 summarises the latest position on prevalence, in comparison with that noted in 2004. There is evidence of a decline in six countries, four of which are new Member States. The decreases in Denmark, Estonia, Italy and Slovakia are fairly small. In the EU-15 the decrease may be linked with government measures (e.g. information campaign in Denmark, stronger control measures), whereas in the new Member States, the main factor is seen in the pace of job creation and the emergence of shortages.

Six other countries show increases in the prevalence of undeclared work; this includes Germany and Sweden, although their prevalence rates remain relatively low. Changes in direct and indirect taxation in Germany have, it seems, had an impact on undeclared work, whilst in Sweden attitudes toward tax evasion appear to have relaxed and may be accounting for much of the change. In Spain there has been a moderate increase, with no specific cause identifiable, although it is interesting to note that the increase would probably have been much greater without the amnesty for illegal migrant workers in 2005.

The other countries showing an increase in prevalence are new Member States – Bulgaria and Malta. In Bulgaria and Malta, the increases seem to be linked with general increases in the size of the informal economy.

There is no apparent change in prevalence in 16 countries. For these countries, there are no specific, new official data on undeclared work. However, at the same time there are no indications from 'indirect' evidence (e.g. numbers of breaches of the law, or anecdotal evidence) of any changes in prevalence.

(1) The 2004 Report included data on Turkey and Norway; these countries are not included in this update.

TABLE 1 → CHANGES IN THE PREVALENCE OF UNDECLARED WORK, SINCE 2004

Country	Comments
Decreases in the prevalence of undeclared work	
Denmark	A regular survey shows continued, moderate decreases since 2001 (from a peak of 3.8% of GDP in 2001, to 3.0% in 2005). There is some evidence that this overall decrease may be hiding an increase of prevalence amongst women (primarily as a result of the strong controls exercised in the male-dominated construction sector).
Estonia	There is evidence that the prevalence of undeclared work has decreased slightly (to around 7-8% of GDP, from 8-9% in 2001). It is still high in relation to the EU-15 but low in comparison with other new Member States.
Italy	Estimates of prevalence, based on national accounts, show a reduction from 7.6% of GDP in 2000 to 6.4% in 2006. However, this reduction has to be seen in the context of an amnesty in 2002 for illegal migrant workers (almost 650,000 workers).
Lithuania	Undeclared work has decreased from about 8% to 6% of the total employed. This appears to be linked to shortages of labour (as a result of economic growth and emigration since 2003/4).
Poland	The prevalence is currently regarded as being around 12-15% of GDP. This is a decrease from previous estimates (in 2003) of 14-25%; figures for the percentage of the population engaged in undeclared work show similar decreases.
Slovakia	Moderate decreases in the prevalence.
Increases in the prevalence of undeclared work	
Bulgaria	There are no data based on national accounts, but survey data indicate that the grey economy has been increasing markedly since 2004. It is concluded therefore, that undeclared work itself is likely to have been increasing.
Germany	Data show that undeclared work was declining until 2006, but it is expected to increase by 1%. This is a result of changes in taxation.
Spain	Figures show an increase from 2003 to 2006 (measured by number of workers undertaking undeclared work, up from 11.6% to 12.3%). However, there appears to have been a decrease in the prevalence in construction and agriculture, as a result of the regularisation of immigrant workers' status in 2005.
Malta	Undeclared work is regarded as increasing over the last few years. However, figures relate to undeclared work and illegal work (the underground economy is the focus of concern in Malta, rather than undeclared work per se).
Sweden	The prevalence has increased in the past decade. A study in 2006 showed it to be 5% of GDP, up from about 3% in 1997. Also, 11% of workers undertook some form of undeclared work in 1997; in 2006, the figure was 13%.
No evidence of change in the prevalence of undeclared work	
Austria, Cyprus, Czech Republic, Finland, Hungary, Ireland, Latvia, the Netherlands, Portugal, Slovenia, UK. • No new specific data, and no indications (e.g. from indirect evidence) of any changes in prevalence.	
Belgium	Same range of figures as in 2004. A study since 2004 (for the construction sector) has identified regional differences, with higher prevalence in regions of persistently high unemployment.
Greece	No new data, but it is understood that the prevalence continues at the same, high level. Bringing the shadow economy into GDP figures has led to Greece's GDP for 2001-06 being revised upwards by over 25% (the revised GDP data are currently being validated by Eurostat).
France	No overall change. However, there appears to have been an increase in the construction, hotels and catering and commerce sectors, with a decrease in 'other' service sectors – as measured by breaches of the law.
Luxembourg	There are no data on undeclared work (as in 2004). However, there has been an increase in the use of undeclared temporary workers (attributed to the strictness of rules regarding use of temporary contracts).
Romania	Current estimates of undeclared work put it at 16-21% of GDP with no apparent change in the prevalence of undeclared work.

There are no data to suggest that the distribution of undeclared work across sectors has changed in any Member States. The sectors most affected are still construction, hotels and catering, agriculture and personal and domestic services. Similarly, the groups most likely to be involved in undeclared work are also unchanged; immigrants (illegal and legal); workers with second, undeclared jobs, students and women providing personal and domestic services.

There have been no significant changes in the measurement of the prevalence of undeclared work since the 2004 report (see annex 1). There continue to be difficulties in adequately measuring undeclared work; the only 'advances' in the field appear to be a handful of specific studies which have added to understanding in some countries. The Swedish Tax Agency undertook a comprehensive study in 2006, and a study on undeclared work in the construction sector was undertaken in Belgium.

In Italy, the Budget Law 2007 introduced the 'congruity indices' (*indici di congruità*) which are to specify the number of labour hours required to produce a good or service, broken down by sectors, category of firm and geographical areas. Firms which do not fall into line with the appropriate index will then be subject to inspection. However, negotiations about the indices (their quantification) are ongoing between the government and social partners, and employers' organisations remain strongly opposed to their introduction. There is interest in this development amongst experts in other Member States, but no official

discussions as yet about the possible use of such indices in other countries.

3. THE IMPACT OF MINIMUM WAGES

A statutory minimum wage operates in 21 of the 27 countries.² In the six countries – Austria, Denmark, Finland, Germany, Italy, Sweden – which do not have a statutory minimum wage, there is no evidence that wage levels alone act as incentives for undeclared work. Clearly, any effect of wage levels needs to be considered alongside the impact of taxation and social security costs (see Section 4).

There are seven countries for which there is some suggestion that the minimum wage is contributing to the prevalence of undeclared work (see Table 2). However, it must be noted that the evidence is not clear-cut and there are no specific studies of the impact of the minimum wage, in any of the countries. As would be expected, it is the relatively high level at which the minimum wage is set that is likely to be acting as an incentive for undeclared work from the point of view of employers. On the other hand, for the employee, the prospect of having access to a potentially higher wage and social security protection could encourage them to leave the informal economy.

TABLE 2 → COUNTRIES IN WHICH THE MINIMUM WAGE HAS AN IMPACT ON THE PREVALENCE OF UNDECLARED WORK

Country	Comments
Greece	There are no specific data on the impact of the minimum wage, but (especially given that it is set close to average blue-collar earnings) it is likely to be providing an incentive for undeclared work.
France	The minimum wage is regarded as having an impact on undeclared work, although there is no specific evidence. The costs of employers' social contributions linked to the minimum wage are small, but they are increased by contributions to pension funds and unemployment insurance.
Cyprus	The minimum wage, which applies only to the non-unionised sector, has been increasing in recent years. There are no data or studies, but, if anything, these increases would encourage undeclared work.
Latvia	The minimum wage has been increased in recent years, aimed at reducing undeclared work. However, there is such a small gap between the minimum wage and the minimum level of subsistence, that the effectiveness of this measure is minimal and therefore the minimum wage may still be an incentive for undeclared work.
Hungary	It is likely that the minimum wage contributes to the prevalence of undeclared work. There is evidence that recent increases in the minimum wage have discouraged employment in small firms, and the employment of low-wage and low-skilled workers; these factors may, in turn, have encouraged undeclared work.
Malta	Employers express concern about the annual increase of the minimum wage and it may therefore act as an incentive for undeclared work. However, there is no specific evidence of the minimum wage having an impact on levels of undeclared work.
Poland	There is understood to be some impact of the minimum wage but it is very limited, especially given the small numbers on the minimum wage.

(2) European Industrial Relations Observatory

For the other 14 countries which have a statutory minimum wage, there is no argument to suggest that it is having an impact on the prevalence of undeclared

work (see Table 3). The reasons for the absence of any impact are various, but in many cases it seems to be because of the low level of the minimum wage.

TABLE 3 → COUNTRIES IN WHICH THE STATUTORY MINIMUM WAGE HAS NO IMPACT, OR FOR WHICH THERE IS NO EVIDENCE

Country	Comments
Belgium	No specific evidence of any impact.
Bulgaria	There does not appear to be an impact, primarily because those on the minimum wage are exempt from social security contributions, thereby removing an incentive to undertake undeclared work.
Czech Republic	The government has been increasing the minimum wage on the basis that this would remove incentives for undeclared work. However, there is no evidence of such an impact, and the new government does not appear to be continuing with this policy.
Estonia	The impact is negligible, especially given that only around 5% of employees are on the minimum wage.
Ireland	There is no evidence of an impact. Breaches of the minimum wage have not been linked to undeclared work.
Spain	The minimum wage does not appear to be having an impact, especially because it is relatively low.
Lithuania	The minimum wage is very low and is therefore unlikely to be having an impact on the prevalence of undeclared work.
Luxembourg	There is no evidence of any impact.
The Netherlands	The minimum wage is well below the lowest wage levels and is therefore unlikely to be having an impact.
Portugal	The limited coverage of the minimum wage means that it probably has little impact. If the increases in its value are monitored and enforced as planned, it is likely that it will continue to have little impact.
Romania	The minimum wage is regarded as helpful in reducing undeclared work.
Slovenia	No evidence of any impact.
Slovakia	There is no specific evidence of an impact. However, the minimum wage has been increased above labour productivity growth and this <i>may</i> have acted as an incentive for undeclared work, particularly in small firms and low-paid sectors.
United Kingdom	There is no evidence of any impact. If the minimum wage level begins to have a detrimental effect on the availability of jobs in low paid sectors and occupations, it is more likely that individuals will turn to paid informal work, rather than to undeclared work.

4. THE IMPACT OF THE TAXATION AND SOCIAL SECURITY REGIMES

For the majority of countries, there are arguments that the taxation and social security regimes are having a strong impact on the prevalence of undeclared work. The exceptions are Ireland, the Netherlands, Spain and the UK. In Spain and the UK, the relatively low taxation levels are unlikely, on their own, to act as incentives for undeclared work. In Ireland and the Netherlands it is not the levels of

taxation that are impacting on undeclared work, but the rigour with which the taxation regimes are being implemented.

In all other countries, there are clear reasons for the links between tax and social security costs and undeclared work – and such links apply for both employers and employees. In most of these countries, it is the smaller employers who are most likely to use undeclared work to avoid tax and social security payments. These employers are also more likely to be able to avoid scrutiny. Amongst employees, it is the lower paid and lower skilled who are motivated to undertake undeclared work and avoid tax and social security payments.

