

Brussels, 24 October 2007

## EU steps up the fight against undeclared work

### What is undeclared work?

Undeclared work is defined as "paid activities that are lawful as regards their nature but not declared to public authorities, taking into account differences in the regulatory system of Member States". This definition has been used systematically by the Commission since its 1998 Communication on undeclared work.

The definition notably excludes criminal activities which are defined in national law. Crime and tax fraud as such are outside the scope of employment policy. This does not mean that there are direct links between fraud and employment but there is no complete match (e.g. money laundering can take the form of declared work).

### Which policies can help curb undeclared work?

There are various examples of successful policy approaches to curbing undeclared work in the different EU Member States.

- The tax burden tends to provide financial incentives for undeclared work, especially in the case of workers with lower pay/skills. This is often combined with receiving social benefits while working undeclared. EU Member States have been reducing the tax wedge on low-paid labour over the recent years by introducing a tax free income base or minimum wages, but the pace of the reduction has been on average rather slow (1.2% on average compared to a starting level of around 40%).
- Undeclared work may occur in conjunction with the evasion of indirect taxes. Hence, some Member States have taken up the possibility offered by Directive 1999/85/EC to reduce VAT on specified labour intensive services. In France, this measure has been applied to building renovation and maintenance and to personal services, leading to significant job creation (more than 40.000 jobs).
- Administrative simplification has been undertaken by a number of member states to remove another strong incentive for undeclared work. Service vouchers have been introduced in Belgium, Austria and Spain, as a simplified system to hire workers for regular domestic services. This measure has often led to significant job creation (e.g. 40,000 extra jobs in Belgium), but also to severe budgetary efforts due to the amount of public subsidies involved.
- Simplified systems for the registration of workers were introduced in several Member States. In France such a system has been set up in the 1990s in order to encourage regularisation of agricultural and seasonal workers. 900,000 workers are currently covered.

- Efforts to improve monitoring and control capacity were undertaken in many Member States. This has often taken place through more effective cooperation at national level between tax/social security organisms and labour inspectorates. To this end, inter-ministerial coordination structures have been set up in France, Belgium, Ireland and Italy, while interfaces between the relevant inspections' databases have been established in Portugal, in order to improve probabilities of detection of undeclared work. These have led to more effective inspections and controls with positive but largely unmeasured employment effects.

### **What is the extent of undeclared work in the different Member States?**

The best available estimates (which were collected through a study carried out for the Commission in 2004 ) show that the overall extent and characteristics of undeclared work differ widely in the Member States, with highs of 20% of GDP or more in some southern and eastern European countries. Undeclared work is still on the rise in several Member States (disregarding the effects of recent regularisation campaigns of illegally staying third-country nationals in Italy, Spain and Portugal), whilst in a number of new Member States strong job creation in recent years and the emergence of labour market shortages, has led to a decline of the phenomenon.

Country	Estimated size	Year	Latest developments
Austria	1.5% of GDP	1995	Slightly decreasing trend since 2005
Belgium	3-4% of GDP	1995, confirmed in investigations in 1997 and 1999	Likely reduction due to success of service vouchers (ca. 40000 new jobs)
Bulgaria	35% of GDP	2004	Signs of expansion
Cyprus	4.2% of GDP	2003	Likely on the increase (clandestine immigrants)
Czech Republic	0.6% of total employment	2004	No increase anymore due to regular job creation.
Denmark	4.3% of GDP (3% black activities + 1.3% ordinary tax evasion)	2005	Declining
Estonia	6.1% of GDP	2001	Clear decrease of volume of envelope wages
Finland	4.2% of GDP	1992	-
France	4-6,5 % of GDP	1998	Increase 2002-'05 on the basis of infractions (DILTI)
Germany	4.5% of GDP (3.1% black activities + 1.4% ordinary tax evasion)	2004	Decline, but risk of increase in 2007 due to VAT increase and labour tax reform
Greece	Over 20% of GDP	1998	Likely increase (push from immigration)
Hungary	18% of GDP	1998	Signs of decline (less self employed and increasing social security incomes)
Ireland	Not available		
Italy	16-17% of GDP	1998/2001	Stagnation if abstraction made of immigrant amnesty of 2002
Latvia	18% of GDP	2000	Slight decrease due to regular job creation
Lithuania	18.9% of GDP	2002	Decrease due to regular job creation and labour shortage
Luxembourg	Not available		/
The Netherlands	2% of GDP	1995	No clear trend, but noticeable shift towards fraud by employment agencies
Malta	5.78% of GDP	2004	/
Poland	14% of GDP	2003	Declining trend due to regular job creation
Portugal	5% of GDP	1996	Trend unclear but likely push from immigration.
Romania	16-21% of GDP	2006	
Slovakia	13-15% of GDP	2000	Moderate decrease due to regular job creation
Slovenia	17% of GDP	2003	Slight decline notably with small enterprises
Spain	15-20% of GDP	1985	Increase 2002-2006 if abstraction made of regularisation of 500000 immigrants in 2005
Sweden	5% of GDP	2004	Slight trend of increase
United Kingdom	2% of GDP	2000	No change observed

What are the main results of the new Eurobarometer survey?

