

# UNREGISTERED EMPLOYMENT IN TURKEY

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## **Abstract**

*It is vital for the Government- as a whole of organized institutions and associations- to be aware of economic and social developments in its borders. That the economy of the government is registered and therefore presence of reliable statistical information have important effects on the functions which the government undertakes such as for whom and how much commodity and service it will produce, how to finance the expenditures for these products, in the light of which data that the policies to be produced will be drawn for economic and social life, and how to create social peace and free competition environment.*

*Informal economy is an important problem of underdeveloped and developing countries and just as the developed countries. Unregistered employment constitutes the major step of informal economy in all countries because informal economic actions are executed thanks to unregistered employment. In case that the individuals do not perform unregistered actions, it cannot be mentioned about informal economy.*

*In this paper, the reasons of unregistered employment in Turkey, its effects and comparison with the world will be dealt with.*

**Key words:** *informal economy, unregistered employment, employment taxes, social security bonus.*

**JEL:** *E21, H20, H30, J38, K34*

## **1. Introduction**

Economic life in our present-day world has a multi-functional and complex constitution. The number of the goods and services has increased, the technologies used have developed, employment facilities have changed and diversified, the developments abroad and inland have changed economic actors and positions. Such quick and multi-dimensional changes and developments may not allow the government to control and regulate what happens in economic life.

The rules which are set up by the government to arrange economic and social lives cause the ones wishing to earn more money to get closer to informal economy. Although the individuals and institutions which are active in informal economy carry some risks, they will both earn more money and get rid of some kinds of bureaucracy. However, these activities include disadvantages for the government and other individuals and institutions. The government is deprived of taxes and other official revenues which are unregistered. Other individuals and institutions are affected negatively due to unfair competition.

Unregistered employment and informal economy are the concepts which are bound to each other. The ones who produce informal goods and services and who do not notify this to the local government usually employ unregistered workers. The most important problem emerged with the reflection of informal economy over working life is the unregistered employment which emerged as employing unregistered and undeclared illegal worker or working unregistered in his self name and account by violating the rules and regulations

which make it mandatory to obey social security system and the law rules regulating the working life. While unregistered employment is in the form of not notifying the labours of the workers to public establishments; it may also be in the form of incomplete notification of labours as day and payment.

Informal economy is closely related with the development levels of the states. From developed countries to underdeveloped ones, proportion of informal economy in national economies represents accrual.

Actually, proportions of informal economy and therefore unregistered employment in underdeveloped and developing countries are quite high. Unregistered employment in Turkey as a developing country makes up half of the employment in parallel with informal economy.

In the study, concepts of unregistered employment and informal economy will be explained and the tight relation between them will be dealt with. Afterwards, the reasons of unregistered employment and its economic and social results will be given place. In the last part, dimensions of unregistered employment in Turkey and in the world will be compared and works and solution proposals devoted to curb unregistered employment will be mentioned.

## **2. Concepts of Informal Economy and Unregistered Employment**

### **2.1. Informal Economy**

If it is to make a general definition, informal economy is the whole of economic activities that cannot be estimated according to known statistical methods used to calculate gross national earnings and revenue bringing. (Derdiyok, 1993: 54).

The concepts such as underground economy, informal economy, hidden economy, secret economy, second economy, black economy, illegal economy, untied economy, irregular economy, parallel economy, unreceipted economy, invisible economy, marginal economy, shadow economy, loss economy, tax-exempt economy, are used instead of informal economy. Informal economy- from the point of taxation- is the whole of activities which are left out of knowledge field of tax administration with the incentive of tax-evasion and avoiding from taxation. (Altuğ, 1994:15).

### **2.2. Unregistered Employment**

Unregistered employment is generally keeping the workers away from awareness of the government, employing unskilled workers, violating the regulations such as minimum age level (child labour), minimum wage, overtime, workplace standards, health and security of workers.

According to this definition unregistered employment: means the ones who are not enrolled in any social security institution for the work s/he makes in the reference week. According to another definition, it is non-declaration of the workers to related public institutions and organizations or avoiding from legal responsibilities such as tax and social security bonuses etc. due to incomplete declaration (MLSS, 2004a:27). Then -as understood from the definition- the most important aspect of unregistered employment is reduction of public revenues.