TABLE 4 → SUMMARY OF THE IMPACT OF THE TAXATION AND SOCIAL SECURITY REGIMES IN EACH COUNTRY³

Country	The impact of the taxation and social security regimes
Belgium	High taxation and social security contribution levels are regarded as contributing to the prevalence of undeclared work.
Bulgaria	Taxation levels and social security contributions (for employers and employees) are relatively high and there are also perceived inequities in the tax regime. Together, these factors mean that the tax regime is an incentive for undeclared work. According to the employers' organisations, medium and large firms are (with minor exceptions) not involved in undeclared work. Traditionally, it has been small and micro-businesses, including the self-employed, that have used undeclared work.
Czech Republic	High taxation of labour and high social security contributions are regarded as strong incentives for undeclared work.
Denmark	Relatively high income and VAT tax rates may act as incentives for undeclared work. There have, however, been reductions in income tax rates since 2004, although these are minimal and there is no evidence of any impact on levels of undeclared work.
Germany	It is considered that the tax and social security contributions are incentives for undeclared work and that contribution levels need to be reduced, if undeclared work is to be controlled.
Estonia	High labour taxes are regarded as the main reason for undeclared work. Personal income tax rates are being decreased to encourage regular employment and the minimum tax rate for social tax has been increased to encourage self-employed people to declare larger proportions of their incomes. Personal contributions have a major role in determining the size of benefits. However, the benefit system includes few incentives for low-wage earners to undertake regular, declared work.
Ireland	The limited information available indicates that there are only tentative links between the size of the shadow economy and changes in taxation levels. However, it appears that increased rigour in the application of the tax regime is more likely to impact on undeclared work than are taxation levels themselves. Also, in specific industries – construction and meat processing – there is evidence of employers classifying workers as self-employed, thus increasing the likelihood of undeclared work.
Greece	The Greek tax regime is regarded as complicated, inequitable and unfair. Tax avoidance and tax evasion are regarded as being widespread; tax revenues and the tax base (as well as tax rates) have been declining. The tax burden for middle-income earners is being decreased and it is anticipated that this will increase incentives for regular, declared work. Social security contributions are high and it is likely that they act as an incentive for undeclared work.
Spain	Given the relatively low level of taxation, it is not likely that tax itself encourages workers to undertake undeclared work. There is an incentive for small businesses to use undeclared work, since they are taxed in relation to number of employees. Also, employers can save considerable social security costs (24% to 28% of paid wages) by not declaring work.
France	The tax and social security regimes continue to create disincentives to work, especially for the low paid. This is despite efforts to tackle the problem through a system of in-work benefits. In the early 1990s, France had the highest level of social insurance funded from social charges on employers. Since then, significant changes have been made to 'mutualise' the cost. However, it is argued by some that this has created further incentives for undeclared work, since the link between employment and entitlement to social benefits is weaker.
Italy	The main reasons for undeclared work appear to be based on employers' willingness to reduce labour costs by evading tax and social security contributions. Some employers employ workers as project contractors (parasubordinati) who then pay 23% (instead of 33%) for pension contributions.

(3) No information is available for Luxembourg

TABLE 4 (CONT.) → SUMMARY OF THE IMPACT OF THE TAXATION AND SOCIAL SECURITY REGIMES IN EACH COUNTRY

Country	The impact of the taxation and social security regimes
Cyprus	The burden of direct taxation has been reduced since 2004, but income tax and social security contributions are likely to continue to have an impact on the prevalence of undeclared work. Indirect taxation has increased and this is providing an incentive for undeclared work in the service sector. There are discussions about increasing social security contributions, with concerns about the impact on undeclared work.
Latvia	The major motive for undeclared work is likely to be tax evasion. There is an ongoing debate about the need to simplify the tax regime for SMEs and thereby remove incentives for undeclared work. The pension system has been revised, linking taxpayers' contributions to benefits, aiming to encourage payment and remove incentives to undeclared work. However, many argue that this is insufficient motivation to make tax and social security contributions rather than evade payments.
Lithuania	The taxation and social security regimes are the main drivers of undeclared work. Wages and salaries are relatively low, whereas tax and social security contributions are relatively high; these factors combine to act as a strong incentive for undeclared work.
Hungary	Income tax is high and this is regarded as having an impact on the prevalence of undeclared work. Likewise, social security contributions are seen as being strong incentives for undeclared work.
Malta	In recent years, income tax levels have been decreased and tax bands revised, thereby reducing an incentive for middle income earners to undertake undeclared work. Corporation tax is charged at a relatively high rate (35%), although it is not clear whether this has any impact on levels of undeclared work used by employers. It is regarded that there is widespread abuse of the VAT system, especially by self-employed people. The difference between the minimum wage and unemployment benefit is small and may provide an incentive for unemployed people to remain on benefit, and supplement their income with undeclared work.
The Netherlands	Due to strict controls it has become harder to hire workers without paying tax and social security contributions (especially the case in sectors where there are large numbers of temporary, seasonal workers). Cash-in-hand workers are not likely to pay tax, but less than 5% of the working population are involved in cash-in-hand work.
Austria	The relatively high VAT and income tax rates and high non-wage labour costs are the main reasons for undeclared work. Estimates show that about half of the increase in the black economy is due to increased tax and social security contributions.
Poland	The tax regime is regarded as a strong incentive for undeclared work, especially for low wage earners. High taxation levels are accompanied by many alternative sources of income from public resources (retirement pension, disability pension, unemployment benefits, social assistance benefits), as well as undeclared work; this is not conducive to undertaking declared work.
Portugal	The corporate income tax rate was reduced in 2005 (from 30% to 25%) and control measures were strengthened. It is not possible however to identify if the reduction in the rate led to any reduction in undeclared work. The tax regime for self-employed people is likely to provide an incentive for undeclared work. Firms with low turnover benefit from a simplified tax system and a low rate of 20%; it is concluded that this has decreased undeclared work. There are stricter controls on larger firms; this suggests that undeclared work is not used by them. It is not possible to identify if the social security regime impacts on undeclared work. Employers regard their social security contributions as high, suggesting that they act as an incentive for undeclared work. However, employers are aware that inspection and control measures have been increasing in recent years.
Romania	The government introduced a flat rate (of 16%) income tax regime in 2005. This has been one factor (among many) likely to have contributed to the growth of the economy. However, there are no proper evaluations or assessment of its impact on the prevalence of undeclared work. Arguably, the flat-rate tax regime could help in reducing the prevalence of undeclared work, if maintained long enough. An assessment of all the relevant factors would however need to be undertaken. Overall however, given the complexities of factors that lead to undeclared work, such a measure does not constitute a panacea in combating undeclared work. The social security regime is similar to the taxation regime in that steady reductions in the contribution rates for various mandatory social security schemes signal the importance attached by national government to the problems created by undeclared work. Arguably, optimal thresholds have now been reached and further reductions in contribution rates may backfire. Again no proper evaluations or assessments have been carried out on the impact of the social security regime on the prevalence of undeclared work.
Slovenia	The gradual abolition of the payroll tax is underway to increase the attractiveness of work. Personal income tax rates have been reduced across the board.
Slovakia	Since 2004, all corporate and individual income is taxed at a flat rate of 19%. Most of the tax exceptions have been abolished, and income taxation has decreased for almost all taxpayers. This had a positive effect on declaring work since there are fewer incentives to move income to a lower tax base. However, high social security costs continue to provide motivation to employ on low/minimum wages. The system is complicated; social contributions are levied on the income from employment, whereas taxes are levied on all types of income. This offers a means of minimising or avoiding social security payments.

TABLE 4 (CONT.) → SUMMARY OF THE IMPACT OF THE TAXATION AND SOCIAL SECURITY REGIMES IN EACH COUNTRY

Finland	Incentives to work are not strong since taxation is high, social security is generous and public services are free. These factors appear to act as a disincentive to work, and an incentive for undeclared work.
Sweden	Tax avoidance (coupled with high taxation levels) appears to be the most cited reason for undertaking undeclared work (as reported in the 2006 Tax Agency study). This is the motive cited mostly by men, the self-employed and the well educated. Doing so is generally regarded as a 'minor offence', with a perception that there is little chance of being caught. It is generally accepted that relatively high social security contributions have been acting as an incentive for undeclared work. A Tax Agency report in 2007 recommends a lower rate of social security contributions (20%, rather than 32%) for employers who are private individuals.
United Kingdom	The relatively low income tax levels are considered to reduce incentives for undeclared work. However, the increase in the overall tax burden over the past decade is problematic for both businesses and individuals. There are two important issues for businesses – the complexity of the tax regime and the large scale of indirect taxes. The fact that formal employment, especially for those on a low income, is becoming increasingly temporary and unreliable is not always an incentive to leave benefit. Tax credits provide support for those on low incomes but create a disincentive for a second earner in a family to work formally.

5. MEASURES AIMED AT TACKLING UNDECLARED WORK

There continues to be an extensive range of measures being implemented in Member States to tackle undeclared work. Many of these measures are not aimed solely at reducing undeclared work, but are seeking to achieve other goals, such as increased employment and stimulation of enterprise which have an indirect effect on undeclared work.

Whilst all Member States clearly have an interest in undeclared work, there are several in which political interest is especially high.

- In Cyprus, undeclared work was not until recently considered a high priority and, for example, it was almost taken for granted that self-employed people would pay little, or no, income tax. The government has now acknowledged that there are relatively large sources of 'additional' tax revenue hidden in undeclared work.
- France has shown an interest in the issue over a longer period, since 2000, and has demonstrated this in the 2004-05 and 2006-05 National Action Plans for the Fight Against Undeclared Work.
- In Italy there has been a lot of political interest in undeclared work in the past three years, prompted by several fatal accidents amongst undeclared workers in the construction industry. Tackling undeclared work is linked with discussions about the reform of the unemployment benefit system and possible moves toward flexicurity principles. However, given the size of the informal economy in Italy, any such changes may provide further unintended incentives for undeclared work.
- In the Netherlands, the government has had a programme (Handhavingsprogramma, 2003-06) to tackle undeclared work for some time. However, there have been concerns about the low rates of detection of undeclared work as 'fraud'; as a result, a new programme focused on stronger enforcement has been implemented.

- In Portugal, the political interest in undeclared work has declined as other concerns have come to the fore (e.g. recession, unemployment and immigration). However, the link between immigration and undeclared work has been acknowledged and incentives have been introduced to encourage immigrants to participate in declared work. The government published proposals in 2006 to introduce elements of flexicurity to the labour market, although these do not address undeclared work specifically.
- In Romania undeclared work has always been high on the political agenda. Economic growth in recent years has highlighted further the dangers of undeclared work and this has prompted the introduction of measures to tackle it. Romania's first National Reform Programme contains strong awareness of undeclared work as an issue and signals measures capable of tackling undeclared work. Assessments of the impact of these measures on undeclared work are however regrettably absent.

Table 5 summarises the measures which have been introduced by Member States in recent years and thereby provides an update to the measures listed in the 2004 Review.

It can be seen that there are many examples of measures designed to bring about stronger enforcement of actions against undeclared work; 21 countries have recently introduced new enforcement measures (and eight of these are new Member States). The other most prominent category of measure concerns subsidies and tax reductions, aimed in general at providing incentives for declared work; 16 countries have introduced such measures in recent years. Social awareness campaigns have been used by ten countries and measures to reduce the administrative burden on businesses and individuals by six countries.

It is too early to comment on the success of these measures. Most of them are recent initiatives, although their evaluation would be useful in order to identify 'good practice' to recommend to other Member States.

