

Undeclared Labour in the Construction Industry

Country report - **Czech Republic** - June '06
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Contents:

A. National regulatory system relevant for construction

- A.1. Applicable legislation and liability regulations
- A.2. Industry-wide agreements and collective agreements

B. Authorities and institutions involved

C. Nature and features of undeclared work in construction

- C.1. Definition of undeclared work
- C.2. Extent of undeclared work in construction
- C.3. Different forms
- C.4. Main actors
- C.5. Reasons for undeclared work

D. Functioning of undeclared work in construction

E. Effects of undeclared work in construction

F. Measures taken

G. Good practices

Bibliographical references

A. National regulatory system relevant for construction

In brief, the status of the construction sector in the Czech economy as a whole can be characterised as follows: share of workers in construction in total employment of the economy has in the last few years been around 8.2%, and added value in construction at current prices as a proportion of total added value is around 7%. In comparison with e.g. the situation in 1995, the role of construction according to both indicators has fallen. In 1995 the share of workers in construction in total employment was 9.0%, and the proportion of added value in construction to total added value was 9.1%. The role of construction is declining, while the role of the service sector has increased.

A.1. Applicable legislation and liability regulations

The following national legislation covering employment in construction is currently in force:

- Tax regulations
 - Act No. 586/1992 on income taxes, as subsequently amended (applicable to individuals and corporations).
 - Act No. 235/2004 on value-added tax, as subsequently amended.
- Social security regulations
 - Act No. 589/1992 on social security contributions and contributions to state employment policy, as subsequently amended (covers sickness insurance, the national pension scheme, and contributions to state employment policy).
 - Act No. 592/1992 on general health insurance premiums, as subsequently amended.
- Labour law regulations
 - Act No. 65/1965, the Labour Code, as subsequently amended.
 - Act No. 435/2004 on employment, as subsequently amended.
- Health and safety at work regulations
 - Act No. 174/1968 on state supervision of safety at work, as subsequently amended.
- Special regulations for construction
 - Act No. 50/1976, the Building Code, as subsequently amended (covers the conditions for construction projects).
- Business entrepreneurship
 - Act No. 455/1991, Trade Law, as subsequently amended.
 - Act No. 513/1991, Commercial Code, as subsequently amended.

The aforementioned regulations entail obligations (tax, welfare and health insurance contributions, labour law and health and safety at work) for employees, employers and self-employed persons:

- Tax regulations (lower tax rates apply with effect from January 1, 2006)
 - Income tax (employees, self-employed persons): tax bands 12, 19, 25 and 32% of the tax base,
 - Corporation tax (business entities): 24% of the tax base.
- Social security regulations (social security contributions, contributions to state employment policy and general health insurance premiums)
 - total contribution for employees: 47.5% of wages (12.5% paid by the employee, 35% paid by the employer),
 - total contribution for self-employed persons: 47.5%, (43.1% excluding optional sickness insurance) of the assessment basis.

A.2. Industry-wide agreements and collective agreements

Collective bargaining at sector level takes place between the leading employers' association, the Association of Entrepreneurs in Building Industries in the Czech Republic, and the Trade Union of Building Workers. That collective bargaining results in a national industry-wide collective agreement. The sectoral collective agreement is extended to the entire construction sector, and therefore also applies to companies where there are no trade unions, and which are not members of an employers' association. At company level, the employer negotiates company collective agreements with union representatives, either affiliated to the Trade Union of Building Workers or independent of the major unions. In the construction sector the generally binding collective agreement applies, due to the extension and obligatory nature, to a substantially greater number of employees than company collective agreements do. Evidence of very good relations between the social partners in the construction sector is found in, amongst other things, the agreement entitled General Principles of Social Dialogue, concluded in October 2002 between the two dominant actors in the social dialogue in the sector, the Trade Union of Building Workers and the Association of Entrepreneurs in Building Industries. In that agreement, both partners declare their consensus of opinion on a number of aspects of social dialogue in the sector. They view it as "the most effective means to maintain and strengthen social conciliation and implement democratic principles on the labour market."

