LEGAL AND SOCIAL ASPECTS OF INFORMAL LABOUR FORMALISATION: PROSPECTS AND CHALLENGES

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ABSTRACT

Informal labour has become one of the main ways of earning income and a reason for non-payment of taxes to the state budget. Governments and international organisations are making many efforts to study the phenomenon of informal labour and formulate proposals for further formalisation of informal labour to «come out of the shadows» of activities in various fields. The relevance of our study is due to the rapid spread of informal employment and informal labour in various spheres of society, which entails economic losses for each state and a lack of faith in the declared labour relations. The purpose of the study is to identify possible ways and prospects for formalising informal labour, to determine the legal aspects of formalising informal labour, to analyse the challenges to the social protection of workers in the course of such formalisation, and to improve the current labour legislation. The author formulated legal conclusions on the legal aspects of formalisation of informal labour, the ways of such formalisation and its prospects. In particular, conclusions on social challenges for all participants in the so-called informal labour relations were pro-

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vided. Finally, proposals for improving the legislation on informal employment were formulated.

**Key words:** informal labour, informal employment, informal economy, formalisation, labour market, labour relations.

### 1. INTRODUCTION

The issue of informal labour, and in this aspect informal employment and informal labour relations, is relevant all over the world, regardless of whether it is economically developed countries or countries with low economic potential. Informality itself is a complex process and a rather confusing phenomenon. Although many analysts and scholars have paid attention to the study of the informal economy, they have not formed a unified vision and have not conducted a comprehensive study. Regardless of the fact that many conclusions have been drawn about this socio-economic phenomenon, its structure, peculiarities of its spread and its very boundaries remain uncertain. This is primarily due to the very nature of the informal economy and the blurred boundaries of informal employment. The lack of sufficient information on these phenomena, and the absence of structured and comprehensive definitions of related concepts creates the illusion of uncertainty and the impossibility of a comprehensive study. However, it is a mistake to say that a comprehensive study is impossible, and therefore further research into the problem is necessary, which is the reason for our work.

Informal labour is a widespread phenomenon in the labour market, as it is inherent in many areas of society. By performing informal labour duties, workers provide themselves with the necessary means of subsistence. In turn, the informal economy accounts for more than half of the world’s workforce and more than 90% of micro and small enterprises worldwide. However, informal labour poses a threat to the economies of various countries, as it simply hinders their development. Every year, the situation with informal employment becomes more complicated, and governments have to think through comprehensive and multi-stage steps to overcome this problem and develop a unified solution to this problem.

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It should also be noted that informality has a dual impact on the labour market, which, on the one hand, characterises the flexibility of employment and, accordingly, is a kind of shock absorber in the market, while on the other hand, the spread of informal, unofficial labour agreements increasingly worsens the information of labour legislation and leads to the preservation of unproductive employment. The topic of informal employment and informal labour has been attracting the attention of many people, from scholars to analysts and ordinary participants in labour relations, since its inception. Unlike formal labour, informal labour is not sufficiently regulated at the legislative level and therefore raises many questions - from the peculiarities of informal labour and employment, their boundaries and scope, to the challenges of social protection posed by such a spread and further prospects for formalising informal labour.

There is a wide variety of definitions of informal labour, informal employment and the informal economy in the scientific literature. Moreover, a common approach is to identify informal labour with informal employment and to consider them in a complex and inseparable manner. In addition, it is worth noting that each country develops a comprehensive approach to the definition of informal employment that is close to its labour relations, and therefore it is expected that the terms used to describe informal employment will differ and have a different nature (focus). It is also common for the same terms to have different meanings in different countries.

In the framework of our study, it is important to note that initially the informal economy and informal labour were considered through the prism of relations in developing countries. This was due to the presence in these countries of a significant stratum of the population that was not involved in the formal labour market, and therefore carried out their activities outside the law, thereby creating their employment system.

The informal sector is one of the central areas of research of the International Labour Organization (ILO), the Organisation for Economic Co-operation and Development (OECD) and the World Bank (WB). They pay considerable attention to this form of employment because it does not actually and legally comply with the requirements of the law, in fact, it exists outside the law itself and is not regulated by it. Accordingly, it poses a direct threat to formal

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employment and formal labour, human rights, as well as to the quality and sustainable development of the economy of each state. Moreover, in the course of such studies, conclusions are drawn regarding the formalisation of informal labour and the regulation of such relations between the actual employer and the employee.