TABLE 5 → MEASURES AIMED AT TACKLING UNDECLARED WORK

Country	Specific measure
Reduction of administrative burdens on businesses and private individuals	
Estonia	Reduction of legislative and administrative burdens with the help of e-services and using IT solutions to provide services to businesses.
Greece	Measures are being introduced to support entrepreneurship (especially amongst SMEs). These measures are likely to remove some of the incentives for undeclared work.
Spain	Measures are being introduced to improve the working conditions and benefits for the self-employed. This should remove some incentives for undeclared work.
The Netherlands	The procedure for issuing employment permits for employees from certain countries has been simplified in an effort to reduce the number of illegal workers. Procedures for declaring tax, for individuals, have been simplified.
Portugal	The procedures for setting up new enterprises have been simplified.
Slovakia	The procedures for setting up new enterprises have been simplified. Services have been provided to support workers in transition from undeclared work to regular work.
Subsidies and tax reductions (including incentives to work in the formal economy)	
Belgium	Reductions in tax and social security contribution levels, to provide incentives for declared work.
Bulgaria	Reductions in tax and social security contribution levels are being introduced in 2007, although the scope of excise duty is being extended. The net result may have a neutral impact on undeclared work.
Czech Republic	A reduction of the tax rates for lower income earners was introduced in 2006, to provide an incentive for declared work.
Denmark	The scope of the Home-Service Scheme (introduced in 1994, to pay a subsidy to households buying household services), has been tightened over the years – from an original subsidy of 50% of the costs and to a narrower range of eligible households. This has probably resulted in an increase of women in undeclared work; there are now demands to widen the scheme again, in order to reduce undeclared work.
Estonia	Reduction of taxes and social security reforms.
Spain	The status of foreign workers was regularised in 2005. This resulted in 500,000 immigrants becoming legal workers. Measures were introduced in 2006 aimed at encouraging permanent work, through monetary incentives including reductions in social security contributions. Measures have recently been introduced to improve working conditions in domestic services. This will improve working hours, offer unemployment benefits and increase the costs of firing such workers. Tax reforms have been introduced to benefit lower earners (a 17% saving for 60% of taxpayers).
France	VAT on renovation work in private homes and on personal services was reduced (leading to the creation of around 50,000 jobs in two years). A measure (introduced in 2001) which allows unemployed people to start work without immediate loss of benefits has been widened.
The Netherlands	Tax credits for everyone in paid employment have been introduced to make paid employment more gainful, especially for people at the lower end of the labour market. An attempt has been made to legalise illegal cash-in-hand work, such as household services. The number of hours above which social security contributions need to be paid is now fairly high.
Austria	A service voucher scheme for household services has been introduced in the care sector. Only workers holding a work permit are eligible and take-up has been less than expected.
Poland	The social insurance burden for the newly self-employed was reduced in 2005. In the first 24 months of self-employment, the basis of assessment is decreased to 30% of the minimum wage.
Portugal	Incentives have been introduced for unemployed people to participate in regular work rather than undeclared work.
Romania	A flat rate income tax was introduced in 2005. This, and steady reductions in social security contribution levels, are presented in the National Reform Programme as key measures to tackle undeclared work. A recent measure by the social partners introduces a higher minimum wage for workers with high educational attainment. This is expected to tackle under-declaration of incomes amongst better educated employees, especially prevalent amongst SMEs.
Slovakia	A flat rate of income tax has been introduced to increase incentives to declare activity.
Finland	A temporary low-wage support measure was introduced in 2006 to stimulate employment of older, low-income workers. The tax allowances for household services has been increased and also expanded to cover care services and renovation work.
Sweden	A tax deduction for household services is being introduced from 1 July 2007. The Government has recently stated that it will decrease social security contributions in some service sectors (those in which undeclared work is most prevalent).
United Kingdom	There are some pilot projects aiming to help people to legitimise their work activity. An in-work benefit (Working Tax Credit) is used to encourage people to take up formal employment.

Increased regulation of the labour market	
Czech Republic	Introduction (from 2004) of stricter conditions on the type of jobs which can be performed by self-employed people (instead of regular employment contracts).
Cyprus	A law has been implemented (January 2006) that requires compulsory tax returns for those earning above CYP10,000, self-assessment by the self-employed, penalties for the late submission of tax returns, and submission of audited accounts by the self-employed earning above CYP40,000.
Malta	There are active labour market policies designed to bring about a shift from undeclared work to regular work. These include measures targeted at female workers (since females are regarded as making up a large part of the underground economy).
Romania	The statutory minimum wage in Romania has been regarded as an important tool to tackle undeclared work. It is not argued that the minimum wage increases the incentives for undeclared work.
Addressing labour market rigidities	
Bulgaria	There are programmes for those disadvantaged in relation to the labour market (e.g. the 'From Social Assistance to Employment' programme will, in 2007, guarantee employment to 27% of the unemployed – it will use 72% of the budget for active labour market policies).
Czech Republic	Part-time occasional work arrangements for registered unemployed are allowed (from 2004). This has created opportunities for unemployed people to work while receiving unemployment benefit (up to a level of 50% of regular working hours, or half the minimum wage).
Ireland	There are several measures that, while not primarily designed to discourage undeclared work, have that effect: Back to Work, Back to Education, and Family Income Supplement, as well as disregards and tapers in the taxation regime. The impact of these measures has been strengthened, since their value to individuals has been increased. Also, the Activation Measures are an important means of discouraging undeclared work; they provide 'progression paths' for long-term unemployed people into work or training.
Greece	A new law is being drafted which will include a fund to provide indefinite employment benefits to older workers in high unemployment areas.
United Kingdom	Various initiatives, for example 'New Deal', provide substantial support for the unemployed to enter formal work and have recently attempted to disrupt informal work by conducting work force interviews at unpredictable times and at short notice.
Stronger enforcement	
Belgium	Electronic registration of migrant workers' movements in and out of the country, and of any foreign business activity. Improved mechanisms for exchange of information between agencies.
Czech Republic	Introduction of more stringent conditions for registration and extension of the powers of the inspection authority (from October 2004). Further restrictive measures (e.g. inspections in the workplace by employment offices and labour inspectorates, financial penalties for undeclared work) introduced in 2007.
Denmark	Stronger controls and enforcement have been introduced since 2004 in specific sectors (e.g. construction and hospitality). There has also been new legislation to give the tax authorities greater access to construction sites in order to monitor employers' records.
Germany	In 2004, a new law redefined undeclared work to exclude non profit-oriented activities, and the competences of customs authorities were extended, penalties increased, and the non-payment of social contribution rates was made illegal. Tax fraud by private households in relation to 'mini jobs' became an administrative offence.
Estonia	Recently introduced control activities include additional company inspections, analysis of samples of companies and follow up of irregularities. As a result of these measures, the proportion of legally paid wages has increased.
Greece	A measure has been introduced to regularise undocumented migrant workers (through three 'regularisation' exercises). There is also a new law intended to simplify and rationalise resident and work permit rights for migrant workers. A further new law is being drafted which will reduce employers' social security contributions for employees under local collective agreements. It will also modernise the Labour Inspectorate.
France	Sanctions have recently been strengthened (e.g. in certain sectors the level of inspections has increased by 14% since 2005 and the number of inspections of individual workers suspected of undertaking undeclared work has increased). A new sanction involves the right to remove public assistance and tax credits/subsidies for SMEs using undeclared work.
Italy	There were several measures in place before 2004; action has been taken to enforce them more strongly. The Biagi Law (2003) outlaws unjustified <i>parasubordinati</i> contracts (project workers); from 2006, it has been more strongly enforced. Newer measures include the so-called Decreto Bersani. This allows for construction sites to be shut down if more than 20% of the total workforce are involved in undeclared work, and for a range of other control measures and penalties. The Budget Law for 2007 also introduced some important measures, including stronger inspection activities and fiscal incentives for hiring workers on open-ended contracts.
Cyprus	Enforcement is being stepped up, to prevent the employment of illegal workers.
Lithuania	Stricter control procedures and additional sanctions have been introduced since 2004.
Luxembourg	A 2006 law proposes to improve the efficiency and operation of the Inspectorate of Labour and Mines.

TABLE 5 (CONT.) → MEASURES AIMED AT TACKLING UNDECLARED WORK

Hungary	Stricter controls of workplaces, especially in construction and agriculture, have been introduced. In 2008, there will be stricter control over the granting of disability certificates (it appears that many workers with certificates undertake undeclared work).
Malta	A new law (2005) is aimed at regulating foreign workers and controlling illegal employment. There are several measures aimed at detecting social security benefit abuse.
The Netherlands	Controls against employers who pay less than the minimum wage per hour will be tightened up.
Stronger enforcement	
Austria	Recent measures have concentrated on stricter enforcement, including additional staff in the inspection organisations. In 2006, fines for illegal employment of foreign workers were doubled.
Portugal	Measures have been introduced to strengthen the inspection and control of the tax and social security regimes (e.g. including steps to combat under-declaration of income).
Slovenia	The competences of inspectorates have been enhanced to enable them to issue administrative measures and fines. Joint inspections between several agencies are now undertaken.
Slovakia	Measures include a massive inspection campaign, stronger surveillance and the enforcement of appropriate sanctions.
Finland	Several measures have been introduced including obligatory personal IDs for construction site employees, and closer scrutiny of migrant workers in businesses using foreign labour. A specific project (VIRKE) has aimed to improve cooperation between the tax authorities, police and customs.
Sweden	The Swedish Tax Agency was given additional staff in 2006 and 2007 to introduce increased tax controls and audits. In the 'high risk' sectors of restaurants and hairdressers, employers have been required to keep staff registers, from January 2007. Construction sector social partners have agreed to the introduction of this requirement.
United Kingdom	The inspection authorities take predominantly punitive measures, through prosecution, to reduce informal work when linked to benefit fraud and tax evasion.
Tax amnesties	
Cyprus	A tax amnesty programme was introduced recently.
Awareness raising campaigns	
Bulgaria	A public debate on the problems of undeclared work was held in 2005 (by the social partners – trade union confederation). A social awareness campaign – 'In the Light' – began in May 2007, run by the Bulgarian Industrial Association.
Denmark	Since 2004, there have been campaigns to change attitudes to undeclared work, e.g. Fair Play, an information campaign run with the social partners to challenge tax evasion, with a special focus on young people.
Germany	Public alliances against undeclared work between the social partners and government were established in construction and transport. Specific measures undertaken include public information campaigns.
France	A 'good practice charter', agreed by sectoral representatives, has been implemented for the construction sector.
Lithuania	Since 2004 there have been extensive information campaigns in the media to raise public awareness of the problem of undeclared work.
Austria	Awareness raising campaigns are being considered as a future option.
Romania	The National Tax Collection Office runs a campaign to warn against undeclared work. The British Embassy ran a campaign to highlight the dangers of illegal migration for work in the UK.
Slovakia	A sizeable media campaign has been used to raise awareness.
Sweden	Efforts have been made to raise social awareness through joint information campaigns by the tax authorities and the Economic Crime Authority. Some campaigns have also been undertaken with the social partners (e.g. in the construction sector).
United Kingdom	There have been several high-profile campaigns aiming to deter fraudulent benefit claims.

6. CONCLUSIONS

This update of the position on undeclared work across the European Union, since 2004, demonstrates relatively little change in the prevalence and the distribution of undeclared work in Member States' economies. It is clear that there continues to be much interest in most countries in the impact of the taxation and social security regimes; concern about possible impact of the minimum wage is less pronounced.

A common feature of this update and the 2004 Review is the relative lack of specific data, or studies, of undeclared work. There are a few exceptions to this, but on

the whole, the level of attention given to undeclared work at a political and policy level is not reflected in the rigour, or the range, of the research on the issue. It must be acknowledged, however, that there are significant difficulties involved in measuring undeclared work.

There continues to be a wide range of measures being used by Member States to tackle the problem of undeclared work. Most of the measures in question have a wider range of objectives and are not specifically designed to address the issue of undeclared work. Many concern enforcement and initiatives aimed at providing incentives for declared work. Given the impressive range of measures being implemented, it will be useful to see the outcome of evaluations of their effectiveness.

ANNEX: PROBLEMS OF ESTIMATING AND MEASURING UNDECLARED WORK

The *EEO Review: Autumn 2004* highlighted the problems associated with measuring undeclared work. These problems still exist.