The generally binding collective agreement concluded between the social partners in construction also governs support for employment relationships, favoured over subcontractor relationships with bogus self-employed persons: "Employers are obliged to secure the performing of current tasks resulting from their business activities by means of their employees, who they employ for that purpose in employment relationships in accordance with the Labour Code. That does not apply to current tasks which the self-employed person arranges himself, or with the assistance of his spouse or children, or which a corporation arranges by means of its partners or members, or if the performance of current tasks by a corporation or self-employed is entrusted to another corporation or self-employed person which is obliged to secure that by means of its employees, which it employs for that purpose in employment relationships in accordance with the Labour Code. Employers may secure work in excess of their capacity, or subcontract for special supplies."

The purpose of that provision of the sectoral collective agreement is to recommend that the social partners pay attention to the abuse of subcontracting arrangements between companies for illegal employment and enterprise.

B. Authorities and institutions involved

The following national institutions are responsible for individual regulatory systems and compliance with the relevant regulations:

- Tax regulations
 - Revenue authorities (at various territorial levels): administer and record tax and deductions, control compliance with tax regulations, apply sanctions
- Social security regulations
 - Social security administrations (with offices at territorial level): implement pensions and sickness insurance benefits, including payment of benefits and control work
 - Health insurance companies: provide health insurance
- Labour law regulations, including health and safety at work regulations
 - Employment offices (at territorial levels): consultancy services, implement active and passive employment policy measures and payment of relevant welfare benefits,

issue permits to employ foreigners, control compliance with employment law and equal opportunity principles

- Labour inspectorates (at territorial levels): control compliance with collective agreements, compliance with labour law regulations and health and safety at work regulations, and compliance with wage regulations
- Cooperation in controls of the employment of foreigners
 - the Aliens Police of the Czech Republic and the customs authorities
- Administration of the law – jurisdiction
 - Courts (at territorial and higher levels): criminal law, civil law and other proceedings
- Local government administration
 - Trades licensing offices or departments: arrangements for conducting trades, controls concerning business in trade, apply penalties and other sanctions
 - Building authorities: applications for building permission, including control work and sanction measures

C. Nature and features of undeclared work in construction

C.1. Definition of undeclared work

In practice, no uniform definition of undeclared work is used in the Czech Republic. According to national legislation, it is necessary to observe a number of regulations, in line with employment status (employees, self-employment), in particular:

- the existence of a proper employment contract, including compliance with all labour law and wage regulations,
- the registration of the company in the commercial register, kept by the courts,
- the registration of self-employed persons in the register of trades kept by the trades licensing offices,
- registration with the revenue authorities and compliance with tax obligations,
- registration with social security offices and compliance with social insurance obligations,
- registration with health insurance companies and compliance with general health insurance obligations,
- other related registration or records, including compliance with the relevant obligations, at e.g. statistics authorities, employment offices, etc.

From the narrow point of view of the individual competent authorities and institutions, the criterion of declared or undeclared work is compliance or failure to comply with the regulatory measures they prescribe. Nevertheless, for the purposes of an uniform overall assessment of the character of work, the most recent generally recognised EU definition from 1998 has been adopted and applied for operational purposes, in relation to OECD and ILO definitions: “undeclared work can be defined as any paid activities that are lawful as regards their nature but not declared to the public authorities, taking into account the differences in the regulatory system between Member States”. Of course, that also means that a definition so formulated can be used in individual countries as an acceptable working definition, but in view of differences in individual countries’ regulatory systems, that entails a certain international incompatibility of the information and data acquired.

The only official national definition concerning illegal work is formulated relatively narrowly from the point of view of the *Employment Act*: “For the purposes of the Employment Act, illegal work is understood as a situation in which an individual does not work for a corporation or self-employed on the basis of a labour law relationship or other agreement (if

that does not concern the spouse or children of that individual, or a partner or member of that corporation), or where a foreigner does not work for a corporation or self-employed on the basis of a labour law relationship or other agreement (and this does not concern the same persons as in the preceding instance), or works contrary to the work permit issued, or without such permit (if a work permit is required pursuant to this Act)”.

