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## **ІНСТИТУЦІЙНІ АСПЕКТИ НЕФОРМАЛЬНОЇ ЗАЙНЯТОСТІ У БАЛАНСІ ДОХОДІВ НАСЕЛЕННЯ**

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## **INSTITUTIONAL ASPECTS OF INFORMAL EMPLOYMENT IN THE BALANCE OF PERSONAL INCOME**

**Abstract.** The article is devoted to the research of institutional aspects of informal employment in the balance of the earned and entrepreneurial income. The essence of informal employment as social and economic phenomenon is considered. Given coverage to main tendencies in the informal sector of the Ukrainian economy. The influence of informal employment on formation and distribution of personal income is revealed. Parameters and structure of informal employment in Ukraine are analysed. The level of informal employment by socio-economic characteristics is examined. The features of informal employment in Ukraine and its influence on the level and differentiation of personal incomes are revealed. The role and significance of the institutional component in the formation of the informal sector of the economy is examined. Main directions and measures aimed at reducing the level of informal employment of population are proposed.

**Keywords:** informal economy, informal employment, personal income, unofficial income, employment legalization.

**Problem statement.** The problem of informal economy and informal employment is rather complicated and ambiguous to study. Special relevance of the issue of informal employment is due to its impact on the formation and distribution of incomes. On the one hand, the participation in informal employment allows to get additional profit, reduce real unemployment rate and increase competitive advantage. On the other hand, informal employment results in the loss of mandatory budget revenues, promotes the spread of corruption and illegal manipulation of macroeconomic performance.

**Analysis of recent studies and publications.** In recent years, a lot of attention has been paid to the research of the problem of informal employment in Ukraine. This is caused both by the growth of its scale in the condition of economic recession and its significant impact on the socio-economic situation in the country. Such domestic scientists as V. Bazylevych, N. Vargs, Z. Varnaliq, Yu. Kulikov, E. Libanova, I. Mazur, V. Mandibura, O. Pyshchulina, Yu. Kharazishvili, A. Khodzhayan and others, Among foreign scientists, we can highlight L.A. Munro, P. Doeringer, J. Losby, G. S. Fields and others.

**The objective of the article** is to study the trends in informal employment in the conditions of economic recession in the context of generation and distribution of incomes.

**Presentation of basic material.** The borders between the notions of the shadow economy and its informal sector are rather conventional. The most typical informal activities are: street trading; services to the population in construction, repair, sewing; private services - cleaning, cooking; tutoring. Consequently, the informal sector includes unregistered economic activities carried out by citizens, independently or within the framework of small production units at their own expense or using working facilities of the enterprises in formal sector.

In Ukraine, informal employment is a significant source of income and consumption and, by its own scale, has a significant impact on personal income level. The volume of informal economy and informal income are not recorded by official statistics.

The scale of informal employment in Ukraine is much higher than in the majority of developed countries, and can only be compared with Italy, where up to 30% of GDP is produced by the "shadow economy". General level of the population engagement in informal employment corresponds to the Latin American countries where such employment accounts to 25-45%.

Working paper No. 6 developed by the Group for technical support of decent work and the Bureau of International Labour Organization for Eastern Europe and Central Asia, the essence of the informal economy is as follows: «Most employees and companies in informal economy are legally producing goods and services, although not always in compliance with administrative requirements, for example, the procedure for registration or immigration. It is necessary to differentiate such activities from criminal and illegal activities, such as production and smuggling of illicit narcotic drugs, since the latter are subject to criminal law and not subject to regulation or protection under labour or commercial law»<sup>1</sup>.

In Ukraine, for the purpose to determine employment and unemployment rate, the State Statistics Service uses the materials of examination of economic activity of the population.

In modern conditions, illegal employment is due to the weakness of socio-economic institutions. The growth of shadow employment leads to a low specific gravity of wages in the cost; high level of taxation of the formal sector of economy, including contributions to state social funds; raise of poverty level across working population; decrease in production volumes in main economic activities; low level of law-obedience.