Indirect measurements include the following:

- *Monetary methods*, such as the measurement of the ratio between cash and demand deposits. These methods assume that most transactions in the underground economy are carried out in cash, which makes it difficult to distinguish between legal and illegal activity. OECD experts, in compiling their handbook on measuring the non-observed economy (OECD (2002) *Handbook for measurement of the non-observed economy*), therefore concluded that this kind of method is of limited use.
- *Labour accounts method*. This involves the comparison of labour market data (i.e. gathered through the Labour Force Survey) with data on labour market participation gathered from other sources (i.e. from household surveys).

- *Econometric modelling*. Such models use certain indicators of an undeclared part of the economy and a set of supposed determinants, and gather indications of its size through modelling.
- *Electricity consumption*. These estimations compare the amount of energy required in declared activities and compare them with measurements of actual consumption. This method assumes that most undeclared labour is energy intensive and these findings are generally not perceived to provide a very accurate picture of the size of the underground economy.

Direct measures are based on survey evidence although there are a number of difficulties with such methods:

- Few such surveys have been carried out and time series are generally not available.
- Limited comparability.
- Veracity of findings depend on quality of questionnaire and skill of interviewers.
- Potential of under-reporting due to disinclination to report underground activity.

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APPENDIX: SUMMARY OF NATIONAL ARTICLES PRODUCED BY SYSDÉM EXPERTS SPRING 2007

Country	Prevalence of undeclared work (UDW)	Role of minimum wages	Role of taxation regime	Role of social security regime	Strategies and measures towards combating undeclared work
Belgium	<p>The preferred definition of UDW in Belgium is a broad one, including undeclared income and fraud.</p> <p>Estimates of the prevalence of UDW vary greatly, from 6% to 20% of GDP. The lower figures derive from measures which use national accounts, with the higher figures coming from macroeconomic studies. The sectors which have the highest levels of UDW are construction, household services, food and drink, hospitality and health care, the latter being to a lesser extent.</p> <p>Since 2004, a study of the construction industry has found high levels of UDW, through the 'pyramid of subcontracting' which is prominent in the sector. Regional differences were observed, with more UDW in areas with persistently high unemployment rates.</p> <p>There is limited evidence on the profile of the UDW worker, and even less recent evidence. However, it is accepted that independent workers and firms are those groups most inclined towards UDW.</p>	No specific reference to the impact of the minimum wage.	<p>There are traditional reasons for high levels of UDW in Belgium: high taxation levels, red tape, high levels of independent work, high incidence of immigrant workers, and a mistrust of the state.</p> <p>Recent evidence suggests that Belgium is performing poorly in the basic functions of administration and justice; this may be contributing to low levels of tax compliance (and therefore relatively high UDW, amongst other effects).</p>	The impact of the social security regime is similar to that of the taxation regime, in particular the high social security contribution levels are likely to be an inducement to UDW.	<p>Interest in Belgium in tackling UDW is high. Measures were introduced several years ago. They included: reduction of taxation, administrative simplification, increased controls and increased penalties. The newest initiatives include electronic registration of migrant workers' movements in and out of the country, electronic registration of any foreign business activity, and improved mechanisms for exchange of information between agencies.</p> <p>Despite an extensive range of control measures, there remain weaknesses in enforcement and punishment. Although the interest and awareness of UDW over the years has been high, the current political will to increase control measures is not apparent.</p> <p>However, there is agreement between government and social partners about the need to tackle UDW. There are specific agreements (2005), for example, covering the construction, cleaning, transport and surveillance sectors. There are also some positive measures in place to provide incentives to declare work. These primarily concern reductions in tax and social security contribution levels.</p>

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Bulgaria	<p>No data based on the national accounts have been published since 2002. Survey data, however, show that the 'grey economy' has been increasing markedly since 2004 and that it covers about 35% of the economy. The sectors which account for most UDW are agriculture, construction, hospitality, motor trade services and personal and household services. Immigrant workers, students, retired people and migrant Bulgarian workers who move in and out of the EU account for most of the UDW.</p>	<p>The minimum wage does not appear to have an impact on the prevalence of UDW in Bulgaria. This is because people receiving the minimum wage are exempt from social security contributions, thereby removing a large incentive for UDW. In addition, social partners negotiate minimum income levels each year for various groups; these income levels are also exempt from social security contributions.</p>	<p>Taxation levels (for employers and employees) are relatively high. There are also perceived inequities in the tax regime. Together, these factors mean that the tax regime is an incentive for UDW (for the non-declaration of income). According to the employers' organisations, medium and large firms are (with minor exceptions) not involved in UDW. Traditionally, it has been small and micro-businesses, including the self-employed, that have used UDW. Their use of UDW seems to be caused by the challenging economic climate in which they operate, and the relatively heavy tax and social security burden.</p>	<p>Like taxes, social security contributions are high. The social security regime therefore has the same incentive for UDW as the tax regime.</p>	<p>Interest in UDW has been high in Bulgaria since 2004. Social partners have been pressing the government to take further action to tackle UDW, and the government is concerned about the high levels of lost revenue as a result of UDW. There are reductions in tax and social security levels being introduced in 2007 (although these are not changing some of the perceived unfairness in the regimes). However, excise duty will be payable on more goods. These two changes are likely to result in a neutral impact on UDW. There are also programmes for those disadvantaged in relation to the labour market (e.g. the 'From Social Assistance to Employment' programme will, in 2007, guarantee employment to 27% of the unemployed – it will use 72% of the budget for active labour market policies). A social awareness campaign – 'In the Light' – was started in May 2007 by the Bulgarian Industrial Association. A public debate on the problems of UDW was also held in 2005 (by the social partners – trade union confederation). The impact of these measures has not yet been evaluated, but this article suggests that there are grounds for 'negative expectations'.</p>
Czech Republic	<p>The incentives to participate in UDW remain high. Although the estimates of the scope of this phenomenon differ, they all agree on its significance in the economy (especially in construction, agriculture, catering, trade and textiles). UDW is dominated by low skilled male workers (sometimes even (...))</p>	<p>For several years the government has been increasing the statutory minimum wage at rates surpassing the growth of nominal wages. In 2006 it reached 40% of average wages in the whole economy. These increases were guided by the opinion that a high statutory minimum wage is enhancing declared (...)</p>	<p>One of the two main incentives supporting the existence of UDW is the high taxation of labour, including social security contributions and personal income tax. (The other being the dysfunctional system of work permits for foreign workers.) Given that undeclared (untaxed) revenues constitute the primary motivation (...)</p>	<p>The Czech Republic provides guaranteed welfare income for families, which is close to the average wage level, which lowers the poverty rates, but can also be demotivating in the search for legal employment. The current Civic-Democratic government is concerned with the extent of pro-work (...)</p>	<p>The issue of UDW is not a high priority in the new government's reform agenda. Some steps to improve the situation using the taxation system have been carried out. The lowering of the personal income tax rates for the two bottom income brackets took effect in 2006 and somewhat increased the (...)</p>

Country	Prevalence of undeclared work (UDW)	Role of minimum wages	Role of taxation regime	Role of social security regime	Strategies and measures towards combating undeclared work
Czech Republic (cont.)	<p>(...) highly skilled), not only unemployed, but also self-employed and with regular official employment contracts. The most common practice of UDW consists of tax evasion in small companies, undeclared earnings from secondary jobs, UDW activities of registered unemployed and high rates of illegal employment of foreign workers in construction and services.</p>	<p>(...) work attractiveness among low skilled workers and has minimal adverse impact on labour demand. There is no credible evidence of this impact, and the new government does not seem to be following this policy.</p>	<p>(...) for UDW, there are recommendations made by academic researchers to substantially simplify tax legislation and collection and to introduce measures to eliminate room for disguising regular employee-employer relationships as self-employment.</p>	<p>(...) activation incentives provided within the Czech social support system, which are likely to lower the official-work disincentives for unemployed workers. There is strong evidence that pretended sickness is being widely misused due to the relatively generous and weakly supervised sickness insurance scheme. People claim sickness benefits and perform UDW. Czechs have one of the highest rates of sickness absence in the EU (on average, some 7% of the workforce is sick at any given time). The length of sickness is associated with the regional level of wages as well as unemployment, which may be related to abuse of the scheme.</p>	<p>(...) attractiveness of declared work, especially for single workers. Important measures to combat UDW have been introduced by the new Employment Code which came into effect in October 2004: introduction of more stringent conditions for registration and increased incentives for employment, extension of the power of the District Labour Offices as an inspection authority. The code also imposed stricter conditions on the type of jobs to be performed by the self-employed (who are subject to lower implicit taxation including social security and other contributions) instead of regular employee-employer contracts. The new Employment Code also allowed for part-time occasional work arrangements for registered unemployed. It created opportunities for unemployed people to work while receiving unemployment benefit, up to a level of 50% of regular working hours or half the minimum wage. The new Labour Code drafted by the MoL and the trade unions, effective in 2007, also introduced further restrictive measures (e.g. inspections in companies and at the workplace by employment offices and labour inspectorates, financial penalties for UDW). The evaluation of measures to combat UDW is hard due to the insufficient policy response to UDW and even the lack of measures. The lack of a significant reform of the work-permit and immigration procedures is the most harmful missing policy related to UDW.</p>

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Denmark	<p>There are many studies of UDW in Denmark, even though the overall prevalence is very low (similar to other Scandinavian countries). The main source of data on prevalence is a regular survey, conducted since 1994. It shows that UDW has been decreasing since 2001, measured as a percentage of GDP. It had been increasing in the 1990s, but is now down from a peak of 3.8% of GDP in 2001, to 3.0% in 2005. The main reasons for the decline are: a shift in undeclared hours worked to the regular economy (possibly as a result of a Government information campaign), increased control of UDW by the authorities, and increased involvement by the trade unions (protection against impact of illegal immigrant workers). There is evidence that the decrease in UDW masks an increase in UDW amongst women. A main explanation for this is that most male UDW is in the construction sector and that sector has been subject to rigorous control in recent years to minimise UDW.</p>	<p>There is no minimum wage in Denmark, although the relatively high level of wages (coupled with high taxation levels) may act as an incentive for UDW.</p>	<p>Relatively high income and VAT tax rates may act as an incentive for UDW. The taxation regime has been changed since 2004 – income tax rates have been reduced. However, there is no evidence of any impact on UDW levels; the reductions in tax rates are minimal (for a low-income earner, from 45.5% in 1999, to 42.9% in 2006).</p>	<p>No commentary on social security.</p>	<p>The Government has used several initiatives to limit the scale of UDW. The Home-Service Scheme was introduced in 1994, to pay a subsidy to households which buy household services such as cleaning and gardening. It was intended to reduce the amount of UDW in such services, by removing the incentives for UDW. Its scope has been tightened over the years (from an original subsidy of 50% of the costs and to a narrower range of eligible households). This has probably resulted in an increase of women in UDW; there are now demands to widen the scheme again, in order to reduce UDW. Since 2004, other measures have been introduced to minimise UDW:</p> <ul style="list-style-type: none"> • stronger control and enforcement (e.g. in specific sectors such as construction and hospitality); • campaigns to change attitudes to UDW, e.g. Fair Play, an information campaign run with the social partners to challenge tax evasion, with special focus on young people; • tax regime enforcement – e.g. new legislation to give the tax authorities greater access to construction sites in order to monitor employers' records.
Germany	<p>According to macroeconomic estimates, the hidden economy and UDW had been in decline in Germany until 2006. In 2007, the level is expected to rise by about 1%. This is due to the rise in the VAT rate, the rise of mini-job taxation, the abolition of housing allowances, the (...)</p>	<p><i>No minimum wage</i></p>	<p>The tax wedge is seen as the main determinant of the volume of the shadow economy. The reduction of hidden activities requires the reduction of taxes and social insurance premiums. However, UDW also emerges if unemployment is high and income prospects poor. The growth of the (...)</p>		<p>A new law was adopted in 2004 to combat UDW and tax fraud. UDW was redefined to exclude non profit-oriented activities, the competences of customs authorities were extended, penalties raised, and the non-payment of social contribution rates was made an element of crime.</p>