### **2.3. Relation between Unregistered Employment and Informal Economy**

In a country where there is no informal economy, it cannot be mentioned about unregistered employment. There is a close relationship between unregistered employment and informal economy. The ones producing goods and services unregistered also employ unregistered workers. So, in the countries where informal economy is high, the unregistered employment is high, too. In the rising market economies, it takes the attention that economy and employment have shifted to unregistered and informal ones in increasing intensity since 1970s. But, informal economy, when both Turkey's economy and other countries' experience

are observed, is in a very complicated and multi-dimensional structure with its reasons, results, and operation. While expansion of informal economy causes the workers to become unsecured on one hand, and it causes on the other hand unfair competition against formal economy. Most importantly, it causes public shortfalls to get bigger and the social security system to break down by giving way to reduction of finance resources hoped to be supplied by taxation revenues (Us, 2004;1).

### **3. Reasons of Unregistered Employment**

The main reasons of unregistered employment are these (MLSS, 2004b, 4);

-Excessiveness of responsibilities and formalities about employment: The most two important reasons of increasing volume of informal economy are tax load and taxation regulations of the public. There is a positive relation between them. As the tax levels and legal regulations increase, the cost of informal economy increases, too (Han et.al., 2006:237).

In addition to tax and other loads that the government takes from over the workers, excessiveness of the formalities as a result of employment's declaration makes informal economy tempting. The cutbacks from the salary such as insurance bonus and tax constitute a big load for the employer.

The major element which determines presence of market economy is competition. Informal economy which impairs competition conditions has aggravated the crisis which is experienced currently. The employer who at last notifies his insured worker to the institution falls back in the competition while fulfilling heavy fiscal responsibilities. The employer whose profit decreases is shifted to informal economy after some time as he will be disadvantaged in comparison to the one who makes production via illegal worker.

- Unfair distribution of the income, poverty and unemployment: Added value that the poor and low-educated workers produce in the production is low, too. As a result, the bonus and tax paid for these people may surpass the added value which these people produce.

- Lack of efficient inspection: Especially public institutions in underdeveloped countries are not efficient. Lack of inspection mechanism and non-deterrent fines make unregistered employment tempting.

- Unattractive social security services: Social security services interest individual's future closely. Social security services which minimize the concerns and possibilities about the future are seen as a serious deficiency in developed societies.

- Highness of unemployment rate and lowness of added value of the employment and uneducated labour power: In the studies carried out, it's been found out that education levels of the people working unregistered are low. As the chance of work choice for uneducated people is low, they find works unregistered.

- Lack of coordination and corporation between public establishments: In coping with unregistered employment, the government and citizens must have mutual agreement. A serious corporation between state agencies must be provided because unregistered employment entails corporation of more than one state agency.

- Reasons arising out of social security system: Dissatisfaction of the services that social security systems offers bring unregistered employment with itself. In this case, the insured applies to agree with the employer and by leaving his/her works unregistered partly or wholly (as daily or wage) he or she may wish the employer to add the money to his wage which the employer pays to the institution.

#### **4. Results of Unregistered Employment**

It is inevitable for the government to struggle with unregistered employment together with its all institutions and associations for expansion of production and employment, prevalence of social security, arrival of health and social security services to a certain standard, clearing away fiscal crises in social security institutions and state finance.

There are positive and negative effects of unregistered employment in economic and social lives. Negative effects: It creates unfair competition (Türk-İş, 2005:2, Us, 2004:15, Gümüş, 2000:68), reduces tax revenues (Us, 2005:95), impairs the trust to the government, curbs the reliability of statistical information (Türe, 2004:138), destroys income distribution, causes the country to reach at macro plan and its goals (Han vd., 2006:236), reduces loan point of the country, causes disqualified production of goods and services, impairs social life (law system) (Türk-İş, 2005:3), supports inflation, enhances unemployment, decreases production and investment, reduces export, causes brain drain (Alptürk, 2007), hinders developments of syndicate activities, employment fields which are deprived of social security and are unhealthy.