For further research, it is necessary to refer to the existing definitions, namely «informal employment», «informal economy», «informal labour» and/or «undeclared labour», developed by the leading international organisations and researchers in this field. Informal (undeclared) labour is essentially a certain paid activity that does not contradict the law by its nature but is not declared to the state authorities. An important clarification is that it does not include criminal activities and activities that do not require notification of public authorities (in particular, running a household for personal needs).7

In its documents, the Organisation for Economic Co-operation and Development uses the definition of hidden employment, which means labour that by its nature is carried out within the framework of the law, but has not been declared in any way to at least one administrative body.8 The International Labour Organization studies informal labour in the context of the «shadow/informal» economy and envisages a transition from the informal economy to the formal economy, which entails the formalisation of informal labour. This hypothesis is set out in ILO Recommendation No. 204.9 According to this document, the informal economy involves various activities of employees and individual economic units that are not covered by formal norms and are not subject to legal regulation under the laws of a particular state.

Since the concepts of «informal employment» and «informal labour» are often equated or derived from each other in many policy documents, it is worth taking a closer examination of the nature of informal employment. In a broad sense, informal employment is equated with economic, commercial, financial or professional activities that are carried out in violation of the legislation of a particular country in terms of non-payment of taxes, concealment of income, lack of documentation of the number of employees, or concealment of production capacities, which affects the amount of output.10 According to the

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9 International Labour Organization, Recommendation № 204: Transition from the informal to the formal economy, 2015.
«Guidelines for the Statistical Definition of Informal Employment»\textsuperscript{11}, the main feature of informal employment is the absence of registration of labour relations with state authorities or non-compliance with other state requirements for the execution of labour contracts.

According to the documents of the State Employment Service of Ukraine, the concept of «undeclared labour» is not systematically used, and there are no regulations that would contain this definition. However, it is worth noting that in Ukraine the informal sector includes business units that are not registered under the provisions of the current legislation; repair work and other individual housing construction; non-agricultural production for own consumption; activities of self-employed persons and casual economic activity\textsuperscript{12}.

In this regard, the main purpose of our study is to identify possible ways and prospects for formalising informal labour, define legal aspects of formalising informal labour, analyse challenges to the social protection of workers in the course of such formalisation and improve the current labour legislation to improve the economic situation\textsuperscript{13}.

2. METHODOLOGICAL FRAMEWORK

This study was based on general and special methods of scientific knowledge. For a thorough research, the author used the methods of systematic analysis, synthesis, comparative legal method, dialectical method, and the method of analysis of legal acts. The method of interpretation of legal provisions was also used to formulate comprehensive conclusions.

Using the method of systematic analysis, the author processed and studied the sources of information related to the chosen topic, including the regulations of international organisations, to determine the characteristics of informal (undeclared) labour, the informal economy, informal employment and the need to formalise informal labour. As a result of the systematic analysis, the author formulated certain provisions and conclusions regarding the prospects for formalising informal labour and also identified the social challenges that subjects of informal labour relations will face in the course of such formalisation.


\textsuperscript{13} Tsymbal, O.: Undeclared labour in Ukraine: forms of manifestation, scale and measures within the labour inspection system, Kyiv, 2017.
Using the synthesis method, the author forms a general vision of the formalisation of informal labour and improvement of labour legislation with due regard for the proposals and conclusions made. Using the comparative legal method, the author analyses the legal regulation of informal labour and informal employment in terms of enshrining the concepts of «informal labour» and «informal employment» at the legislative level, as well as the understanding of these categories by various international organisations. On this basis, the author provides general recommendations for further improvement of the system of legal regulation of informal labour relations and their further formalisation.

The article uses the dialectical method to reveal the content of social challenges faced by both the State and informal workers and employers in the context of the formalisation of informal labour. By using the methods of legal document analysis and interpretation of legal provisions, the author identifies the specific features of informal labour, informal employment and the informal economy, which further achieves the stated purpose of our study.

The empirical basis of the study is the international legal acts, EU legal documents and national regulations taken for analysis. Several foreign and Ukrainian scholars have paid attention to the problems of legal regulation and standardisation of working conditions of informal workers, including Rodgers, Lipova, Petrova, Packar, Tsymbal, Williams, Lansky, etc.