Country	Prevalence of undeclared work (UDW)	Role of minimum wages	Role of taxation regime	Role of social security regime	Strategies and measures towards combating undeclared work
Germany (cont.)	<p>(...) additional tax on top incomes and the increase of contributions to pension and health insurance. UDW is most prevalent in the construction and hotel and catering sectors. This is confirmed by survey-based estimates. UDW appears to be more or less accepted by the population, especially in the activities of private households.</p>		<p>(...) shadow economy was also attributed to the rise and persistence of unemployment in Germany.</p>		<p>Tax fraud by private households in the area of mini jobs became an administrative offence. Public alliances between the social partners and the federal and regional government against UDW were established in the sectors of construction and transport. Specific measures undertaken include public information campaigns and improvements in the information flows.</p>
Estonia	<p>The share of UDW has decreased to about 7-8% of GDP, which is relatively high compared with the EU-15, but one of the lowest amongst the new Member States. Envelope wages have also been decreasing. Tax evasion is the main reason behind the UDW in Estonia. In public opinion, UDW has become less acceptable.</p>	<p>The impact of the minimum wage on UDW is negligible. The share of employees on the minimum wage is only around 5%.</p>	<p>High labour taxes are the main reason for UDW. The implicit tax rate on labour is around 38%. To reduce labour and capital costs and encourage regular employment, the personal income tax rates are decreasing. Also, the minimum tax rate for social tax has increased forcing self-employed people to declare a larger share of their activities.</p>	<p>Social tax contributions have been personalised since 1999 and many benefits are directly related to personal contributions and hence provide incentives for formal employment. Personal contributions have a major role in determining the size of benefits. However, the benefit system creates a number of situations where there are few incentives for low-wage earners to enter formal employment.</p>	<p>One of the most successful policies has been a reduction of legislative and administrative burdens with the help of e-services and using IT solutions to provide services to businesses. Other policies include lowering taxes, social security reforms where personal contributions have a major role in determining the size of the benefits, and the control activities undertaken by the authorities. The measures to increase controls over UDW include different cooperation agreements between different state institutions mainly aimed at information exchange and raising public awareness. Control activities include company inspections, analysis of samples of companies and following up irregularities, as well as activities of local government. As a result of these, the proportion of legally paid wages has increased alongside the tax funds. Reforming the employment law remains an important challenge. The current legislation, outdated in many (...)</p>

Country	Prevalence of undeclared work (UDW)	Role of minimum wages	Role of taxation regime	Role of social security regime	Strategies and measures towards combating undeclared work
Estonia (cont.)					(...) ways, may induce UDW and increase the use of self-employment with lower social protection rather than regular employment.
Ireland	<p>There is no new evidence which challenges the 2004 estimates of prevalence. However, there is some doubt now about the measures mainly used (they were based on cash holdings). However, other estimates (e.g. based on GNP aggregates) indicated similar results.</p> <p>Note – the paper discusses tax evasion and the shadow economy, as 'proxies' for UDW.</p>	<p>A minimum wage was introduced in 2001 but there are no specific studies of its impact on UDW. It could be that employers would engage employees on an UDW basis in order to pay below the minimum wage. Large inflows of migrants can be an incentive for some employers to use UDW to avoid the minimum wage. While individual such cases have emerged, there is no evidence of this; breaches of the minimum wage have not been linked with UDW.</p>	<p>There are only tentative links between the size of the shadow economy (= UDW) and changes in taxation levels. However, recent evidence suggests that increased rigour in the application of the tax regime is more likely to impact on UDW than are taxation levels (fraud investigations have uncovered large-scale evasion of tax, mainly by well-off individuals, who were declaring only part of their incomes). Greater access to bank accounts by the Revenue authorities has been a significant feature here. Also, in specific industries – construction and meat processing – there is evidence of employers classifying workers as self-employed, thus increasing the likelihood of UDW.</p>	<p>See note on Activation under next heading</p>	<p>Ireland has several measures which are mainly intended to encourage persons to take up employment, but also discourage UDW: Back to Work, Back to Education, and Family Income Supplement, as well as disregards and tapers in the taxation regime. It can be argued that the impact of these measures has been strengthened, since their value to individuals has been increased. Also, the Activation Measures for the unemployed (jointly operated by the Department of Social and Family Affairs and FAS) are an important means of discouraging UDW; they provide 'progression paths' for long-term (3 months+) unemployed people into work or training. Many referred for interview leave the unemployed register, suggesting that they may have been involved in UDW. Thus, the Activation Measures are regarded as generating an additional deterrent to UDW. A Working Group – the Hidden Economy Working Group – is to be re-launched (under the 2007 Ten-Year Framework Social Partnership Agreement, 'Towards 2016'). It is an advisory group, and will promote more effective ways of tackling UDW.</p>

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Greece	<p>Quantitative data on the prevalence of UDW are not available. It is, however, generally accepted in Greece that the 'informal sector' is large, 24-30% of GDP. It has led to Greece's GDP for 2001-06 being revised upwards by over 25% (as a result of bringing the shadow economy into the figures). The revised GDP data are currently being validated by Eurostat. The Greek employment structure lends itself to a high prevalence of UDW – a high proportion of self-employed, immigrants and family workers, especially in agriculture.</p>	<p>There are no data on the impact of the minimum wage, but (especially given that it is set close to average blue-collar earnings) it is likely to be providing an incentive for UDW. The main employers' association (SEV) has argued for the ability to recruit young people at below the minimum wage. Doing this would remove some incentive to UDW.</p>	<p>The Greek tax regime is regarded as complicated, inequitable and unfair. Tax avoidance and tax evasion are regarded as being widespread. Tax revenues and the tax base (as well as tax rates) have been declining; the opposite of what is happening in most EU and OECD countries. The Government is introducing tax reforms which will reduce the tax burden for middle-income earners. It is anticipated that this will make the tax regime more employment-friendly and increase incentives for regular, declared work.</p>	<p>Social security contributions are high; they account for more than 34% of gross labour costs (the EU average is 31%). It is likely that this acts as an incentive to UDW.</p>	<p>Several measures have been introduced in recent years to tackle UDW. A measure which has had a real impact on levels of UDW is regularising undocumented migrants (through three 'regularisation' exercises). There is also a new law intended to simplify and rationalise resident and work permit rights for migrant workers. There are also measures being introduced to support entrepreneurship (especially amongst SMEs). These measures are likely to remove some of the incentives for UDW amongst SMEs and the self-employed (who have contributed disproportionately to the prevalence of UDW). A new law is being drafted which will include a fund to provide indefinite employment benefits to older workers in high unemployment areas. It will also reduce employers' social security contributions for employees under local collective agreements and will modernise the Labour Inspectorate. It is anticipated that these changes will reduce the level of UDW.</p>
Spain	<p>Figures show an increase from 2003 to 2006 (measured by number of workers undertaking UDW, up from 11.6% to 12.3%). Regularisation of Immigrants in 2005 appears to have caused a decrease in UDW, in construction and agriculture.</p>	<p>The minimum wage does not appear to be the explanation for the increase in UDW, especially because it is relatively low. Workers seem to accept UDW in order to receive higher earnings, saving both tax and social security costs.</p>	<p>It is reasonable to conclude that the tax regime does not itself provide strong incentives for UDW, except for those small businesses which are taxed in relation to number of employees. Given the relatively low level of taxation, it is not likely that tax itself encourages workers to undertake UDW.</p>	<p>Employers can save considerable social security costs by not declaring work – between 24% and 28% of paid wages.</p>	<p>Immigration and UDW are linked. Therefore the government regularised the status of foreign workers in 2005. This resulted in 500,000 immigrants becoming legal workers. UDW is also linked to the temporary nature of much employment. The government tackled this in 2006 with measures aimed at encouraging permanent work, through monetary incentives including benefits in social security contributions. Measures have (...)</p>

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Spain (cont.)					(...) recently been introduced to improve working conditions in domestic services. This will improve workers' rights (including working hours, right to unemployment benefits and an increase in firing costs). Tax reforms have been introduced to benefit lower earners (a 17% saving for 60% of taxpayers). This will help to discourage UDW. The government is encouraging self-employment and is introducing measures to improve the working conditions and benefits for the self-employed. This should remove some incentive for UDW amongst the self-employed.
France	Estimates of the size of UDW in the French economy depend on the method used for calculation. The report published by the Commission on undeclared work in the EU estimates the level of UDW in France to be between 4% and 6.5% of GDP. The sectors most affected by the phenomenon are construction, hotels and catering, other services and commerce. Statistics measuring the level of reported breaches of the legislation in relation to UDW in different sectors show an increase in such offences in all these sectors between 2003-2005 with the exception of 'other services' which have witnessed a significant decline.	The minimum wage, linked to a system of social security and other contributions for employers, can be seen to play a role in UDW. While the level of employer social contributions linked to the minimum wage is rather small, this cost is raised by contributions to pension funds and unemployment insurance. Another factor is the low marginal productivity of work at this pay scale and in these sectors which have no difficulties in recruiting staff.	Particularly for the low paid, the tax and social insurance system continues to create disincentives to work (and incentives to underreport activity), despite efforts to seek to address this problem through a system of in-work benefits.	High social insurance costs and other levies on enterprises have long been blamed for the persistence of UDW in the French economy. In the early 1990s, France had the highest level of social insurance funded from social charges on employers. Since then, significant changes have been made to this system in an effort to 'mutualise' more of the cost of social insurance. However, it is argued by some that this system has created further incentives for UDW as the link between employment and entitlement to social benefits is weaker. New ways of funding unemployment and social insurance benefits are currently being studied.	Since 2000, there has been a real willingness in France to give this issue higher priority as demonstrated by the formulation and implementation of the 2004-05 and 2005-06 National Action Plans for the Fight Against Undeclared Work, which have included incentive and disincentive measures. Among the successful measures were the reduction of VAT on renovation work in private homes and personal services. It was estimated that in the first two years of its operation in the early 2000s this measure created 34,000 jobs directly and 20,500 indirectly. The experiment has been extended throughout the EU until 2010 and a further evaluation will be carried out in France in 2007. In 2005 the European Council refused to apply the same measures to the catering industry. The new French (...)