There are some benefits of unregistered employment: These are: It provides employment (Türk-İş, 2005:3), supports economic growth (Sarılı, 2002:44), supplies optimum distribution of the resources (Altuğ, 1994; 67), increases competition power of the country (Sarılı, 2002:44), and increases tax revenues.

#### **5. Positive Effects of Taking Unregistered Employment under Registration**

With taking unregistered employment under registration, the following results emerge (MLSS, 2004b;32):

- Bonus revenues of social security institutions will increase
- With the increase of bonus revenues, relatively real increase can be achieved in the pensions
- The quality of health and insurance services provided by social security institution will increase
- Financial burdens on the institutions which work in accordance with the rules will reduce.
- With the increase of registered employment, social security bonus levels that workers and firms pay will reduce gradually.
- The people who work unregistered will have health and social security rights that they were deprived of formerly.
- Competition conditions which operate positively in the direction of unregistered firms will shift to the ones which realize its legal responsibilities and pay its taxes.
- Qualified workforce and therefore productivity will increase.
- With the reduction of unhealthy employment conditions relative reduction will occur in work-related accidents and occupational disease.
- Child labour will diminish.
- Employment conditions of women, handicapped people, and other people open to abuse will get better gradually.
- Unregistered foreign workers will be prevented.
- Urban strawl problems arising out of immigration will disappear.
- It will provide work security system to develop into more positive points
- Credibility and investment reliability in international arena will be gained.
- Justice in taxation will be accomplished.

- With the increase of registered employment, it will be reached to an organized society via unions.
- Substandard and disqualified goods and service production will reduce.
- Economic plans will be able to be done on the basis of more realist data.

## 6. Dimensions of Unregistered Employment in Turkey and in The World

In this part of the study, firstly unregistered employment rates in some countries will be dealt with. The relation between countries' development levels economically and unregistered employment rates will be highlighted. Afterwards, the number of unregistered employment in Turkey will be given. The reasons of high proportion of unregistered employment in Turkey will be explained and policies about the solution of the problem will be proposed.

### 6.1. Unregistered Employment in the World

Experimental findings show that unregistered activities are more prevalent in underdeveloped countries (Carillo-Pugno, 2004:273). Unregistered employment grows on a vast scale according to OECD data, except for Russia. Unregistered employment in Brazil takes up half of the whole employment, and in India %85 (OECD, 2007:2).

**Table1:** Dimension of Unregistered Employment in some Countries

Countries	Share of Unregistered Employment in GNP
France	14.7
Germany	14.8
Italy	27.2
Holland	13.8
Spain	23.0
Sweden	19.5
England	13.0
USA	10
Peru	60
Niger	76
Turkey	48.9

Resource: www.tisk.org.tr, www.tuik.gov.tr, Antunes-Cavalcanti (2005).

Unregistered employment increases 2-3 folds more than the increase in GNP of the countries because informal economy grows faster than the formal one. The Table 1 represents the share of unregistered employment in GNP for Turkey and some countries. Unregistered employment rates are quite low in developed countries such as USA, England, Germany, Holland, France, and Sweden. The rate of unregistered employment in Italy and Spain which completed their developments later has a bit risen. The rate of unregistered employment in Peru and Niger which are underdeveloped is quite high. Unregistered employment rate of Turkey which is a developing country is %48,9 (TSI, 2007:2).

The countries which have the biggest informal economy are the ones where inflation is constant, unfair and speculative earnings increase, the incomes are distributed unfairly, and the economy is out of control (Dura, 1997: 6, Toptaş, 1998: 85).

## 6.2. Unregistered Employment in Turkey

The sectors in which informal economy is prevalent in Turkey are agriculture, construction, retail commerce, traditional sectors like gift and home services, manufacturing and company services and reformist modern sectors where people are basically self-employed (Kenar, 2002).