On the other hand, the existence of employment in officially unregistered sector of economy is objectively conditioned by the possibility to get higher profits than in legal sector, and for a certain category of people, it is a main source of income. The employment in informal sector contributes to the development of entrepreneurial abilities, deepened realization of the ability to work in the conditions of economic

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<sup>1</sup> Кулаев, О., Лапер, Ф. (2014) *Содействие переходу к формальной экономике на примере некоторых стран-участниц СНГ*. Москва: МОП.

recession and crisis. All this results in relatively high efficiency of the mechanism of employment formation in the conditions of shadow economy, although it requires the increased labour intensity from the employees and a lack of state guarantees in case of illness, accident, age etc. Therefore, the employment in the informal sphere allows to save labour potential, contribute to solving income problems and even fundamental survival of some segments of population<sup>1</sup>.

Certainly, the income from informal activities helps to maintain a standard of living for poor segments of population. But the wealthy segments get more from such activity. According to expert data, 20% of wealthy people have over 70% of informal incomes<sup>2</sup>. Therefore, informal revenues not only make impact on the dynamics of personal incomes, but also serve as a source of uneven distribution of income in different segments of population, which greatly amplify the inequality in society and results in increasing social contradictions.

According to the Report of Global Competitiveness Index 2015/2016, the efficiency of state and social institutions (along with the macroeconomic environment) remains one of the most competitive «failures» of the Ukrainian economy (130 th among 140 countries)<sup>3</sup>. Extremely low ranking in this subindex evidences that administrative and legal conditions, in which business entities operate, are still unfavourable owing to the consistently high level of corruption, lack of efficient judicial system and proper protection of property rights. Such factors negatively affect not only the business climate in the country, but also the society's loyalty to the state as a whole.

According to the results of random population (households) survey in economic activity issues in 2016, the number of informally employed population decreased by 342.1 thousand people in comparison with the previous year and amounted to 4.0

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<sup>1</sup> Харазішвілі, Ю.М. Тіньова зайнятість та тіньова оплата праці в Україні: оцінки та прогнози (2011). *Стратегія розвитку України. Економіка, соціологія, право*, 4(1), 171-182.

<sup>2</sup> Пишуліна, О. М. Диференціація населення за рівнем доходу та ефективність інституційної організації механізмів його перерозподілу в Україні (2007). *Стратегічні пріоритети*, 2(3), 93-102.

<sup>3</sup> Тенденції тіньової економіки в Україні (2016). *Офіційний сайт Міністерства економічного розвитку і торгівлі України*. <[www.me.gov.ua/Documents/Download?id=404ea78d...](http://www.me.gov.ua/Documents/Download?id=404ea78d...)>

million persons or 24.3% of total number of employed population (in 2015, such share was 26.2%).

Among women, the share of the employed women in the self-employed sector is bigger than that of men 77.5% vs. 72.1%, and in rural areas it is much bigger than in urban settlements - respectively 92.2% and 44.8% (Table 1)<sup>1</sup>.

Table 1.

Employed population by gender, place of residence, employment forms and status  
in 2015-2016

	Employed population			Including informal employment				
	Total, K persons	Including		K persons	Including			
		employed	Self- employed		employed		Self-employed	
				K persons	in %	K persons	in %	
<b>2015</b>								
<b>Total</b>	<b>16443,2</b>	<b>13823,4</b>	<b>2619,8</b>	<b>4303,3</b>	<b>2385,2</b>	<b>17,3</b>	<b>1918,1</b>	<b>73,2</b>
Women	7872,4	6781,9	1090,5	1772,2	935,0	13,8	837,2	76,8
Men	8570,8	7041,5	1529,3	2531,1	1450,2	20,6	1080,9	70,7
Urban settlements	11309,0	10311,3	997,7	2118,3	1697,8	16,5	420,5	42,1
Rural area	5134,2	3512,1	1622,1	2185,0	687,4	19,6	1497,6	92,3
<b>2016</b>								
<b>Total</b>	<b>16276,9</b>	<b>13731,7</b>	<b>2545,2</b>	<b>3961,2</b>	<b>2069,3</b>	<b>15,1</b>	<b>1891,9</b>	<b>74,3</b>
Women	7827,4	6775,2	1052,2	1669,0	853,6	12,6	815,4	77,5
Men	8449,5	6956,5	1493,0	2292,2	1215,7	17,5	1076,5	72,1
Urban settlements	11178,5	10219,7	958,8	1891,9	1462,8	14,3	429,1	44,8
Rural area	5098,4	3512,0	1586,4	2069,3	606,5	17,3	1462,8	92,2