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France (cont.)					<p>(...) President has committed himself to re-examining this issue. In the personal services sector, tax reductions, service vouchers and new tax credits for individuals legally taking on such staff should have the effect of reducing illegal immigration and UDW. Similar measures have also been taken to simplify employment in the area of live performance. Since 2001, measures have been put in place to allow unemployed individuals to start work without immediate loss of social insurance and other benefits. This system has been widened to reduce disincentives to work. Prevention measures have also included awareness raising and other voluntary measures, such as the 'good practice charter' agreed by sectoral representatives in the construction sector.</p> <p>The regime of sanctions applied has also recently been strengthened (e.g. in certain sectors the level of inspections has increased by 14% since 2005). A new law on SMEs also highlights greater controls and sanctions against UDW. Strengthened administrative sanctions include the right to remove public assistance and tax credits/subsidies for employers found guilty. There are also increasing numbers of inspections and sanctions for individuals engaged in UDW.</p>
Italy	<p>There has been much political interest in UDW in Italy over the past three years, prompted in particular by some fatal accidents amongst undeclared workers in the construction industry. The National Institute of Statistics and the Industrial Development Association in the south produce (similar) estimates of the prevalence of UDW, based on national accounts. Estimates show a reduction in (...)</p>	<p><i>No minimum wage in Italy.</i></p>	<p>The main reasons for UDW appear to be based on employers' willingness to reduce labour costs by evading tax and social security contributions.</p>	<p>As noted, evasion of social security contributions and tax appears to account for UDW. Some employers employ workers as project contractors (<i>parasubordinati</i>) who then pay 23% (instead of 33%) for pension contributions. But in the new notional defined contribution pension system benefits depend on contributions paid, and this will further decrease pension replacement rates.</p>	<p>Italy has several measures aimed at tackling UDW which were in place prior to 2004. Enforcement has not always been rigorous. For example, the Biagi Law (2003) outlaws unjustified <i>parasubordinati</i> contracts, but until 2006 it was not strongly enforced. Newer measures include the so-called <i>Decreto Bersani</i>. This allows for construction sites to be shut down if UD workers are 20% of the total workforce and for a range of other control (...)</p>

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Italy	(...) the proportion of GDP accounted for by UDW; from 7.6% of GDP in 2000 to 6.4% in 2006. However, this reduction depends almost entirely on the 2002 amnesty for illegal migrant workers (647,000 of them). UDW is highest amongst the lower productivity sectors and geographical areas: agriculture, services, construction, and in the south.				(...) measures and penalties for UDW. The Budget Law for 2007 also introduced some important measures, including stronger inspection activities and fiscal incentives for hiring workers on open-ended contracts. It also included the 'congruity indices' (<i>indici di congruità</i>) – these may be recommended as good practice for other Member States. These indices are to specify the number of labour hours required to produce a good or service, broken down by sectors, category of firm and geographical areas. Their values are to be negotiated between the government and social partners. Firms which do not fall into line with the appropriate index will then be subject to inspection. Employers' organisations are strongly opposed to the indices and negotiations with social partners about their value are still under way. Tackling UDW is seen as being linked with discussions about the reform of the unemployment benefit system and possible moves toward flexicurity principles. However, given the size of the informal economy in Italy, any such changes may provide further unintended incentives for UDW.
Cyprus	There are no official figures on the prevalence of UDW in Cyprus. However, it seems that the main types of type of UDW are by: illegal immigrants employed in legal work such as construction; the under-reporting of income by the self-employed; paid workers (including teachers and doctors) holding second, undeclared jobs contrary to their terms of employment; work by retired people, students and those on benefits who may not declare jobs they hold. Estimates are that these workers and their UDW (...)	The minimum wage which only applies to the non-unionised sector has been increasing in recent years. Though no data or studies confirm this, it is likely that these increases would act to increase undeclared work.	There is an incentive for individuals to avoid income tax through UDW. This is the case despite the fact that the burden of direct taxation was reduced in 2004. However, it must be noted that indirect taxation has increased, providing an incentive for the service sector in particular to use UDW.	Social security contributions are set at 6.3% of insurable earnings (payable by both employers and employees). This is likely to be an incentive for UDW. There are discussions under way to increase the contribution levels to improve the viability of the social insurance scheme. This is likely to lead to a potential increase in UDW. From this standpoint, it may be preferable to improve the viability of the social security system by increasing the retirement age.	Until recently, UDW was not considered a high priority in Cyprus and it was, for example, taken for granted that self-employed people would pay little, or no, income tax. The government has started to acknowledge that there are relatively large sources of 'additional' tax revenue in UDW. Measures implemented recently include: <ul style="list-style-type: none"> • a tax amnesty programme; • a new law (implemented in January 2006) which requires compulsory tax returns for those earning (...)

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Cyprus (cont.)	<p>(...) amounts to about 10% of GDP; illegal immigrants and under-reporting by the self-employed account for the majority of UDW. It is not known whether small firms are more inclined to UDW than larger ones.</p> <p>It is regarded that UDW occurs at relatively high levels because of unskilled labour shortages, flexibility of hiring and firing immigrant workers, and the lower costs (to employers and for employees) of UDW. Under-reporting by the self-employed avoids income tax.</p>				<p>(...) above CYP10,000 self-assessment by the self-employed, penalties for the late submission of tax returns, and submission of audited accounts by the self-employed earning above CYP40,000.</p> <p>The above measures are designed to reduce tax evasion by the self-employed, but it is doubtful whether they will have an impact because their enforcement is not assured.</p> <p>The government is also clamping down on the employment of illegal workers.</p>
Latvia	<p>There is no consensus in defining UDW, and different definitions, indicators and measures are used. The estimates are various, and range from 16-18% by the state institutions to 40% or more by private commentators. The highest prevalence of UDW is thought to be in construction and wood industries. Underreporting of income (envelope wages) is rather more prevalent.</p>	<p>Since 2002 the government has been increasing the minimum wage, hoping to reduce incentives to pay the minimum wage + cash in the envelope. However, the gap between the minimum wage and the minimum level of subsistence undermines the effectiveness of the measure.</p>	<p>The major motive for underreporting of income is likely to be tax evasion. There is an ongoing discussion about the need to simplify the tax administration for SMEs.</p>	<p>To curb the evasion of social tax, the pension system has been overhauled, linking taxpayers' contributions to benefits. Reforms of maternity leave were undertaken, with higher benefits for mothers who have paid larger social tax payments. However, commentators argue that given the unstable social insurance system, many citizens are not motivated to put future gains from making tax and social contributions before present gains from tax evasion.</p>	<p>Surveillance of enterprises is undertaken to identify workers without work contracts, resulting in financial penalties for firms. Preventive activities, such as reminders, explanation requests, interviews, seminars and public information campaigns are also undertaken. Co-operation activities between different state bodies involved in tackling UDW are underway. However, administrative barriers and contradictory regulations undermine the effectiveness of inspections. In addition, no personal fines can be levied on enterprise owners/managers in breach of rules (only corporate fines are allowed).</p> <p>The problem of enforcement is acute. Policy relying on fines is unlikely to be very effective as enforcement of such fines is weak. Fiscal decentralisation has had the effect of curbing tax evasion. Local government has a stake in improved tax collection as it receives a large proportion of personal income tax revenue. The government claims UDW is (...)</p>

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Latvia (cont.)					(...) decreasing, and points to increasing social tax payments. However, reasons for this are unclear, as the result of the baby boom, reforms in the pension system or maternity leave payments could be behind such changes.
Lithuania	UDW has started to shrink significantly since 2003/2004, as economic growth and mass emigration led to shortages of employees in many sectors. An improved situation on the labour market led to increasing employees' demands for better remuneration and work conditions. UDW has shrunk from about 8% of the total employed to about 6%. UDW is more prevalent amongst small companies and more frequent amongst lower skilled and lower paid individuals.	The minimum wage has been growing rapidly, but is still very low compared with the EU-15. Regarding non-contractual employment in registered enterprises, the level of the minimum wage is too low to encourage regularising UDW. In cases of envelope wages, employers link the legally paid part of wages to the level of the minimum wage.	The tax and social security regimes are the main drivers of UDW. The levels of wages and salaries are low, whereas the levels of tax and social security contributions are relatively high. Roughly, the average tax wedge on a salary is about 50%.	A central co-ordination unit exists to analyse the origins and co-ordinate the control and prevention of UDW within the State Labour Inspectorate. Different institutions conduct joint inspections and share relevant information. Since 2004, special prevention measures have been developed (extensive information campaigns in the media, research into UDW). Stricter control procedures of work conditions and additional sanctions have also been introduced.	
Luxembourg	There is no systematic data on UDW in Luxembourg. In 2006, the Inspectorate of Labour and Mines carried out 17 major actions, 4 specific actions against UDW and 217 medium size actions leading to 10 preventive closures of construction sites. There has been a rise in the use of undeclared temporary workers, which has been attributed to the strictness of the labour code regarding the use of temporary contracts. In addition, increasing recourse to competitive tendering has given rise to more and more employers being unclear about who exactly is working on their sites.	The lack of data on UDW makes it difficult to assess the impact of minimum wages, tax and social security regimes on this phenomenon. However, the study '2Plus' argues that UDW is increasingly the result of 'underemployment' in the regular economy, which, in order for employers to avoid paying taxes and social security contributions, drives workers into having to take on second undeclared jobs, often in the personal services sector. The project also proposes a system for the regularisation of 'occasional' work, which allows employers to benefit from tax benefits while enabling such employees to be covered for the purposes of pension and social insurance.			A separate administrative unit for the fight against UDW has been established. A law of 2006 is proposing to improve the efficiency and operation of the Inspectorate of Labour and Mines.

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Hungary	<p>There have not been any new comprehensive measures issued on the prevalence of UDW since 2004, but UDW is a serious problem for the Hungarian economy, where the labour activity rate has been low since the beginning of the transition. It is probable that a significant number of long-term inactive people actually work unofficially. These workers can be grouped in at least two distinct groups: without a labour contract and not paying any taxes, and those 'forced' entrepreneurs (with different tax margins and possible costs deductions).</p>	<p>There is some evidence, but not a formal study on the effect of the abrupt increase in the minimum wage on the prevalence of UDW. The existing evidence shows the negative impact of a large increase of the minimum wage on employment in small firms and the job finding probabilities of low-wage and low-skilled workers. The effects appear to be stronger in depressed regions, where the minimum wage bites deeper into the wage distribution.</p>	<p>High income tax countries – such as Hungary – would be expected to have a high rate of undeclared work. The tax regime has a more long-lasting effect on the prevalence of UDW, than such measures as strict control of employers (which in Hungary is also successful to some extent). In the long term, high taxes will affect negatively the activity rate in the country and increase labour costs. Those who continue to be registered employees, but declare lower wages simply to avoid taxes, have to pay higher taxes and contributions, as they pay them after the new level of the minimum wage.</p>	<p>The government issued a new piece of regulation (in September 2006), which increased the payment of social security contributions for those on the minimum wage, unless they declared that they were earning the minimum wage; in this case, however, the individual ran the chance of facing a tax control. As a result, starting in 2007, 140,000 people started to pay social security contributions, possibly caused by the control of the social security system. The increase of the social security contribution from 2% of the gross salary to 6% could have a negative impact on declared employment.</p>	<p>Stricter controls of workplaces (especially in construction, agriculture and trade, where UDW is the most prevalent) were introduced, followed by fines for those engaged in UDW. Next year the system of granting disability pensions is going to be changed, introducing stricter controls when obtaining a disability certificate. It is a serious problem, as a large part of Hungarian inactive people receive disability pensions (there are around 500,000 disability pensioners under the retirement age limit, which is 7.3% of the population aged 15-64). Regulation that actually encourages people to work legally is the stricter control of health insurance payments. Starting with next year, only those who have either paid the contribution on a regular basis, or where the state pays their insurance on the basis of their social situation, will receive free-of-charge health assistance. Regulation concerning the work of pensioners also changed. Starting in 2006, working pensioners have to contribute 8.5% of their pension to the state budget. If a person retired before the retirement age, up to the eligibility age he or she can only work if his pension is suspended for the period of employment. This change may have a positive effect on the state budget, as early retirement becomes more expensive for the individual, but it also increases the costs of declared work for all pensioners, and especially for those below the retirement age. Thus, it is likely that some pensioners will choose to work without a labour contract.</p>