C.2. Extent of undeclared work in construction

By way of introduction, it must be said that there are very few studies of the extent and forms of undeclared work in the Czech economy, or at least of certain forms of that, and practically none concerning the specific features of different sectors, including construction. The more reliable studies produced in the last few years include the following (in addition, a number of reports have been presented at various international conferences, especially concerning illegal work by immigrants in the Czech economy):

- *Country study on informal economy in the Czech Republic*, M. Horakova, J. Kux, 2003, as part of the Regioplan Netherlands and INREGIA Sweden study *Undeclared work in an enlarged Union*, with estimates of at least 10% of GDP and 5-6% of the labour force, and listing construction as one of the main sectors for undeclared work (without specifying further).
- *Shadow economy*, parts I, II, III, M. Fassmann, Czech-Moravian Confederation of Trade Unions 2001, 2003, 2005, with estimates according to Gutmann’s “currency-demand deposit ratio method” (approximately 16% of GDP) and Kaufman’s “electricity consumption method” (approximately 8-12% of GDP); in Czech only.
- *Illegal employment of foreigners in the Czech labour market*, A. Kroupa, M. Horakova et al., RILSA 1997, with financial support from the ILO, based on a questionnaire with approximately 50 groups of questions for experts from the Aliens Police, employment offices, revenue authorities and representatives of trade unions and employers’ associations, with related group discussions, especially concerning forms, causes, reasons and related problems, limited of course to the issue of illegal work by foreigners in the Czech economy.
- *Illegal/irregular immigrants and their economic activities in the Czech Republic* (draft report of a ongoing research project), D. Drbohlav et al., Charles University, Prague 2004.

As part of the present report, an attempt has been made at an accurate estimate of the extent of undeclared work in construction. Although the calculations can only be very approximate, the analysis conducted reveals that the extent of undeclared work in construction is considerable.

Basically two methods were used:

(i) Calculation based on the first *Czech national labour accounts* for 1998 with certain new calculations, compared with other data sources and the results of consultation (the balance of the population’s activities, estimates for illegal immigration based on data from the Aliens Police, result of controls performed jointly by employment offices, financial and other institutions, consultation with trade union bodies and employers’ associations in construction). As has already been said, reliable estimates of the extent of undeclared work cannot be naturally made: based on the sources listed only a very rough, approximate estimate of the potential extent of undeclared work in construction is possible, including work performed in the form of second jobs (moonlighting) and other forms of undeclared work, as possibly 35-50% of the extent of declared work. An estimate of the extent of illegal work by foreign workers is between 40,000 and 50,000 (compared with approximately 45,000

foreigners working legally in the sector), and the extent of undeclared work performed in various forms by Czech workers, regularly or occasionally, is evidently much greater; potentially 100,000 to 150,000 Czech workers (according to statistical company records, declared work in construction accounts for approximately 400,000 jobs). By way of illustration, with a very rough estimate of 250,000 to 350,000 persons working illegally in the Czech economy as a whole (5-7% of the labour force), the proportion of undeclared work in construction is around half that figure. Our figures on extent of undeclared work are estimates based not on one single source, but more sources have been put together. As concerns the *Czech workers* working illegally, the basis for our estimates has been the first Czech labour accounts based on principle on LFS results (signalling higher real employment in construction than officially reported by establishment surveys), completed by some other assumptions (of several experts, estimating probable part of hidden economy covered by this method). Estimates of the extent of *illegally working foreigners* were based on discussions with construction experts (trade unions and employers), surprisingly quite independently suggesting approximately the same probable extent. These estimates were confronted with the results of official controls conducted in the units concentrating particularly on selected problems of illegal work of foreigners in the whole economy (no separate data for construction available). According to our expectations the outcome of inspections indicated partly lower figures - illegally working foreigners in these units equalled 35% of legally working foreigners (in construction results are probably higher).

(ii) Method based on *national accounting data*. This primarily concerns the Eurostat pilot project “Exhaustiveness”; launched in 1998 and aimed at ascertaining how completely the economy is captured in countries’ national accounts. According to data from that project, the proportion of the shadow economy in construction accounted for around 20% of the gross added value in that sector in the Czech Republic, and alongside the trade sector, and following accommodation and catering and other personal service sectors, it was the most significant sector in terms of not covering the proportion of actual value of work in the sector. Although this concerned in essence the proportion of the shadow, grey economy in terms of the statistical capturing of work, it can be expected that undeclared work was the decisive factor. The lower proportion of the shadow, grey economy to GDP than the estimated proportion of the extent of undeclared work results from the distinctive structure of undeclared work in construction: predominantly its poorly qualified and badly paid labour force, to a considerable extent in the form of second jobs (moonlighting).