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3. RESULTS AND DISCUSSION

It is worth noting that for quite a long time informal employment (even taking into account the risks logically arising from the very definitions of risks) was seen as a catalyst for business adaptation to various kinds of changes. But today, informal labour is a destabilising factor in the country’s economic sector. Moreover, it carries significant risks due to the insufficient level of response from government agencies and the lack of legal regulation of informal labour in general due to its nature. That is why there is a need to transform the sphere of informal employment and informal labour into formal employment and to further regulate such labour. In the course of formalisation, certain risks and social protection challenges will undoubtedly arise. They always exist alongside development prospects. Therefore, it is worth analysing the legal aspects of informal labour formalisation in more detail and highlighting its main mechanisms.

In general, the main mechanisms of formalisation are the characteristics of the institutional environment and economic growth factors\(^{21}\). These mechanisms have certain differences in their application. For example, economic growth factors automatically reduce the percentage of informal employment as a consequence of economic growth. Therefore, the main goal is to remove any obstacles to economic growth. As for the characteristics of the institutional environment, they assume that this is not enough\(^{22}\). However, we cannot but agree that in most cases, economic growth is the catalyst for the formalisation of informal work. Since the increase in the percentage of employment in the informal sector is due to the lack of appropriate legal regulation, unsatisfactory business climate and hidden wages, the percentage of informal employment can be reduced if the following conditions are met reforming formal institutions and improving the economic policy model in general\(^{23}\).

The following should be noted: international experience of formalising informal labour shows that strict measures taken by state authorities did not bring the desired result, i.e. were ineffective. At the same time, soft measures in the form of creating certain stimuli for the transition to formal employment brought the desired result. This is because strict measures lead to a decrease in economic activity without increasing the formal sector of the economy\(^{24}\).

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Therefore, in our view, policies to formalise informal work should be soft and incentivising, and therefore include the following response instruments:

– Formulation of a comprehensive economic development strategy and its implementation - to change the existing model of economic development that has led to the growth of informal employment; including the strategy’s coverage of the process of improving the business and institutional environment, which promotes effective anti-corruption activities and intensive creation of more formal employment opportunities;

– Modernisation of public administration through the development and implementation of specific step-by-step measures aimed at increasing the trust of both employers and employees in the tax authorities and the tax payment process itself (based on the principles of equality and impartiality);

– Improving the level and quality of public service delivery is an important factor in increasing the value of formal employment in the eyes of the population and in understanding the importance of paying taxes. This is reflected in the following - employees and employers should see the result of fulfilling their tax obligations in the form of receiving relevant services and goods;

– Implementation of a set of measures aimed at improving the quality of human capital of the country’s working population;

– Developing a range of measures aimed at informing the population about the prospects of formal employment, promoting it and reducing the negative perception of informal employment. Such measures may include educational activities on taxation and the direct link between taxes and benefits for the population. Explanatory work can be carried out regarding the conduct of informal business and criminal liability for non-payment of taxes, features of imposing fines for informal employment, etc.\(^\text{25}\)

The state should also take some measures to improve the conditions for small and medium-sized businesses and create prospects for attracting investors, which will become a springboard for further formalisation of informal labour with direct benefits for employers and employees. The so-called stimulus measures should be administrative in terms of reducing barriers to business legalisation or the creation of new businesses and expansion of existing ones\(^\text{26}\).

\(^{25}\) Tsymbal, O.: Undeclared labour in Ukraine: forms of manifestation, scale and measures within the labour inspection system, Kyiv, 2017.

Some studies suggest that the tax burden should be reduced to facilitate the rapid formalisation of informal labour, as this step would be a good incentive for many enterprises to come out of the shadows. However, such a step may not be applicable in all countries, but in economically developed countries\textsuperscript{27}. For example, in Ukraine, whose economy is in a very difficult state, the possibilities of using tax instruments to reduce Ukrainian informal employment have been virtually exhausted. Therefore, if social contributions from legal businesses continue to decline, this will not lead to an increase in the tax base, but will instead lead to a reduction in insurance revenues. And this, in turn, will have a significant impact on pensions and the quality of medical services\textsuperscript{28}.