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Malta	<p>There has not been much political interest specifically in UDW in Malta. Focus has been more on the 'underground economy' (illegal work and UDW). Interest has also focused on the abusers of social security, on illegal immigrants and on concerns about female employment (the latter is linked with the Lisbon Strategy). There are no official figures on the prevalence of UDW. Unofficial estimates of the 'underground economy' (UDW and illegal work) put it at 25% of GDP. It is regarded as consistently increasing over the last few years. UDW appears to occur mostly in construction, household services and hospitality.</p>	<p>It is difficult to ascertain if the minimum wage is having an impact on levels of UDW. Employers express concern about the annual increase of the minimum wage and it may therefore act as an incentive for UDW.</p>	<p>In recent years, income tax levels have decreased. In the last budget, the government revised the tax on bands and thereby removed an incentive for middle income earners to take on UDW. Corporation tax is charged at a relatively high rate (35%), although it is not clear whether this has any impact on levels of UDW. It is regarded that there is widespread abuse of the VAT system, especially by self-employed people.</p>	<p>The difference between the minimum wage and unemployment benefit is small. This does not therefore provide an incentive to take regular work. Instead, it may provide an incentive for unemployed people to remain on benefit, and supplement their income with UDW. The social security system is currently being evaluated to identify if it can be improved so as to encourage more people to fully declare work.</p>	<p>The principal components of flexicurity are being discussed in Malta; discussions take the form of exploring improvements to workforce flexibility whilst also improving the social security system. The latter is regarded as closely linked to UDW (i.e. abuse of social security benefits is seen as linked to undertaking UDW). The debate about immigration focuses on the growth in the number of illegal migrants in Malta, and on their involvement in UDW. This is seen to be distorting the labour market, especially in construction and in hospitality. The government has several initiatives which are directly or indirectly tackling UDW. These include a new law (from 2005) aimed at regulating foreign workers and controlling illegal employment. The Employment and Training Corporation conducts skills profiles of all unemployed people to refer them to training and employment. There are several measures aimed at detecting social security benefit abuse. A range of measures have been introduced to improve the taxation system. There are also active labour market policies designed to bring about a shift from UDW to regular work. This includes measures targeted at female workers (since females are regarded as making up a large part of the underground economy).</p>
The Netherlands	<p>The level of UDW is difficult to quantify. Existing figures only apply to the number of investigations that have (...)</p>	<p>The lowest pay scales are well above the minimum wage level so the wage level as such may be a reason for UDW but this is not (...)</p>	<p>Due to strict controls it has become harder to hire workers in the Netherlands without paying wage tax. Cash-in-hand (...)</p>	<p>Due to strict controls it is more difficult to hire workers without paying social security contributions. This is especially the case in sectors (...)</p>	<p>The Dutch Government is determined to achieve improvements in combating UDW (Handhavingsprogramma 2003-06).</p>

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<p>The Netherlands (cont.)</p>	<p>(...) been carried out and fraud cases detected. Therefore figures are not representative for the actual level of UDW. Sectors known for a high level of illegal employment include construction, hotels and restaurants.</p>	<p>(...) an effect of the minimum wage level.</p>	<p>(...) workers are not likely to pay tax. Hiring a moonlighter may be attractive, as they charge a lower price and because no VAT would be payable. Less than 5% of the working population would be involved in cash-in-hand working.</p>	<p>(...) where there are large numbers of temporary (seasonal) workers. Frequent controls are carried out.</p>	<p>The Court of Audit however found that the probability of someone who commits fraud being detected is very low for all types of fraud. The Ministry of Social Affairs and Employment published a new programme Handhaving-sprogramma 2007-10 which aims amongst other objectives to intensify the fight against illegal employment. By liberalising the procedure for employment permits for employees from Poland, Slovakia, Hungary, the Czech Republic, Slovenia, Estonia, Latvia and Lithuania, the government aims to decrease the number of illegal workers. At the same time controls against employers who pay less than the minimum wage per hour will be tightened. Procedures for declaring tax have been simplified reducing the chance that tax payers will 'forget' certain sources of income. This is done by supplying tax forms to tax payers with existing and known information already completed. Tax credits for everyone in paid employment help to make paid employment more gainful, especially for people at the lower end of the labour market. An attempt has been made to legalise illegal cash-in-hand work like house cleaning. The number of hours above which you need to pay social security contributions is now fairly high which means that this kind of fraud has disappeared. The labour unions play an explicit role in ensuring that employers do not hire illegal workers or pay foreign workers less than the wages negotiated in the collective labour contracts, acting as a partner of government in preventing and combating UDW.</p>

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Austria	UDW is a relevant labour market issue, despite a decrease of the proportion of the black economy in the GDP. UDW is frequent in the field of care and nursing of elderly people, where a significant number of people from the new Member States are employed. Restriction of access of workers from the NMS means that UDW is the only way to find employment in Austria. The attitudes of Austrian citizens towards UDW are lax.	The national minimum wage does not yet exist. Collective bargaining takes place at a sectoral level. The government plans to introduce a general monthly minimum wage of EUR 1,000, which is currently being negotiated. Its effects on UDW are debated at the moment.	The relatively high VAT and income tax rates and high non-wage labour costs are the main drivers behind the UDW. Some estimates show that about 50% of increase in the black economy is due to the increase in tax and social security contributions.		The measures concentrate on the stricter enforcement of the existing rules. Also, the increase of staff in the institution responsible for tackling UDW and extension of its competences are expected to lead to a stricter enforcement of the relevant acts. In 2006, the fines for illegal employment of foreign workers were doubled. Also, employers were obliged to keep up-to-date accounts where cash transactions were involved. Social partners have proposed to oblige employers to register all newly employed workers before the employee starts work. This is currently used as a loophole in case of inspections. To address UDW in the care sector, the government introduced a service voucher for household activities. Employees remunerated by the voucher become part of the social insurance system. The take-up of the voucher has been less than expected. Only workers holding a work permit are eligible. Future options to combat UDW include campaigns to raise awareness of UDW and the reduction of tax rates or non-wage labour costs.
Poland	The 'black economy' share of the GDP total in Poland is between 12% and 15% and is decreasing. The scale of UDW in 2004 decreased in comparison with previous years (1995, 7.6%; 1998, 4.7%; 2004, 4.2% of persons aged 15 and above took up UDW). UDW is most often undertaken by men (63% of the total number of undeclared employees), inhabitants of cities (52%), mostly aged 45-59, with elementary vocational education and lower education (69%).	The influence of minimum pay on UDW is weakened by the possibility of it being reduced. From 2003-05 employers had the opportunity to fix pay lower than the defined minimum but not lower than 80% of minimum pay for the first year worked and 90% in the second year of work. In December 2005 221,300 persons received pay which did not exceed the minimum wage and 34,700 persons received pay at the permitted sub-minimum level.	The high tax wedge has a negative influence on the employment of the least productive persons, whose potential wages are close to minimum pay. The tax wedge is higher in Poland than the EU average, and the difference in 1999-2004 was clearly increasing. The tax wedge also includes para tax burdens of various characters. For a number of Poles avoiding fiscal burdens is not seen as theft because they do not see the link between their actions and the necessity to impose (...)	The existence of the high tax wedge is accompanied by a number of sources of alternative income from public resources, such as retirement pension, disability pension, unemployment benefits, social assistance benefits, and from UDW, which is not conducive to increasing the attractiveness of legal work. High taxation of work encourages low wage earners in particular (i.e. usually low qualified) to escape into the 'black economy' and make use of available benefits.	UDW is perceived as a socio-economic problem, however no clear measures to limit it are apparent, particularly in relation to those aimed at increasing the attractiveness of legal work in comparison with alternative sources of income. In 2004-07 a number of solutions were introduced aimed (directly or indirectly) at combating UDW. In 2005 regulations concerning the employment of unemployed nannies, housekeepers and domestic help (...)

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Poland (cont.)	UDW mainly occurs in gardening and agricultural works, neighbourhood services, refurbishments and repairs, and installation and refurbishment services.	The influence of the level of the minimum wage and its effect on the interest in UDW exists but is quite limited.	(...) increased taxes on honest tax payers.		<p>(...) were introduced on the basis of the activation contract. In practice the opportunity was not taken up by tax payers on a visible scale for a variety of reasons, the administrative burden being one of them.</p> <p>To reduce burdens connected with social insurance in 2005 an improvement was introduced for persons who become self-employed. During the first 24 months from when the economic activity started, the basis of assessment for insurance fees is reduced to 30% of the minimum wage.</p> <p>In the area of UDW the Ministry of Labour and Social Policy develops projects of legal regulations, monitors the activity of employment agencies, and runs informative campaigns on the dangers that can be encountered while undertaking UDW. Since 2004 there have been no significant actions to change the personal income tax system and/or reduce the remaining burden on wages.</p> <p>Recently, in April 2007, the government passed an amendment of the Act on the Reduction of the Disability Pension Fee (from 13% to 10% gross pay from 1 July 2007 and from 10% to 6% from 1 January 2008).</p> <p>The amendment of the Act on personal income tax (2006) could lead to an increase in UDW as it introduces changes in the regulation of self-employment. It met with criticism from entrepreneurs and tax law specialists because it infringes the rules of freedom of economic activity and leads to the reduction of self-employment.</p> <p>The growth of illegal employment could be the effect of the above changes.</p>

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Portugal	<p>UDW had a high political profile a few years ago, but there is less interest in it now, with other concerns (e.g. recession and unemployment) being more prominent. UDW is not a central issue in the National Employment Plan for 2005-08, although measures are planned to tackle UDW and illegal work.</p> <p>Concrete data on the prevalence of UDW are not available. Estimates of the proportion of GDP accounted for by UDW are between 15% and 37%. There is no reliable evidence about relative changes in prevalence of UDW since 2004.</p>	<p>The minimum wage in Portugal has, over recent years, declined in value relative to average wages. There are however plans to increase it, up to 2011. There are concerns (especially from employers' organisations) that increases may act as an incentive for UDW, encouraged by poor enforcement.</p> <p>Overall, it can be argued that the low level of the minimum wage, and its limited coverage, mean that it probably has little impact on UDW. If the increases in its value are monitored as planned, it is likely that it will continue to have little impact on UDW.</p>	<p>The corporate income tax rate was reduced in 2005 (from 30% to 25%) and control measures were strengthened. It is not possible to identify if the reduction in the rate led to any reduction in UDW.</p> <p>The tax regime for self-employed people is likely to provide an incentive for UDW.</p> <p>Firms with low turnover benefit from a simplified tax system and a low rate of 20%. It is concluded that this has decreased UDW.</p> <p>The stricter controls on larger firms suggest that UDW is not used by them.</p>	<p>It is not possible to identify if the social security regime impacts on UDW. The rate of contributions paid by employers is seen by them as high, which may suggest it acts as an incentive for UDW. However, employers are aware that inspection and control measures have been increasing in recent years.</p> <p>Some employers do avoid social security contributions by legally paying workers for services, rather than employing them on contracts.</p>	<p>The government (from 2005) has paid close attention to problems relating to immigration. It has produced incentives for immigrants to participate in regular, declared work.</p> <p>The government published proposals in 2006 to introduce elements of flexicurity to the labour market, although these do not address UDW specifically.</p> <p>There are reforms under way of the social security regime, although there is no specific link between this and UDW.</p> <p>The focus of the reforms is on the sustainability of the regime. Several measures have been introduced which may have an impact on the prevalence of UDW. They include steps to simplify the creation of new firms, and incentives for unemployed people to participate in regular work rather than UDW.</p> <p>Other measures have aimed at strengthening the inspection and control of the tax and social security regimes (e.g. including steps to combat under-declaration of income).</p>
Romania	<p>UDW has always been high on the political agenda. However, economic growth in recent years has brought UDW (as defined by the EC) in particular to the fore, and prompted measures to tackle it.</p> <p>UDW features prominently in Romania's National Reform Programme, although there are no official figures to quantify its prevalence or to assess the impact of measures intended to reduce it.</p> <p>Current estimates of the prevalence of UDW range from 16% to 21% share of GDP. The conclusion, from analysis of available data, is that the prevalence of UDW has (...)</p>	<p>The minimum wage in Romania has been regarded as an important tool to tackle UDW. Social partners agreed a minimum wage which may be above the statutory (government assigned) level. This is regarded as helpful in reducing incentives for UDW.</p> <p>It is not argued that the minimum wage increases the incentives for UDW.</p>	<p>The government introduced a flat rate (of 16%) income tax regime in 2005. This has been one factor (among many) likely to have contributed to the growth of the economy. However, no proper evaluations or assessments have been carried out of the actual impact of the flat rate income tax regime on the prevalence of UDW and therefore no final conclusions about impact can be drawn.</p> <p>Given the complexities of factors that lead to UDW, such a measure does not constitute a panacea in combating UDW.</p>	<p>Contribution levels have been steadily decreasing since 2003, but (as noted) in the absence of proper evaluation and assessments, the impact of the social security regime on the prevalence of UDW is inconclusive.</p> <p>One argument is that optimal thresholds have now been reached and further reduction in contribution rates may backfire.</p>	<p>The Lisbon Strategy in 2005 coincided with the government's introduction of a flat rate income tax. This, and steady reductions in social security contribution levels, are presented in the National Reform Programme as key measures capable of tackling UDW. However, no evaluation of the impact of these measures has been undertaken.</p> <p>The minimum wage is also seen as a key tool in tackling UDW. A recent measure by the social partners is to introduce a higher minimum wage for workers with high educational attainment. This is expected to tackle under-declaration of (...)</p>

