

Employment and Social Affairs Platform

Policy Brief
On
Undeclared work in Albania
-evidence and policy recommendations-

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List of abbreviations

GDP - Gross Domestic Product

GTD – General Taxation Directorate

KPIs - Key performance Indicators

LFS - Labour Force Survey

SSO - State Statistical Office

VAT - Value Added Tax

WB – Western Balkans

1. Introduction

Undeclared work – work that in itself is legal but not declared to the authorities for tax, social security and/or labour law purposes – plays an important role in all economies in the Western Balkans. This challenge has been recognized both in the national Economic Reform Programmes¹, prepared annually by the Western Balkan economies as part of their economic governance dialogue with the EU, and the EU strategic documents related to the enlargement process^{2,3}.

In this context, under its Employment and Social Affairs Platform project and in close coordination with Ministries of Labour and Social Affairs, the Regional Cooperation Council (RCC) has commissioned diagnostic reports for each Western Balkan economy, which review and assess in-depth direct and indirect policy approaches with regard to undeclared work and provide rapid appraisal of applicability and transferability of EU policies to the WB6 economies. The insights in these reports will be further discussed in national and regional fora and will provide the trigger for future collaboration and mutual learning in tackling undeclared work.

Inspired by the successful experience of the European Platform Tackling Undeclared Work, this work will support the establishment of a WB6 Network for Tackling Undeclared Work, with the immediate objective of enhancing cooperation on tackling undeclared work using a holistic and integrated approach, that joins up on the level of both strategy and operations the policy fields of labour, tax and social security law, and involving social partners.

This policy brief draws on the diagnostic report for Albania and aims to provide information related to the current size, character and drivers of undeclared work in Albania, a summary of policy measures employed so far by the government and outline some key indicative recommendations for policy makers and other stakeholders to better address undeclared work.

2. Evidence and analysis

2.1 Informal economy

The informal economy sprouted upon the fall of communist regime in 1991 when the private sector flourished. The rapid pace of privatization process between 1991 and 1994 transformed 70 percent of the economy into private. This fast transformation associated with the weak role of the state and capacity to design an effective regulatory, legal and institutional framework further fuelled this phenomenon.⁴

Estimates of the size of informal economy and undeclared work vary depending on the measurement methodology employed. The Albanian Institute of Statistics (2002) concluded that the Albanian informal economy as a share of gross value-added is 27.9 percent.⁵ The Organisation for

¹ https://ec.europa.eu/neighbourhood-enlargement/policy/policy-highlights/economic-governance_en

² The communication of the European Commission on a credible enlargement perspective for and enhanced EU engagement with the Western Balkans, 2018 recognizes that economic development in the region is hampered by an entrenched grey economy.

³ In its Communication on EU Enlargement Policy, the European Commission emphasized that all Western Balkan economies face high unemployment rates and persistently high levels of informal economy (European Commission, 2018)

⁴ Ruli, G. (2003) "Characteristics of Informal Sector Development in Albania", Chapter 13 in Belev, B. [ed.] *The Informal Economy in the EU Accession Countries: Size, Scope, Trends and Challenges to the Process of EU Enlargement*, Center for the Study of Democracy, Sofia.

⁵ OECD, "The informal economy in Albania, analysis and policy recommendations," December 2004, <https://www.oecd.org/investment/investmentfordevelopment/35443365.pdf>.

Economic Co-operation and Development (2004) estimated the size of the informal economy as a share of gross value-added at 26.6 percent in 2002 and 26.0 percent in 2001.⁶

Muco *et al.* (2004), drawing on different estimations methods (electricity method, monetary method, national accounts method), concluded that informal economy in Albania varies from 30 to 60 percent of GDP.⁷ In 2015, the Albanian government disclosed that the informal economy makes up 50 percent of GDP.⁸ Medina and Schneider (2018) measure the size of informal economy as a proportion of GDP using the Multiple Indicators Multiple Causes (MIMIC). According to this method, the average size of informal economy amounts to 32.72 percent.⁹

The World Bank Enterprise Survey is a prominent direct method used to estimate some patterns of the informal economy. As indicated in Table 1, 40.2 percent of surveyed businesses in Albania accept that they do compete with unregistered/informal businesses, higher than the average for Europe and Central Asia. Manufacturing firms are more likely to compete against unregistered or informal firms than service sector businesses (41.2 percent compared to 39.7 percent). The same is true when it comes to the percentage of firms identifying practices of competitors in the informal sector as a major constraint. A higher percentage of manufacturing firms (23.4 percent) consider other informal businesses as a major constraint compared to the service sector firms (18.1 percent).

Table 1: Prevalence and impacts of informal enterprises in Albania, 2013

Indicator	Albania	Europe and Central Asia	All Countries Globally
Percent of firms competing against unregistered or informal firms	40.2	38.1	54.3
Percent of firms identifying practices of competitors in the informal sector as a major constraint	19.9	19.5	28.3

Source: World Bank Enterprise Survey 2013.