However, it may be noted that an alternative could be to create conditions where income disclosure and tax payments are compensated by certain benefits, for example, in the field of healthcare, banking or other social services. An option for the gradual formalisation of informal labour could be partial legalisation, which means allowing entrepreneurs to have and enjoy the benefits of legal status (attracting investors, additional funding from the state through targeted programmes, protection mechanisms, etc.) and the benefits of illegal status, such as reduced tax burden\textsuperscript{29}.

Based on the above, the following legal and social aspects, approaches and mechanisms for formalising informal work can be identified:

− Define the concept of «informal labour» at the legislative level, in particular in the Labour Code, Tax Code, Employment Law, Law on Social Insurance in Case of Unemployment, etc., which should cover all types of informal labour, areas where it is widespread, the responsibility of informal labour relations, and a list of possible penalties. This should be enshrined to create a clear understanding of the essence and nature of informal labour and the risks for both employers and employees;

− Developing an economic development strategy that, in combination with the above point, will help reduce the number of workers and employers involved in informal employment;

− Legal regulation of the so-called freelancing, determination of its scope and distribution;

\textsuperscript{27} Williams, C.C., Lansky, M.A.: Informal employment in developed and developing economies: Perspectives and policy responses, \textit{International Labour Review}, 152(3-4) 2013, pp. 355-376.

\textsuperscript{28} Williams, C.C.: The changing conceptualisation of informal work in developed economies, \textit{Informal Work In Developed Nations}, 2010, pp. 11–33.

\textsuperscript{29} USAID “Leadership in Economic Governance” Program, 2015.
- Simplifying and reforming administrative and fiscal procedures for companies to give them an incentive to comply with the law\textsuperscript{30};

- Strengthening cooperation between the relevant structural units of state authorities in terms of detecting violations of labour relations registration or payment of tax and insurance payments;

- Create a register of organisations that use informal or «shadow» employment and introduce restrictions on the participation of such organisations in public tenders\textsuperscript{31}.

- The legal framework should include rules governing the rights and obligations of formalised workers, such as minimum wages, working hours, working conditions, leave, protection from discrimination and other aspects of employment;

- Creating a favourable business environment, including space for entrepreneurial activity, simplified business registration procedures, support for small businesses and access to financial services;

- Promoting an inclusive labour market that provides for equality of opportunity and rights for all employees. Such a labour market includes mechanisms to reduce barriers to entry into the labour market, adaptation, expand access to education and training, promote entrepreneurship and small business development, and reduce social inequality\textsuperscript{32};

- Creating favourable conditions for attracting foreign and domestic investors;

- Develop and implement potential opportunities for accessible business services, markets, technology and infrastructure;

- Coordinate international cooperation mechanisms.

It is also worth analyzing what prospects will be opened for the state, for society and the workers themselves within the framework of the formalisation of informal work. The following can be attributed to them:

- Provision of social protection – primarily health insurance for employees, accident insurance, and pension;

\textsuperscript{30} Tsymbal, O. I.: Counteracting informal employment in Ukraine: assessment approaches and policy priorities, 2017.

\textsuperscript{31} Tsymbal, O.: Undeclared labour in Ukraine: forms of manifestation, scale and measures within the labour inspection system, Kyiv, 2017.

− Progressive and sustainable economic development of the state - due to the transparency of tax payments, the amount of contributions to the budget will increase, the tax base will expand, and therefore the economy sector will gradually change for the better;

− Protection of employees' rights - the formalisation of informal labour implies legislative protection of employees' rights. As a general rule, this applies to the established minimum wage, standardised working hours, the right to paid leave, parental leave, study leave, protection from discrimination, etc.;

− Ensuring social justice - this point flows seamlessly from the previous one, as it helps to eliminate the problems of exploitation, underpayment and illegal working conditions that are often observed in the informal sector;

− Ensure greater transparency in the labour sector and support the fight against illegal activities such as tax evasion and illegal employment;

− Stimulating the development of human capital - this in turn allows employees to access educational courses as part of their upskilling, training and professional development, which improves their skills and competencies. Such actions will lead to increased productivity and innovation among employees, and globally contribute to the development of the economy as a whole;

− Creation of a favourable business environment - this perspective is the simplification of the procedures for registering an enterprise, reducing bureaucratic administrative barriers and supporting small and medium-sized businesses. The creation of such an environment contributes to the development of the business itself, an increase in the number of jobs, tax revenues and improved employment conditions.