An analysis of the data acquired reveals that the greatest extent of undeclared work was in the initial period of economic transformation, in the first half of the nineties. The pre-transition period was characterised by the non-existence of the private sector. Only in the last years before transition some exceptions were officially admitted, based on special permits of local administrative bodies – for example repair of electronic equipment, dressmaker activities, smaller construction activities etc., mostly in the form of second jobs and with a negligible number of persons involved. In construction these activities were mostly connected with construction or maintenance of family houses with the help of relatives, friends, neighbours, later also using the services of people with special permits. However, quite often these activities were carried out illegally too, but no estimates exist.

In the first years of transformation there was an exaggerated emphasis on the automatic functioning of the market, relevant legislation was lacking and control mechanisms were minimal. As legislation was gradually developed and control became more effective, there was a gradual decline in the extent of undeclared work from approximately the mid-nineties

on. That trend need not of course apply in full to construction, especially in consequence of the rising number of foreigners working illegally in the 1990s.

C.3. Different forms

In construction one can meet different forms of undeclared labour: for basic or additional income, permanent or temporary/seasonal work, non-registered or under registered. It mostly depends on the actors conducting these activities. Quantification of the extent of the various forms is difficult. In one of the previous studies of CERGE in Prague (with a small sample of interviews in approximately 1000 households and the whole economy concerned) there was information on estimated shares of Czech individuals doing undeclared work often (regularly) and occasionally. According to the study 15.5 % of individuals were doing undeclared work in the form of permanent work and a large majority of 84.5 % was doing undeclared work on occasional basis only.

A basic typology of the forms of undeclared work in construction (not ranked according to the importance) can be characterised as follows:

- individuals working on their own account, for the most part repair work or small-scale plumbing and construction work for households; as a rule these are Czech citizens, directly connected to customers; payment is in cash (they perform this work as part of their main employment, and in the form of second jobs following their work in regular employment),
- self-employed persons (small traders) often working without proper accounting documents, with direct payments from customers,
- the bogus self-employed, self-employed persons working for companies, contrary to the Employment Act, as subcontractors, instead of working in regular employment,
- a pyramid of subcontractors with a single main contractor, which hire individual labourers; a clientele system, where the workers are largely employed illegally.

The extent of those activities is as a rule closely associated with economic cycles.

Construction work tends to be closely linked to booms or recessions in the economy as a whole; during boom periods with labour shortages and demand for (unskilled) construction workers, which tends to be accompanied by a rise in declared and undeclared work, while periods of recession dampen demand for work (declared and undeclared) in construction. The specific forms of undeclared work depend furthermore on whether the workers are foreigners or Czech citizens.

Although there is no hard evidence, experts confirm that undeclared labour appears in practically all branches and trades: in case of larger firms site preparation, building of complete constructions (houses, shops, factories), civil engineering, in case of medium sized companies building installation and completion too, in case of smaller firms or self-employed maintenance and smaller repairs.

a) Forms of undeclared work of foreigners.

- Foreigners working in the Czech Republic illegally (without work permits) for employers, predominantly small construction companies, for the duration of their tourist visas, or working without residence and work permits.

- Foreigners working illegally (without work permits or residence permits) for a company that is one of many subcontractors for a large construction company. The subcontractor supplies only workers and no means of production. In such a company, some foreigners are working legally and some illegally.

- Foreigners working illegally (without work permits or residence permits) for a licensed employment agency (Temporary Agency) that has authorisation to lend its own employees pursuant to the Employment Act; usually for large construction companies. As in the preceding example, some foreigners are working legally and some illegally. A commercial law relationship pursuant to the Commercial Code applies between the construction company and its subcontractor or agency, which conclude a contract for work done. In those subcontractors and agencies there are other breaches of the regulations, in addition to illegal employment. Often no employment contract is concluded between the employee and the subcontractor or agency, or workers commence work before the employment office issues work permits, or continue working after those permits have expired. Subcontractors or agencies often request a greater number of work permits for an excessive number of foreigners, who then work for other employers. Often there is failure to comply with wage regulations and regulations governing health and safety at work. Working hours are not adhered to, and the place of employment does not correspond to the work permit. Workers from Slovakia are a special case; they contribute to all three forms of illegal employment. According to bilateral agreements they don't need work permits, but are obliged to register with the appropriate employment office for the employer's registered office.