2.2 Undeclared work

In terms of undeclared work, a few statistics could be drawn to elaborate on its size and nature.

Southeast Europe Leadership for Development and Integrity (SELDI, 2016) conducted a survey in Albania with 1,050 households and the results revealed that 39 percent of respondents were employed in the informal sector. The same survey uncovered that 39.75 percent of employees declare not to have a written contract with their employer, 30.29 percent of employees declare that they do not pay for social and health security benefits while 28.82 percent of employees declare to pay social security on minimum wage and 18.9 percent receive higher remuneration than in contracts.¹⁰

⁶ Idem.

⁷ Muço, M., Sanfey, P., Luçi, E., Hashorva, G., "Private Sector and Labour Market Developments in Albania: Formal versus Informal," April 2004, <https://wiiw.ac.at/private-sector-and-labour-market-developments-in-albania-formal-versus-informal-dlp-3281.pdf>.

⁸ See here: <https://kryeministria.al/al/newsroom/lajme/lufte-kunder-informalitetit-per-te-ulur-taksat-dhe-rritur-rrogat-e-pensionet1441104996>

⁹ Medina, L., Schneider, F., "Shadow Economies Around the World: What Did We Learn Over the Last 20 Years?" January 2018, <http://www.ipm.al/wp-content/uploads/2018/01/MALAJ-Shadow-Economies-Around-the-World-What-Did-We-LEARN.pdf>.

¹⁰ SELDI (2016), "Hidden Economy and Good Governance in Southeast Europe Regional Assessment Report," http://selidi.net/fileadmin/public/PDF/Publications/HIDDEN_ECONOMY_06.pdf.

Other studies measure undeclared work based on inspections conducted by the labour inspectorate. During 2017, the Albanian State Labour Inspectorate (SLI) inspected 7,958 enterprises and reports that 706 employees were not insured, while 1,575 employees had no written contract.¹¹

The National Business Forum (2015) conducted a survey of 400 businesses in Albania and released that businesses do not report to the tax authorities 29 percent of their labour force. Businesses that do report the real number of their employees use other manoeuvres to stay less taxed such as paying envelope wages.¹²

According to the Labour Force Survey, in 2017, the share of informal employment in the non-agricultural sector was 30.3 %, decreasing compared to 2016 by 1.6 percentage points, and by 3.8 percentage points compared to 2015¹³.

2.3 Policy approaches

The Albanian government has taken courageous measures to reduce the informal economy and particularly the undeclared work. On one hand, fundamental reforms towards improving the business environment were initiated. On the other hand, the General Taxation Directorate started with the implementation of an ambitious action plan to tackle informality. Nonetheless, the level of undeclared work remains high. Therefore, further efforts are required in this regard, especially to tackle the informal economy and undeclared work through a holistic strategic approach. To employ effective reforms, a thorough understanding of the size and nature of informal economy and undeclared work is essential.

Albania does not have a single agency to tackle informal economy and undeclared work. Undeclared work is mostly tackled by SLI, while tax non-compliance by tax administration. SLI was moved under the Ministry of Finance and Economy in 2017 and this was considered as positive by various stakeholders, because it could yield a better coordination between SLI and General Taxation Directorate (GTD), which is under the Ministry of Finance and Economy.

In September 2015, the Albanian government elevated its focus on informality and undertook diverse actions to mitigate the associated issues. Direct and indirect control measures were put in place. The past four years have seen steady increases of the **penalties and sanctions** for informal employment in Albania.^{14/15/16}

In June 2016, an amended Labour Code entered into force. The amended Code made the **written contract between employer and employees mandatory**, while before the changes the contracts and its amendments could also be made verbally.¹⁷

¹¹ Albanian State Labour Inspectorate (2017), *Annual report*, Tirana, Albania.

¹² Kosta, B. (2016), "National Business Forum Perspectives on the Issue of Informality in Albania," Tirana, Albania.

¹³ <http://www.instat.gov.al/al/publikime/librat/2018/tregu-i-pun%C3%ABs-2017/>

¹⁴ Starting from September, 2015 when the government started the actions against informality.

¹⁵ Law 99/2015 on some changes and additions to the law no. 9920, dated 19.05.2008 "On tax procedures in the Republic of Albania as amended".

On September 21, 2016, decision on the proposal on some additions and amendments to the law no. 9920, dated 19.5.2008, "On tax procedures in the Republic of Albania".

¹⁶ Read here: <https://www.tatime.gov.al/c/6/69/procedurat-tatimore>.

¹⁷ Specifically Article 21, Point 1 changed from: "The labour contract may be concluded and amended verbally or in written manner" into "The labour contract may be concluded and amended in a written manner".