The ways of unregistered employment in Turkey are these (Yereli-Karadeniz, 2004:182-194):

- Non-declaration of the works of the employee to related public institutions and organizations.
- Incomplete declaration of the works of employee as wage
- Incomplete declaration of the works of employee as day
- Non-declaration of the works in a second job
- Unregistered employment under the name of trail period
- Wagerworkers declared to social security institution and non-declared to tax administration
- Unregistered employees who work unregistered on their own will (foreign illegal workers, child workers, retired people working unregistered, the ones taking orphan wage as well as working unregistered, the ones taking invalidity contribution as well as working unregistered, the people taking unemployment benefit as well as working unregistered, Green card owners)

In Table 2, the rate of unregistered employment to total employment is given

**Table 2:** Unregistered Employment in Turkey

<b>Total employment (Million)</b> <b>(a)</b>	<b>Unregistered Employment (Million)</b> <b>(b)</b>	<b>(a/b)</b>
23.747	11.612	48.9

Resource: TSI (2007).

According do the data of 2007, the total employment in Turkey is 23.747 millions. In proportion to country's population (73 millions), registered employment rate is low when it is compared to the world %48). That new employment fields are not opened in parallel with the population growth increases both unregistered employment and unemployment.

### 6.2.1. Reasons of Unregistered Employment in Turkey

The reasons of unregistered employment show difference from country to country. Factors such as economic development of the countries, education level, social and cultural structures, psychology of taxpayer, loyalty to the government have effects on unregistered employment in different degrees. The major reasons of unregistered employment in Turkey have been explained below.

#### 6.2.1.1 Injustice in The Distribution of Tax Burden

Tax burden is one of the most important indicators which is considered in assessing a country's public finance. This indicator implies how much of the resources are taken by the government in a country's economy. (SPO,2006:7).

In Table 3 the member of OECD countries and Turkey's tax burden is given. The increasing at tax burden's main reason in developed countries is the financing of the prosperous country and the reason in developing countries is cronic public deficit (SPO,2007:3).

**Table 3: Tax Responsibility in OECD Countries (2003)**

Countries	Not Includes Social Security	Includs Social Security
OECD Average	26,8	36,3
OECD Europe	27,7	38,9
OECD America	21,1	26,1
AB 15	28,9	40,5
Turkey	25,9	32,8

Kaynak: OECD (2005), Revenu Statistics 1965-2004, Paris.

Tax burden in AB countries, increases parallel to the increase of public share in economy. Especially in order to finance the social security deficit, tax burden increased fast and (including social security payments) it reached %40s. The increasing tendency at tax burden in last years has calmed down, even in some countries tax burdens decreased (SPO,2007:4).

In Turkey, especially until the beginning of 1990 tax burden was at lower levels when we compare with OECD countries but by the beginning of 1990s it regularly increased, and its rate in the Gross Domestic Product was %25 in 1997, but it increased to %32,5 in 2003 and it is estimated in 2005 it reached %34,5 (SPO,2007:11). Tax burden is one of the most important indicator to evaluate a country's public finance. With this indicator, we can see how much of the source is taken by the country as a tax or under with other names. In Turkey when we look at the numbers it shows that the rate of money which goes from country resources to the state increases day by day.

Tax burden is high when it is compared to the world. But, tax burden is not distributed fairly between individuals, sectors and regions.

In the distribution of tax burden, a balanced distribution between direct and indirect taxes in UN-15 countries calls the attention (World Bank, 1991, 2). However; the distribution over the tax burden has changed with the participation of new countries (European Commission, 2005:6-11).

#### **6.2.1.2. Deficiency in Finding Employment Fields**

The big informal economy in Turkey means one out of every three workers in urban areas and three out of every four workers in rural areas are not enrolled in any social security institution. Consequently, few workers can get retirement, health and unemployment insurance (World Bank, 2006:2).

The rate of total employment to total population is low in Turkey. While OECD average is %64.3, EU average is 65.1; this rate in Turkey is %45.8. The unemployment rate of Turkey is high, too, when unemployment points are observed. Unemployment average of OECD countries is %6,7, EU's is 7.6 and %10.6 in Turkey (According to 2002 data, MLSS 2004b:101-102). Albeit the effective economic growth currently, finding employment and participation level to work-power in Turkey is rather low (World Bank, 2006:1).

In Turkey, %47 of the employment is in agriculture, %15 is in the industry and %38 is in the service sector. However; these rates in Europe are agriculture %12, industry %36, and services %52 successively (World Bank, 2006:17).