- Undeclared work by foreigners also takes the form of “quasi-business” relationships. Two laws govern the establishing and operation of business activities by foreigners, the Trade Law for small enterprise and the Commercial Code for business entities. The Trade Law is most frequently abused by foreigners. In view of its relatively liberal nature, which for unregulated trades does not impose any special restrictions on enterprises, foreigners do not ask employment offices to issue work permits, but operate as entrepreneurs. Traditionally the Vietnamese have opted for that practice in the Czech economy, and today especially Ukrainians working in the construction sector. Employers prefer rather to engage foreign entrepreneurs than to undertake the complicated administrative procedures associated with obtaining permits from employment offices to employ foreigners. A relatively large proportion of foreigners therefore use their trade licenses for quasi-business, as bogus self-employed people. Such people formally operate businesses, but in fact are in a subordinate employment relationship with another entrepreneur, as one of them does not act in his own name and on his own liability, as the Trade Law defines business activity. In operating a trade, foreigners often fail to meet their legal obligations, such as not paying tax, health insurance and social insurance contributions on behalf of the entrepreneur himself. A trade licence can in essence be obtained for any kind of activity. The trade licence office does not investigate whether the applicant has the means of production required for the performance of the activity in question. According to employment office staff this form is declining, and being replaced by employment through agencies, since the new Employment Act has come into force, prohibiting such quasi-business. The option of establishing a trade is often used by foreigners solely to legalise their residence. After meeting the general conditions for establishing a trade, which include no criminal record, a minimum age of 18, and competence to undertake legal acts, the trade licence office issues a trade licence. A trade licence can also serve foreigner as a document of the purpose of their residence, on the basis of which the Aliens Police issues a long-term residence permit for the purpose of conducting business. It is up to the foreigner whether he will indeed engage in regular business, or whether he opts for the aforementioned strategy of quasi-business, or whether the trade licence serves solely to legalise his residence, for the purpose of engaging in other activities.

- The Commercial Code is used to a far lesser extent than the Trade Law to legalise residence, or for quasi-business. An explanation can be sought in the fact that establishing a corporation

under the Commercial Code is much more costly, as business entities and cooperatives, with the exception of general commercial partnerships, must deposit an amount of some tens of thousands of crowns. But still it is occasionally used to obtain access to the labour market, or to legalise residence. To that end, the most widespread forms of business entities (limited-liability companies and general commercial partnerships or cooperatives) are used. The advantage of a limited-liability company is that a single person may found it, or that on the basis of the level of investments, the majority partner has decision-making rights over the other partners, who in the case of illegal employment may be in a subordinate relationship with regard to the majority partner. Often tens of people establish a single limited-liability company or cooperative. According to the new Employment Act, partners in a business entity who are simultaneously employees of that company or cooperative are required to have work permits to work in the Czech Republic.

b) Forms of undeclared work of local workers.

- Unemployed citizens, or persons who are otherwise economically inactive, working individually for a construction company without employment contracts; deductions and tax are not deducted from wages. Or citizens working illegally for a company that is a subcontractor for construction work, or an agency (an employment agency which has gained authorisation to lend its own employees pursuant to the Employment Act) that only supplies employees to a construction company. In a subcontractor or employment agency, only some employees are employed illegally.

- Citizens in regular employment who in their free time provide various kinds of work and services without any kind of authorisation, in return for a consideration. Compulsory deductions and tax are not deducted from their income.

- Repeated employment (more than is permitted by the Labour Code) on a fixed-term employment contract. An employment relationship for a fixed term between participants (the same employer and employee) can be arranged or extended, by means of agreement between the participants, for a period of two years at most from the day of the beginning of the employment relationship. This applies to every additional fixed-term employment relationship arranged in the period in question between those participants. Those restrictions do not however apply to cases defined by law where a fixed-term employment relationship is agreed.