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<p>Romania (cont.)</p>	<p>(...) remained constant, although evidence might be a little contradictory.</p>				<p>(...) incomes for better educated employees, especially prevalent amongst SMEs (educated employees were officially paid at the minimum wage, with an additional but undeclared wage). Information campaigns have also been used to tackle UDW. The National Tax Collection Office runs a campaign to warn against UDW. The British Embassy ran a campaign to highlight the dangers of illegal migration or work in the UK. Flexicurity is new to the agenda in Romania.</p>
<p>Slovenia</p>	<p>There is no official measure of UDW. Estimates vary widely, from 7-24%. UDW is mostly widespread in the construction, catering and trade sectors.</p>		<p>The gradual abolition of the payroll tax is under way to increase the attractiveness of work. Personal income tax rates are diminished across the board and progression is reduced by also reducing the number of tax brackets.</p>	<p>A national social protection programme was adopted in 2006 to increase the attractiveness of work and motivate unemployed people to actively look for work and accept occasional and temporary employment.</p>	<p>UDW is not a major political priority. A law to define and tackle UDW was adopted in 2000 and amended in 2006 to regulate many forms of non-standard employment and encourage the declaration of economic activity. A commission was set up in 1997 to co-ordinate activities of many agencies involved in tackling UDW. The competences of inspectorates have been enhanced to enable them to issue administrative measures and fines. Joint inspections between several agencies are undertaken. Action is needed to create more reliable estimates of UDW, enhance the efficiency of the judicial system in collecting fines, undertake a public awareness raising campaign, improve the capacity of inspectorates and introduce sanctions for people caught undertaking UDW.</p>

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Slovakia	A law was adopted in 2005 to define and regulate UDW. At the same time, crucial labour market reforms, the introduction of a flat income tax, and simplification of the business environment boosted the creation of formal jobs and increased incentives to declare activity. A massive inspection campaign and sizeable media attention further raised awareness of UDW. Since, 2004, UDW has been moderately decreasing (to around 7%).	Administrative increases of the minimum wage beyond labour productivity growth result in increased labour costs. This may threaten jobs particularly in small, firms and low-paid sectors, and encourage the emergence of UDW.	Since 2004, all corporate and individual income is taxed at a flat 19% rate. Most of the tax exceptions have been abolished, and income taxation has decreased for almost every taxpayer. This had a positive effect on people's decision to work formally. The opportunity for tax fraud and tax evasion has decreased. Incentives to move income to a lower tax base have been weakened.	Motivation to employ at low/minimum wage is still present due to high social security costs. High payroll taxes are among the main impediments to regularising UDW. Social insurance contributions are amongst the highest in the OECD countries. The system is complicated. Social contributions are levied on the income from employment, as opposed to taxes, which are imposed on all types of income. This opens ways to minimise or avoid social security payments. Due to high marginal taxation, disincentives to work exist mainly for groups at the bottom of the wage scale.	UDW is not a major political priority, due to a widespread tolerance of informal activities in society. However, it is receiving increased attention from the policy makers. Preventive measures consist of the creation of a favourable legal and administrative environment, strengthening of incentives and removing disincentives to declare work on both supply and demand sides. Administrative rules on business start-ups were simplified, certain tax incentives adopted and the tax wedge decreased. Enforcement activities consist of the adoption of a special law on UDW, strengthening surveillance and the application of appropriate sanctions. Services have also been actively provided to support firms/workers in transition to declared work. Action is needed to simplify and harmonise the tax, social insurance and social benefit regimes to decrease the tax burden and remove existing disincentives to work mainly for low-paid workers.
Finland	Estimates of the grey economy's share of Finnish GDP vary from slightly below 5% to almost 18% depending on the method of calculating. In addition to foregone tax revenues (EUR 2 billion per year approx) the grey economy causes significant indirect losses to enterprises as a consequence of the weakening of their competitiveness. With the opening of borders and increase in immigration, there have been greater opportunities for domestic and foreign organised crime to expand into business and other social circles. Key problem sectors (...)	<i>No statutory minimum wage in Finland</i>	The time spent working in Finland ranks among the lowest in the OECD countries. Perhaps the reason for the low amount of working hours is that there is a lot of unemployment and a lack of incentives to work since taxation is high, social security is generous and public services are free. Finnish consumers belong to a group of Nordic welfare states with a high income tax burden but they also belong to the group of countries with lower purchasing power.	Social security in Finland is relatively generous and this acts as a disincentive to work. Work incentives are a problem especially with regard to low income jobs. Work incentive problems have increased given the increased prevalence of atypical job relationships. When the income level of part-time and fixed-term jobs is about 20% below that of full-time jobs, the effects of the labour incentive measures for eliminating income traps have been smaller in reality.	A key way of combating the grey economy and financial crimes in Finland is cooperation between authorities (VIRKE project). The enhancing of cooperation between tax authorities, police and customs has gained importance in accounts and investigations. The government has implemented four programmes combating the grey economy and financial crime. A working group called ULTEVA – 2 was formed comprising central government and labour market organisations. The objective was to monitor the adherence to collective (...)

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Finland (cont.)	(...) are construction and restaurants. In addition, transport, shipyards, cleaning as well as eastern trade are also problem sectors.				<p>(...) labour agreements particularly with respect to foreign temporary workers. Several laws combating the grey economy have been drafted including:</p> <ul style="list-style-type: none"> • construction site employees are required to have an obligatory personal ID • the appointment of representatives to supervise the benefits of workers coming from abroad in businesses using foreign labour • the domestic labour responsibility for the use of its foreign labour and adherence to labour agreement laws. <p>A goal of tax policy is to combat the grey economy and a range of specific measures are under consideration. During 1996-2006 the smallest reservation wages were lowered by taxation and expense policy measures by about 30%. Preconditions for employed older low-income workers have been improved by the introduction last year of a temporary low-wage support measure. The amount of tax deductibility of housework has also been increased and also expanded to cover caretaking services in addition to renovation work.</p>
Sweden	The Swedish Tax Agency published a study of UDW in December 2006 and found that the extent of UDW in Sweden is 5% of GDP. UDW has increased in the past decade – in 1997, 11% of the 18-74 age groups undertook some form of UDW; in 2006 the figure was 13%. The majority of workers involved in UDW are male, young (including students) and are skilled craft workers or small business (...)	<i>No minimum wage in Sweden.</i>	Tax avoidance appears to be the most cited reason for undertaking UDW (as reported in the 2006 Tax Agency study). This is the motive cited mostly by men, the self-employed and the well educated. The study also suggests that high levels of taxation prompt workers to undertake UDW. Doing so is generally regarded as a 'minor offence', with a perception that there is little chance of (...)	A Tax Agency report in 2007 recommends a lower rate of social security contributions (20%, rather than 32%) for employers who are private individuals. This reflects the generally held view in Sweden that relatively high social security contributions have been acting as an incentive for UDW.	Tackling UDW is a high priority for the Swedish Government and several initiatives have been implemented. Efforts have been made to raise the social awareness of UDW through joint information campaigns by the tax authorities and the Economic Crime Authority; some were undertaken with the social partners (e.g. in the construction sector). The Swedish Tax Agency was given additional (...)

Country	Prevalence of undeclared work (UDW)	Role of minimum wages	Role of taxation regime	Role of social security regime	Strategies and measures towards combating undeclared work
Sweden (cont.)	(...) owners (including self-employed). UDW is highest in agriculture and fishing, catering, taxis, car repairs, and personal and household services. UDW is also more prevalent amongst those on low incomes and amongst the employed (i.e. unemployed people are less involved in UDW).		(...) being caught. It is generally accepted in Sweden that high taxation levels have restricted the growth of the personal services sector – affecting both the demand for such services, as well as their provision. This is likely to be having an impact on labour market gender equality. A 2007 Tax Agency report recommends several changes to tax legislation, including: tax allowances if the employer is a private person; income from work between parents and children to be tax free; and income from work should not affect student loans. The report also recommended increased control procedures, especially in the construction sector.		(...) resources (staff) in 2006 and 2007 to introduce increased tax controls and audits. In the 'high risk' sectors of restaurants and hairdressers, employers have been required from 1 January 2007 to keep staff registers. Construction sector social partners are in agreement with introducing this requirement. A tax deduction for household services is being introduced from 1 July 2007. This is expected to shift the balance of work in household services from UDW to regular, declared work. The Government has recently stated that it will introduce a measure to tackle UDW in the taxi industry. It will also decrease social security contributions in some service sectors (those in which UDW is most prevalent).
United Kingdom	Nothing new to quantify assessments of UDW. Evidence from 2004 Review showed the incidence of UDW with be low in the UK compared with most Member States.	To date it is not clear that the National Minimum Wage (NMW) has had any significant impact (either positive or negative) on informal work. Should the NMW begin to have a detrimental effect on the availability of jobs in low paid sectors/ occupations, it is more likely that individuals will turn to paid informal work.	The low tax environment should if anything reduce the incentive not to declare work. Tax credits also provide support for those on low incomes. The tax credits system however creates a disincentive for a second earner in a family to work formally. Many people are not aware they are eligible for tax credits. The increase in the overall tax burden over the past decade is problematic for both businesses and individuals. There are two important issues for businesses – the complexity of the tax regime and the large scale of indirect tax losses.	The design of social security payments creates adverse incentives for individuals to stay on benefits rather than find employment. There is a limit on the amount of work that can be undertaken while on benefits and the earnings disregard is also very strict. This forces people either to work fewer hours than they could or to take up informal work as well. The fact that formal employment especially for those on a low income is becoming increasingly temporary and unreliable is not always an incentive to leave benefit.	ALMPs contained in various New Deal initiatives provide substantial support for the unemployed to enter formal work and actions have recently attempted to disrupt informal work by conducting work force interviews at unpredictable times and at short notice. Immigration has been linked to increased rates of informal work. Immigrant workers are more likely to work in sectors in which informal work is more prevalent such as agriculture and construction. The Department for Work and Pensions and HM Revenue and Customs take predominantly punitive measures to reduce informal work when linked to benefit fraud and tax evasion, through prosecution. New Deal for Communities (...)

Country	Prevalence of undeclared work (UDW)	Role of minimum wages	Role of taxation regime	Role of social security regime	Strategies and measures towards combating undeclared work
<p>United Kingdom (cont.)</p>					<p>(...) works closely with communities to tackle worklessness and increase paid employment (but does not directly target the informal economy). DWP has run several high profile campaigns aiming to deter fraudulent benefit claims. There are some regional and sub-regional pilot projects aiming to help people to legitimise their work activity. Working Tax Credit is an important in-work benefit that should encourage people to take up formal employment.</p>

European Commission

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