Among rural dwellers, each second person was employed informally. While among the dwellers of urban settlements, such employment was not so spread due to wider job. The reasons of particular incidence of informal relations in the countryside is the reduction of the number of persons engaged in agriculture because of the change of legal forms of enterprises in rural areas. The availability of powerful, modern working facilities in crop and livestock farming promotes additional release of employees, so the area of their employment became illegal work in various fields, work in backyards and

<sup>1</sup> Ринок праці у 2016 році (2017). Офіційний сайт Державної служби статистики України.  
<<http://ukrstat.gov.ua/>>

on farms that is illegal or informal. Men, as compared to women, were more inclined to work informally (57.5%).

In recent years, the situation with the ratio of employees in the informal sector of the economy of urban and rural dwellers has changed. Previously, in the cities, informal employment was not significantly due to employment opportunities in the formal sector of economy. However, the decrease in rural dwellers owing to mortality and migration, as well as destructive processes that took place in the Ukrainian economy in view of military operations led to the growth of urban informal employment at a faster pace in 2015-2016.

Informal employment is usually inherent in the population of certain socio-economic groups. Thus, in 2016, informal labour relations prevailed in the self-employment sector, where the share of the population working informally was 74.3%, and among employed population, such share was 15.1% (Table 1). By the place of residence, the share of self-employed persons is 44.8% in urban areas and 92.2% in rural areas. The reason is the mass unemployment in rural areas due to the lack of industrial, processing, social facilities.

At the same time, during 2016, the employment structure of the officially and unofficially employed population changed. Therefore, in 2016, compared to 2015, the share of officially employed population (84.9% vs. 82.7%) increased, and, respectively, the number of self-employed persons reduced (25.7% vs. 26.8% %). At the same time, reverse processes took place among the informally employed population (Figure 1)<sup>1</sup>.

Fig. 1. Official and informal employment by employment status in 2015-2016  
(in % to respective employment status and workplace type)

The analysis of informal employment by age groups shows that its highest level is peculiar to the persons aged 15-24 (35.6%) and 60-70 years (36.0%). The specified

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<sup>1</sup> Ринок праці у 2016 році. (2017). Офіційний сайт Державної служби статистики України <<http://ukrstat.gov.ua/>>

categories of population are more vulnerable and socially unprotected in modern economic conditions. The incidence of informal employment among persons who attained pension age is primarily due to the low level of pension provision, which prompts them to seek additional means of living (Table 2). In most cases, the informal employment in young people is manifested in the need for additional earnings during education. Also, this fact is evidence of the existence of objective and subjective factors that impede the employment of young people in the formal sector of economy.

It is proved that in all age groups, the level of informal income is about one third. The most active, mobile and productive age group as the highest level – 35-39 years old (36%)<sup>1</sup>.

Table 2.

Unofficial employment of population by age groups in 2016

	Total		Including by age groups (years old),							Working age, K, persons
	K, persons	in % to total employed	in % to total employed population of the respective age group							
			15–24	25–29	30–34	35–39	40–49	50–59	60–70	
<b>Total</b>	<b>3961,2</b>	<b>24,3</b>	35,6	25,3	23,0	23,0	21,8	22,6	36,0	<b>3726,6</b>
Women	1669,0	21,3	31,5	21,2	18,5	20,3	18,7	20,8	38,5	1539,6
Men	2292,2	27,1	38,9	28,4	26,5	25,4	25,2	24,5	33,5	2187,0
Urban settlements	1891,9	16,9	25,9	18,8	17,6	16,7	15,6	15,0	14,7	1832,2
Rural area	2069,3	40,6	48,3	39,4	39,3	39,1	35,1	39,2	71,7	1894,4

Education has a significant impact on informal employment: the lower is education level, the lower is income and the higher is the need in additional income in the informal sector. In 2016, among the informally employed population, two thirds (66,2%) were the persons with vocational and complete secondary education, and those with higher education (including complete, basic and incomplete higher education) predominated among the officially employed population (61.2%).