It is the first time that a harmonized survey on undeclared work is carried out across the whole EU-27 on the topic of undeclared work. However, given the sensitiveness of the subject investigated and the pilot nature of the survey, its quantitative outcomes should be taken with caution and are likely to provide only a lower bound of the actual values. This being said a number of interesting findings, concerning especially the qualitative features of undeclared work, can be highlighted:

- The main reason to perform undeclared work is the mutual benefit for both consumer and supplier (i.e. avoiding taxes and administrative burden).
- Undeclared work is more prevalent among students, unemployed and self-employed and it is particularly concentrated in household and personal services, construction and (on the demand side) retail.
- There is a large variation in the incidence of undeclared work across Member States and its intensity, in terms of hours of work, is larger in Southern and Eastern Europe.
- Envelope wages (i.e. wages paid cash-in-hand without registration) are far more widespread in Central and Eastern Europe and concern especially the construction sector. They constitute a significant share of the total pay (around two-fifths) for the workers involved.
- The detection risk matters: people who consider the risk to be small are more likely to be involved in undeclared work.
- People involved in undeclared work tend to be more tolerant of norm-resistant behaviours. Also, undeclared work done by a private person for a household is more accepted than other forms of norm-resistant behaviours such as receiving welfare payment without entitlement or using public transport without ticket.
- Somewhat surprisingly, people with a higher level of education and in professional groups with above-average income are more likely to purchase undeclared goods/services.
- In more than half of cases undeclared work seems to substitute for regular employment: a majority (53%) of purchasers of undeclared goods/services say they would have acquired them in the regular market in the absence of the undeclared work option, showing the scope for regular job creation.

What is the relationship between free movement of workers and undeclared work?

The non-application of the right to free movement of workers increases the scope for undeclared work. For example, transitional arrangements limiting the free movement of workers constitute a driver for undeclared work because of the impossibility for certain workers from new Member States to regularise themselves in the old ones.

The legal framework on free movement of workers is a safeguard against undeclared work. Free movement of workers is a basic right laid down in the Treaty, which works effectively for several decades. The basic regulations date from 1971 as far as social security is concerned (including for the self employed), and from 1996 as far as the rights of posted workers are concerned. Once cross-border workers (whether in dependent employment or self employment), are correctly registered to social security and labour institutions, they can be controlled in the same way as nationals. It is thus crucial that cross-border workers and their employers have a user-friendly administrative framework to comply with these regulations. This is why the changes in the regulatory framework would notably aim to improve administrative transparency and simplification in the interest of the user, on the basis of better cooperation between institutions across borders.

### **What could be the role of the "platform" of labour inspectorates?**

The Green Paper on Labour Law stressed the need for more cooperation between Member States in particular in the field of posted workers. The Commission plans to adopt a recommendation aimed at reinforcing such cooperation through the use of the Internal Market Information System, as well as a decision setting up a high level committee. The Committee should support and assist the Member States in identifying and exchanging good practices as regards control and enforcement of relevant legislation.

### **How can social partners participate?**

In a number of Member States, social partners have signed special agreements with the government in order to curb the incidence of undeclared work in specific sectors, such as construction. An illustrative example is the tripartite alliance against undeclared work in the construction sector in Germany. This sets a number of targets such as raising public awareness of the negative consequences of undeclared work, enforcing rules concerning tax and social security contributions payment and minimum wages and ensuring fair competition. These agreements have triggered a number of innovative measures in the construction sector, such as formalised notification for reporting suspected situations of undeclared work, a job identification chip-card to be carried by all construction workers, the exclusion from public procurement in case of infraction and the improvement of local information flows between sectoral organizations and control authorities.

### **What is the link with the flexicurity agenda ?**

The problem of a segmented labour market, where large groups of workers are trapped in unprotected activities, is also increasingly recognised. UDW represents an extreme case of labour market segmentation and runs against all the key principles of flexicurity. The Communication on flexicurity proposes eight principles and four typical pathways, which can be considered as a point of departure for Member States in designing their own flexicurity strategies, according to their own particular situations and traditions. Such strategies could help transform informal work into formal employment by making work more attractive from the point of view of both workers and employers. Concretely, flexicurity would imply more rights for workers in the form of access to training, active labour market policies and unemployment benefits in case of unemployment, while at the same time improving the conditions for regular job creation by employers by reducing the administrative burden and ensuring the availability of a more skilled workforce.

### **What can PROGRESS offer?**

The PROGRESS programme , with an annual envelope of ca. 20 million € in the employment section, supports inter alia studies, the development of statistical tools and the exchange of good practices through networking and dissemination activities. This programme is suited for filling current gaps in measurement and the pooling of expertise among national authorities, involving stakeholders such as notably the social partners. These will feature among the priorities of the programme in 2008.