Turkey has represented an effective development since 2001 and this development has been supported by a series of reforms which provide to reduce inflation, to improve public expenditures, to pave way to increase foreign investments directly. Albeit the current effective economic growth, finding employment and participation level to work-power in Turkey is rather low (World Bank, 2006:1).

#### **6.2.1.3. Burdens of Financial Loads**

While tax and social security cuts on employment are the revenues for the government, they are elements of expenditure in terms of the employer. Increase of these

burdens means the increase in the expenditure of employing. Taxes and social security bonuses on labour in Turkey is quite high.

**Table 4:** Fiscal Loads on Employment in OECD Countries (%)

Turkey	42,7	Norway	29,6	Austria	35,5
Poland	42,1	Italy	35,2	Spain	33,4
Greece	39,2	Denmark	29,6	USA	11,9
England	27,1	Canada	21,5	Korea	16,2
Belgium	40,3	Switzerland	18,6	Australia	16
Portugal	26,6	Germany	35,7	Mexico	18,2
Hungary	39,9	Iceland	11,0	Japan	24,9
France	41,7	EU-15	31,6	OECD	27,7

Resource: OECD, Taxing Wages 2004–2005, February 2006.

\* The rate of taxes taken from the wages and total of employer and employee social security bonuses to work-power expenditure, year 2005

According to the Table 4, Turkey is the country where taxes and bonuses on employment are the biggest. According to OECD data, Turkey takes place on the top list in terms of the burdens for employment tax between 30 OECD countries. In other words, the most deterrent application in terms of tax and insurance bonuses to curb employment increase in the world is in Turkey.

When the OECD data in which family tax support-prevalent in OECD countries- is taken into account, it is observed that %42 of average employment cost is allocated for employment taxes (taxes taken from the wages and social security bonuses) in Turkey which is on the top list. This rate is approximately %24 in the general of OECD, %17,6 in the USA, %9 in Ireland. It takes the attention that employment taxes have reduced in the USA, Hungary, Korea, Luxemburg, and Ireland in 2002. Social security institution bonus burden feeds unemployment and informal activities (MLSS, 2004b:58, MLSS, 2006:14, Korkmaz, 2001:276).

As there are empiric studies supporting the thesis that tax burdens on employment increase the rate of unemployment, there are other studies which manifest that quality of syndicate under structure, constitutional properties in collective agreement and similar fields can be effective in the relation which is in question (Brant-Burniaux-Duval, 2001:28). However; it is useful to assert that high fiscal burdens on labour do not give way to unregistered employment alone (OECD 2004:254).

#### **6.2.1.4. Dissatisfaction of Social Security Services and Ignorance**

The quality of the services in return for social security bonus affects the individual's bonus payment. Especially dissatisfaction of health services are not seen as the equivalent of the bonuses paid. Therefore, in the comparison of utility-cost inequality are observed between the services and bonuses paid. Problems such as ownership of the institutions by the government, employment of the state officials in the institutions, lack of enough inspection for the institutions reduce the demand for social security services.

Unemployment insurance must be able to be used more commonly. For the time being, less than %4 of the unemployed workers can enjoy unemployment insurance. However, this number is %14 in Korea, between %25 and %75 in the OECD (Verghis, 2006:16).

In the press announcement of ILO (International Labour Organization) dated 5<sup>th</sup> March, 2006; prevalence of unregistered employment in Turkey was stated (ILO, 2006:1). The people who are deprived social security rights, defenceless, and who are working out of



social security network are subjected to dangers due to working environment and health conditions.

#### **6.2.1.5. Attitudes towards the Government**

The government behaves quite seriously while collecting taxes and other revenues. It imposes fines on the ones who do not fulfill their tasks. But, tax amnesties due to political incentives disappoint the honest people who fulfill their tax tasks. Along with this, the government does not pay the same attention while it is spending these taxes and revenues because the government and local administrations don't check whether the expenses that they make are effective, productive, and appropriate. Therefore, instead of the most necessary needs of the people, expenses are made in the direction of the institutions. Also, speculations in the adjudication system of the government cause the thought that the taxes collected are not used appropriately. Policies of expenditure must change, except for tax and social security services.