Mostly, people with low education level and those who are engaged in physical or unskilled labour are employed unofficially. In particular, the share of unofficially

<sup>1</sup> Ходжаян, А. (2017). Тенденції функціонування неформального сектору економіки України. *Економіка*, 1 (190), 35-41.

employed was among the employees with the simplest professions was significantly higher than among the officially employed population (49.0% vs. 9.2%).

Among economic activities, the most widespread informal employment was in agriculture, forestry and fishery (40.8%), in wholesale and retail trade, repair of motor vehicles (20.9%), and in construction (15.5%) ( Figure 2)<sup>1</sup>.

Fig. 2. Unofficial employment of population by economic activities in 2016  
(in % of total unofficially employed population)

The biggest share of unofficially employed persons did not exceed the average in Ukraine (24.3%) in total employed population in 2016 in eleven regions of the country. The highest value was observed in Ivano-Frankivsk region (53.2%), and the smallest in Kyiv region (10.3%).

Despite the considerable work done and the received analytical material based on the results of sampling population survey in economic activity, State Statistics Service of Ukraine is limited only to the labour market framework and does not examine earned and entrepreneurial income from informal employment, as well as the underestimated value of the gross product that can called the «result» of informal economy functioning.

The above mentioned quantitative data allows to find out the features of informal employment in Ukraine. Since the labour market of Ukraine refers to transformational model, according to its characteristics, informal employment in Ukraine is similar to comparable phenomena in Third World countries: significant scales for the spread of informal employment, low educational level of unofficially employed persons, poor development of industrial and manufacturing spheres, blurring the boundary between formal and informal employment. Secondary nature of informal employment makes Ukraine similar to the developed European countries. At the same time, informal employment in Ukraine has a number of specific features. Since informal employment

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<sup>1</sup> Ринок праці у 2016 році. (2017). Офіційний сайт Державної служби статистики України  
<<http://ukrstat.gov.ua/>>



is secondary, its earnings are lower than those earned through official and unofficial activities. Total number and share of unofficially employed are distributed unevenly and depend on the region and territory of residence. In rural areas, informal employment is hardly the only mean of survival. Because of this, the share of informally employed people in the agrarian western and northern regions of Ukraine is the highest. This explains the prevalence of self-employed persons among the unofficially employed.

The majority of population involved in the informal economy makes its choice consciously and voluntarily in favour of it. Thus, informal employment has transformed into a strategy for adaptation and operation of social agents in market economy. First of all, it concerns self-employed persons. At the same time, many employers are inclined to breach labour legislation, imposing informal employment as a non-alternative phenomenon. Therefore, it is precisely for hired employees that informal employment has a forced nature and is a manifestation of exclusivity and numerous derivations they experience in everyday life<sup>1</sup>.

Since most employees expect to receive a minimum retirement pension, they are not interested in paying significant contributions. Therefore, the employees agree to receive salary «in envelopes». Solidarity pension system creates a favourable environment for dependents in the society and discredits productive labour. Thus, it is necessary to establish a close relationship between making personal pension contributions to the Pension Fund of Ukraine and the amount of pension, which will be a strong incentive for the hired employee to get official salary paying all deductions.

To ensure the transition of the entities from informal sector of economy to the formal one, we consider it necessary to form a favourable economic and institutional environment for this process, and to make appropriate promotion among the population. The sphere of the shadow economy is capable of preserving its attractiveness until the conditions for equally profitable activities in the field of legal entrepreneurship are created.

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<sup>1</sup> Струченков, О.В. (2014). Неформальна зайнятість населення України: кількісний та якісний виміри. *Сучасні суспільні проблеми у вимірі соціології управління*, 281 (15), 228-234.

Wages in Ukraine are one of the lowest in the world. At the same time, the main component of tax revenues is payroll budget, however it is strange. An incomprehensible paradox - the most oppressed factor of production - labour - is the main source of revenue in the country's budget. This reality is the result of disproportions between primary factors of production (labour, capital), which results in unjustified high tax burden on incomes of population and business<sup>1</sup>.