The old Labour Code, <http://www.qbz.gov.al/botime/Kodi%20i%20Punes%202014.pdf>. The new Labour Code: <http://www.qbz.gov.al/botime/Kodi%20i%20Punes-2016%20i%20azhurnuar.pdf>

Improvements were made to the **detection system of undeclared work**. The GTD introduced risk assessment analysis to select businesses which will be the subject of an inspection. However, only 70 percent of businesses are selected using the system while the remaining percentage continues to be manually selected. In addition, the GTD has created on its **website a section "fighting informality"** where businesses can report concerns about possible tax abuses.¹⁸

The government **reduced the Value Added Tax (VAT) for the supply of accommodation services** from 20 percent to 6 percent.^{19/20} In 2018, the government released the decision to **reduce the threshold of VAT** in order to include into formalization scheme as many businesses as possible.²¹

The GTD has organized **informative meetings** on operations plans to tackle informal economy. However a strategy to tackle informal economy is not prepared yet.²²

Some progress has been made on **increasing labour market participation** (from 59.6% in 2013 to 66.8% in 2017) and the **quality and effectiveness of labour market institutions and services**. In addition, Albania managed to make some progress on **implementing the national employment and skills strategy** (NESS) for 2014-2020.²³ Active labour market policies continue to be implemented, however they covered only 5.5 percent of the unemployed in 2017.

In summary, the informal economy in Albania is being tackled to some extent by fighting tax evasion and promoting tax compliance, but undeclared work is not addressed in a comprehensive manner. Hence, fundamental efforts should be made towards building a holistic strategic approach to tackling the undeclared work. In this light, the following section provides some recommendations stemming from the brief analysis above.

3. Policy implications and recommendations

- **Strategic management initiatives:** a holistic integrated approach towards tackling undeclared work should be pursued. Cross-cutting strategic objectives and key performance indicators across institutions responsible for tackling undeclared work should be designed.
- **Policy measures to deter undeclared work:** the effectiveness of electronic systems for data mining, data sharing and data analysis should be improved. In terms of labour law, the amended Labour Code is being implemented. The monitoring of the implementation of the Labour Code amendments requires strengthening of data collection and instruments for disaggregated data. State Labour Inspectorate capacity and performance should be further strengthened. Other

¹⁸ See here: <https://www.tatime.gov.al/c/8/64/luftojme-informalitetin>.

¹⁹ The standard Valued Added Tax rate in Albania is 20%, except for cases where the reduced VAT rate is applicable per article 49 of the Law on VAT. One of the most important changes done through the new Decision of the Council of Ministers is precisely related to this article and stipulates that the reduced VAT rate which will be applied to the supply of accommodation services will be 6%.

²⁰ See here: <http://www.financa.gov.al/njoftime/lajme/ulet-tvsh-per-turizmin-nga-20-ne-6-ministri-ahmetaj-promovojme-sektorin-nxisim-investimet-dhe-te-ardhurat&page=3>.

²¹ The threshold was 5 million All and was reduced into 2 million All. Decision No. 652 dated 11.12.2017 "On some amendments and additions on the decision" no. 953, dated 29.12.2014, on implementation of the law No. 92/2014, "On the value added tax in the Republic of Albania", amended.

²² The government provided several reasons of taking this decision which were related to better tackling of undeclared through the prevention of any form of non-declared transactions. The main scope of this change is to include small business in the system, to track the movement of goods, as well as the obligation of big enterprises to issue an invoice for every performed transaction, <https://www.tatime.gov.al/d/8/45/45/301/dpt-takim-me-tatimpaguesit-e-medhenj-per-planin-anti-informalitet>.

²³ See here: http://www.kerkojpune.gov.al/wp-content/uploads/2014/02/Strategjia_per_Punesim_dhe_Aftesim_2014-2020.pdf.

initiatives should be employed such as the introduction of supply chain responsibility in public works contracts.

- **Supply side measures:** Incentives and smooth transition from employment to self-employment should be utilized. In addition specific sectoral policies need to be tailored (tourism sector, agriculture, etc).
- **Changing citizens' values, norms and beliefs:** Public awareness campaigns to showcase the benefits of declared work should be beefed up. This will gradually help to change the values, norms and beliefs regarding the benefits of declared work. A continuous education of citizens about the tax system and tax morality would help.
- **Reforming formal institutions:** The efforts to change the citizens' norm should be associated with the change of formal institutions. It is indispensable to develop effective training of tax and labour inspectors.
- **Improving the involvement of social partners:** Social dialogue remains weak in both the private and state sector. To raise awareness among businesses of the benefits of declared work (and costs of undeclared work) so as to increase the level of voluntary cooperation, and reduce the need for enforced compliance, social partners could also run (with support from the State Labour Inspectorate and/or Tax Administration) awareness campaigns.

4. Research parameters

This brief draws from the undeclared work diagnostic report and action plan for Albania prepared as part of a regional exercise by a team of experts for the RCC. The methodology includes a review of existing surveys on undeclared work, a desk-based survey of policy measures initiatives to explore the policy instruments used by the government, social partners and employers' organizations, and in-depth interviews with representatives of Tax Administration, State Labour Inspectorate, and economic experts.

References

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