Along with the prospects for formalising informal work, certain social protection risks are worth discussing in more detail. Social risks are associated with the possibility of negative situations with possible losses as a result of adverse factors affecting a particular object. Informal employment itself is an area of risk, and its formalisation can lead to the disclosure of hidden risks and the emergence of new ones. The following risks in the process of formalising informal labour can be identified:


- Lack of financial sustainability and stability - formalisation may place a financial burden on both employees and employers. Under the new formalised status, employers will be obliged to pay social contributions and taxes, which will increase costs. At the same time, employees may receive significantly lower wages, as employers will have to deduct the amount of taxes from the already official salary;

- Mandatory access to social protection - may include reform of social programmes and systems to ensure participation of formalised workers and their entitlement to benefits such as health insurance, pensions, etc.;

- Compliance with social protection standards - setting minimum wages, working hours and other parameters can be a challenge, especially in sectors where workers have different skill levels and perform a variety of jobs;

- Creation of mechanisms for employers to provide social protection - establishment of administration systems capable of tracking employer and employee contributions, monitoring compliance with social protection requirements, and ensuring timely and fair payments of benefits and support;

- Risk management - consists of the development of risk reduction strategies for employees and employers, including protection against job loss, and payment of compensation in case of temporary unemployment.

Within the framework of the study, we are also forced to state the fact that despite all attempts, opportunities, and proposals, it is a priori impossible to completely eradicate informal labour. Its percentage can be reduced, undoubtedly, taking into account the above arguments. The problem lies in the policy and capacity of the state itself, its economic development, political and legal aspects, and the ability to allocate significant funding to address informal employment issues. In fact, formalisation itself significantly increases costs for the enterprise and for consumers of its services or goods, which significantly reduces supply and demand. Undoubtedly, the formalisation of informal labour will bear fruit in the long run, but it requires considerable effort, funding, legislative intellectual activity and global study of this issue.

4. CONCLUSION

The formalisation of informal work requires a systematic approach and in-depth analysis of the nature of informality. In addition to the existing perspectives - ensuring social protection, progressive and sustainable economic development of the state, protection of workers’ rights, ensuring social justice, ensuring greater transparency in the labour sphere and supporting the fight against illegal activities such as tax evasion and illegal employment, stimulating human capital development,
and creating a favourable business environment - there are several social challenges. Social protection challenges in the course of formalising informal work include the lack of financial sustainability and stability, mandatory access to social protection, compliance with social protection standards, the establishment of mechanisms for employers to provide social protection, and risk management.

Government agencies have some tasks to limit informality. For example, it is the restriction and reduction of the scope of informal employment, since it is a priori impossible to completely rid the labour market of informal labour. Therefore, first of all, it is necessary to think over a detailed and long-term strategy for the economic development of the state, which will be different from the existing one, which will lead to the growth of informal labour. The public administration system needs to be modernised to increase the level of public trust in the state authorities, including employers and employees.

A logical extension is to improve the level and quality of public services, as this is an important factor in increasing the value of formal employment in the eyes of the population and in understanding the importance of paying taxes. Employees and employers will see the result of fulfilling their tax obligations in the form of receiving relevant services and goods. Several measures should be taken to familiarise the population with the prospects of formal employment, to promote it and to increase the negative perception of informal employment. For example, such measures could include educational activities in taxation and the direct link between taxes and benefits for the population. There may be explanatory work on running informal businesses and criminal liability for tax evasion, as well as on the specifics of imposing fines for informal employment.

In the global aspect, the economic policy model as a whole should be fully improved and all the problematic aspects should be worked out. Without a doubt, informal work will expand to new horizons, attracting potential employers and employees with certain benefits, mostly financial. It is very difficult to refuse them because the current economic situation not only in Ukraine but also around the world leaves much to be desired. Both at the international and national level, responsible authorities should consider a set of actions and measures that will first stop the spread of informal labour and then promote its formalisation. Such measures should be soft and gradual and include certain incentives for employers and employees.

The formalisation of informal labour should be more voluntary, but with mandatory legal regulation, to accelerate economic progress, not stop it. The peculiarities of the labour markets of different countries should be taken into account in general and separately. This should be done to develop effective procedures for formalising informal labour and introducing the experience of countries where this is more successful to those that are only at the initial stages.
LITERATURE


   – DOI: https://doi.org/10.1108/13552551211253919


   – DOI: https://doi.org/10.1111/j.1564-913X.2013.00196.x