The increase of minimum state guarantees in labour payment is one of the measures taken in many European countries with the aim of legalization of wages and introducing mandatory formal employment. It is anticipated that increase of minimum wage levels and its annual review will promote legalization of wages and increase revenues to the budgets at all levels. The increase of minimum wage by 2 times since 01.01.2017 was definitely a positive step for hired employees and the state, but in parallel led to undesirable consequences - dismissal of the part of hired employees by employers.

Assessing the current taxation system in Ukraine, one can state that there is an excessive total tax burden on the population and its unfair distribution by various groups. This is especially true for indirect taxes included in the price of goods and services, and their amount for a taxpayer does not directly depend on his income. Due to the fact that consumption structure varies for different segments of population, the principle of reasonable taxation may be implemented through differentiated approach to indirect taxes on individual goods and services. The development of the optimal taxation idea also requires a better justification of the progressive scale, while fixing the amount of real non-taxable minimum, based on the fact that each member of the society has the right to things and services necessary for his existence. Thus, fairer distribution of the tax burden will help to unshadow informal sector of the economy.

The government should introduce the measures aimed at minimizing the impact of systemic factors shadowing the economy that are still insurmountable and relevant, namely:

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<sup>1</sup> Харазішвілі Ю.М. (2011). Тіньова зайнятість та тіньова оплата праці в Україні: оцінки та прогнози. *Стратегія розвитку України. Економіка, соціологія, право*, 4 (1), 171-182.

- Low efficiency of the state in providing the institutional bases for the development of competitive economy. This is due to the high weighted average rate of taxation of enterprises in Ukraine (52.2%), whereas in Europe and Central Asia it equals to 34.8%, while in OECD countries it is 41.2%.

- Excessive regulatory and tax pressure on the corporate sector, high payroll taxes, which pushes employers to hide real level of employee wages and keep informal employment practices. By subindex Impact of Taxes on Incentives to Labor in GIC 2015/2016, Ukraine has the 121st rating among 140 countries.

- Low efficiency of functioning of judicial and law enforcement agencies. The level of independence of the judicial power and the reliability of law-enforcement bodies are assessed by international experts as extremely low (respectively 132 and 133 in the GIC rating 2015/2016).

- High level of corruption.

According to the world practice, the main prerequisite to reduce the number of persons employed in the informal sector of economy is to promote small business development. Small business sector in foreign countries with developed market economy is one of the most important and provides about 70% of workplaces and 50-65% of gross domestic product. In the United States, for example, 54% of population is employed in small businesses, 73% in Italy, and 78% in Japan<sup>1</sup>. These are countries with stable economic development, stable high standard of living, significant share of population generates its standard of living due to the functioning of small business it. It is possible to achieve the development of small business by reducing tax burden, facilitation of registration procedure and activity licensing, providing benefits to the employers who create jobs, to exempt from tax burden a profit share invested in production expansions and creation of new jobs.

**Conclusions.** Therefore, main direction of legalization of employment, labour and entrepreneurial incomes is:

- ✓ ceasing mass impoverishment of population,

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<sup>1</sup> Дідух, О.А., Кравець, І.М. (2014). Неформальна зайнятість як соціально-економічне явище. *Вісник Хмельницького національного університету*, 3(2), 79-83.

- ✓ increase in demand for labour in official economy,
- ✓ reduction of tax burden;
- ✓ decrease of personal income differentiation and ensuring social justice (by introducing progressive taxation with simultaneous control over income and expenses);
- ✓ introduction of measures to increase tax ethics;
- ✓ increase of minimum state guarantees in the field of personal income (policy of developing wage growth);
- ✓ establishment of a close relationship between making personal pension contributions to the Pension Fund of Ukraine and the amount of pension.

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[6533-4ab6-b56f-50e5243eb15a&tag=TendentsiiTinovoiEkonomiki](https://doi.org/10.6533-4ab6-b56f-50e5243eb15a&tag=TendentsiiTinovoiEkonomiki) (2017, June, 12). [In Ukrainian].

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