#### **6.2.1.6. Lack of Inspection**

The possibility of tax evaders to be inspected is rather low in Turkey (%2-3). The employers who do not fulfill their tasks about employment are aware of the fact that they will be inspected with a low possibility. In addition, though they are punished as a result of inspection they carry the hope that amnesty will come out. So lack of enough inspection and control push the individuals to unregistered employment.

It is not possible to put forward the inspection as the solution of unregistered employment. Unregistered employment implies a structure which feeds from the current economic system and which reflects closed agreement (T.R. premiership, 2006).

#### **6.2.1.7. Low education level**

For the relation between education level and unregistered working to be understood, distribution of education level in profession groups and unregistered working needs to be examined. Employment type which has low education level is observed more in agriculture and non agriculture production activities whose unregistered employment is high. The people who have high education level work in profession groups where unregistered working is low. While the people graduated from primary school or with lower education are active in agricultural profession group where unregistered working rate is the highest, %91,2 of unregistered working rate which is largely %51, %55,9 of the people graduated from university works in the profession groups of scientific and technical personnel, self-employed people, and related professions which has the lowest unregistered working rate of %7,1.

#### **6.2.1.8. Unemployment**

The employees and employers have disagreements between themselves in making informal economy into formal one (Valk-Süral, 2005:59). While the employees demand more money and more flexible working conditions, and the employers the opposite one.

Besides the disagreement between the employers and the employees, there is unemployment level of %11 in Turkey. The rate of the uneducated and unskilled people in unemployed fashion is quite high. Such people admit to work on low salary and without any social security. These conditions are more tempting instead of being unemployed.

#### **6.2.1.9. Political Indifference**

That the half of domestic income and employment is out of registration must worry the politicians. Because these both reduce tax revenues and impairs social regularity. But, this situation suits the politicians' purposes as the struggle with informal economy and unregistered employment will cause loss of votes. Additionally, unregistered employment and informal economy will consolidate the soul of enterprise in the future (Carillo-Pugno, 2004:258).

## **7. Struggle with Unregistered Employment in Turkey.**

A circular published by Ministry of Social Security and Labour and The Project of Struggle with Unregistered Employment (PSUE) went into effect in 4<sup>th</sup> October 2006 for a comprehensive struggle with unregistered employment in Turkey.

The aim of the PSUE project: support of the works to minimize the rate of unregistered employment in total economic growth, making public opinion conscious of the long term disadvantages that unregistered employment will cause.

In the scope of E-Government applications, it is shifted to e-declaration application for working life. So taking the individuals under record will be easier and available.

Only legal and administrative regulations are not enough to increase the registered activities in the economy. It mustn't be forgotten that even if the best tax regulations are prepared and they are applied in the best way, the results expected from these regulations will not be realized unless tax awareness and ethic are not developed in the society (Sarılı, 2002;49). So the volume of registered employment can be increased with the common attitudes of government and all sectors of the society.

## **8. Conclusion and Assessment**

There are various reasons for unregistered employment. While the rates of unregistered employment can be different from country to country, the reasons of unregistered employment represent difference. So there is no one recipe and solution way for the problem of unregistered employment.

While the tax burden is not heavy in Turkey, the distribution of tax burden is not fair. This unfair distribution causes taxes to stay over some certain parts of the society. The taxes must be distributed to the basement and tax rates must be pulled to a reasonable level for a fair tax distribution.

The economy of Turkey grows constantly and its population has increased. However, in employment facilities, there is not increase at the same level. This brings unemployment and unregistered employment with itself. Reduction of taxes and other burdens on production, investment, and employment will bear new employment facilities.

Social security and tax cuts on employment in Turkey take place at the top list among OECD countries. Reduction of these costs which increases the expenses of the employers will both increase employment and reduce unregistered employment.

Education level and unemployment rates are closely related with unregistered employment. It must not be forgotten that allocating more share for the education in government budget will add to the development of the country in the long term.

Increasing the quality in social security services and especially in health services, and making the society conscious of social security increase registered employment.

Efficient and enough inspection mechanism, deterrent fines are effective in preventing unregistered employment. Increase of the inspection officials and good education of them is important in this respect.

Struggle with unregistered employment must be effectively carried out in corporation with society, public administration and civil society institutions because this struggle is carried out by social agreement. Consequently, economy of the country and social life will be affected positively.

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