

Undeclared Work in Western Europe

Undeclared work, also known as informal work or shadow economy, represents a significant challenge within the labour markets of Europe. This form of employment is defined as any legal paid activity that is not declared to the state authorities (European Commission, 2007).

Undeclared work leads to far-reaching social and economic consequences (Schneider ,2011). Since this type of employment is illegal and not reported to the state authorities, employees cannot protest violating fundamental rights such as withholding wages, deviation from acceptable working hours and wages below the minimum level. Furthermore, the workers are deprived of social benefits such as sick leave, vacation, and pension provisions. This situation poses a dual threat to the state and society. For example, if an injury or illness prevents employees from working, employees are exposed to financial risk without protection. Additionally, they may become a significant financial burden during their retirement years due to the inability to save money for the future.

The unreported economy creates imbalances in the market by establishing prices lower than the actual market value, encouraging consumers to purchase products and services in the unofficial market. This results in decreased demand in the declared conventional market. Consequently, businesses engage in undeclared trade to maintain competitiveness and survive in the market. This practice creates a moral hazard, as it may encourage others to follow suit. At the macro level, the informal employment reduces countries' tax revenues by evading taxes. Consequently, this leads to less money in state budgets, which affects the quality and the extent of public services.

In this policy proposal, we address the available strategies for European Union countries to tackle the undeclared economy and to effectively reduce its prevalence. The objectives of this policy are threefold: to safeguard state revenues, ensure fair competition, and protect workers from exploitation.

The unofficial economy in the European Union is estimated to be 17.5% of GDP, with higher rates in Eastern European countries and lower rates in Western European countries (Schneider, 2022). As decision-makers in Western Europe, we must distinguish between the different reasons that lead people to this work: escaping poverty (common in Eastern Europe), moonlighting (common in Western Europe), and social solidarity (common in Western Europe) (Pfau-Effinger, 2009). Therefore, the policy we lead will mainly focus on the last two. *Moonlighting* involves individuals holding a second job, yet due to high tax rates and additional burdens like social security contributions, some choose to underreport or not declare their income from this job. To encourage full income declaration, tax systems should adopt policies that facilitate the tax payment for workers with multiple jobs.

Social solidarity is another common reason for undeclared work in Western Europe. However, decision-makers face a challenge in dealing with it as it involves questions of values and ethics. When a person provides services or products in exchange for help to others, it can be seen as breaking the law.

Therefore, addressing a policy position might be difficult due to the ethical and social aspects involved. As a result, some countries, such as Germany, do not intend to introduce policies addressing mutual aid and undeclared work due to their social orientation.

If countries intend to adopt a policy promoting solidarity, we recommend employing information systems and streamlining the taxation process. It is essential to clearly demonstrate the benefits of declaring income and transactions such as saving for retirement. Simplifying the tax system will facilitate a quicker and more efficient process for both providers and recipients of goods and services. In addition, increasing awareness about the illegality of working in the underground economy is essential, as some may not be aware that their actions are unlawful. However, imposing sanctions on those involved could provoke public opposition and diminish trust in the legal and tax systems, making it an unwise political move for governments.

The European Commission (2007) advises adapting a broad definition of undeclared work to align with each country's specific laws and conditions. However, many European countries, including the Netherlands, UK, and Spain, have yet to implement this guideline. We assert that establishing clear and specific laws is essential for addressing undeclared work, as clarity in legislation raises public awareness and facilitates compliance. For example, France legally defines undeclared work in seven clauses, Austria categorizes certain recruitment activities as undeclared employment, and Denmark treats illegal immigrants engaged in undeclared work as committing dual offenses. Without clear definitions, both employers and employees may unknowingly participate in illegal activities, such as cash payments for services unreported to fiscal authorities, perpetuating the issue.

Countries should devise strategies that make the risks and consequences of participating in the shadow economy outweigh its benefits. Germany, for example, has successfully implemented a sanctions policy where businesses caught engaging in undeclared work face closure and bans from public contracts. In the UK, the *Naming and Shaming program* since 2010 publicly exposes those who violate employee rights, effectively deterring such practices. However, increasing penalties is insufficient without robust enforcement, including enhanced surveillance, dedicated enforcement units, and proactive inspections to verify employee credentials and work conditions.

Additionally, installing surveillance cameras in high-risk businesses can aid in compliance.

Simultaneously, countries should provide incentives like tax benefits and simplified tax declaration processes to encourage lawful employment, particularly for self-employed individuals and part-time workers. In Western Europe, we recommend establishing social rights funds for freelancers to balance

the high taxes they pay, promoting declaration and fostering trust between these workers and the tax system. However, excessive taxation can deter self-reporting, necessitating social adjustments to the current system to encourage compliance.

Discourse programs in Belgium and the UK have shown effectiveness in reducing undeclared work by enabling safe reporting of such activities. These reports lead to investigations and penalties for offenders, subsequently increasing government revenue through recovered taxes and fines, which surpass the operational costs of the programs. These disclosure initiatives extend beyond employees to include those aware of any informal employment, enhancing the enforcement system's reach. To further address undeclared work, particularly in the context of illegal immigration, we recommend integrating strategies that increase employer accountability. However, challenges like forged documents in France show that mere document retention by employers is inadequate. We advise implementing official biometric verification systems to authenticate worker documents more reliably.

Additionally, we propose expanding the reporting mechanisms to include illegal migrant workers, potentially offering them a pathway to legal status upon reporting. This approach not only aims to decrease undeclared employment but also to incentivize legal employment through monitored frameworks. Considering the significant illegal immigrant population in some of the EU countries, these policy proposals require careful consideration and discussion to address possible internal social and cultural impacts in these countries.

On April 11, 2024, the European Union Parliament approved a new immigration and asylum seekers policy, scheduled to be implemented in 2026 (Frontex, 2024; European Parliament, 2024). This policy aims indirectly to mitigate the issue of illegal immigrants participating in the shadow economy by establishing clearer legal pathways and stricter enforcement measures.

A final point to consider is the importance of sharing and inclusion in policy decisions regarding informal work. Encouraging feedback and participation from the public can lead to creative and practical solutions. This approach improves policy outcomes and helps build public trust in the tax and state systems by showing that everyone's input is valued.

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