- The loan of machinery with operating personnel, which was in the past covered by a provision of the Labour Code, no longer in force, concerning the temporary assigning of employees. Many construction companies still incorrectly practice the lending of employees in accordance with the now invalid legislation. Until the new Employment Act came into force, the temporary lending of employees was legally based on a provision of the Labour Code that allowed an agreement between an employer and employee on the temporary assigning of the employee to perform work for another corporation or self-employed person. That legislation did not provide sufficient protection of the rights of temporarily assigned employees, and was therefore abolished. Now, only employment agencies that have obtained permits for that activity may temporarily assign employees; in other cases this is illegal.

- “Quasi-business” (bogus entrepreneurs), this is usually understood as a situation in which one entrepreneur “employs” another entrepreneur. The former, instead of employing an employee in a labour-law relationship (on the basis of an employment contract), seeks to conclude a commercial law contract. Formally, that should therefore be a relationship between two independent entrepreneurs, but is in fact an employment relationship, in which

one party is dependent on and subordinate to the other (fixed working hours; the use of the employer's means of production, energy, raw materials or tools; work is performed solely at the employer's place of work, etc.). This is not enterprise, as the activity does not display any of the essential features of enterprise (systematic activity performed independently by the entrepreneur in his own name and on his own liability for the purpose of achieving a profit). The employer's motivation for using this system in an attempt to simplify his wage and accounting responsibilities, and above all to reduce expenses (it is not necessary to pay compulsory contributions, as in the case of an employee). Another motivation is an attempt to exclude the applicability of the Labour Code, which protects the employee far more than the aforementioned contract concluded between "entrepreneurs". This system is often confused with outsourcing: outsourcing is the entrusting of an entrepreneur's work and activities, which the entrepreneur does not wish to undertake himself (or by means of his employees) to other parties. According to a provision of the Employment Act, a corporation or self-employed person is obliged to implement the current tasks ensuing from their activities by means of their employees, which they employ to that end in labour-law relationships in accordance with the Labour Code. The law defines exemptions from that general obligation to ensure that tasks are performed by employees: the obligation does not apply in cases when a self-employed person performs current tasks himself, or with the assistance of his spouse or children, or when a corporation performs current tasks by means of its partners or members, or when a corporation or self-employed person uses temporarily assigned employees from an employment agency to perform that work.

- Other forms of illegal employment according to extensive definitions, where every instance in which the relevant laws are not observed is illegal:

- Untaxed incomes for work performed
- An employee's wage consists of the subsistence minimum and a supplement from which obligatory deductions and tax are not paid
- Failure to pay the bonuses stipulated by law; erroneous classification in wage tariffs; failure to observe working hours
- When one company lends employees to another company and makes use of the institution of business travel, with a duration in excess of one month
- After the end of regular working hours, the employee works for the same employer under an employment agency, where he has secondary employment. The aim is to reduce wage costs for overtime payments and the opportunity to exceed the limit for overtime work defined by law.

C.4. Main actors

In essence the following main groups of actors in undeclared work are closely associated with individual forms of carrying out such work (again not ranked according to their importance):

- illegal foreign workers (especially Ukrainians and Slovaks),
- regular company employees performing undeclared work as their second jobs, following their main employment (moonlighting),
- persons receiving welfare benefits (pensioners, the unemployed) performing undeclared work, often on an occasional basis, in order to increase their incomes,
- other persons not in regular employment, or receiving welfare benefits,
- self-employed persons occasionally performing at least part of their work in the form of undeclared work.

The character of work performed by those persons is in the majority of cases unskilled labour in construction and bricklaying work, frequently badly paid (that especially concerns illegal

foreigner workers and persons receiving welfare benefits), but sometimes more demanding work, such as plumbing and other skilled labour. It appears that in cases of undeclared work, it does not depend so much on the size of the companies making use of such labour. In construction, it is found not only in small units, such as small traders or small enterprises, but can also be found in large enterprises, although there is of course a difference in the forms of undeclared work used. For small units it tends to be an activity for individuals, small traders or persons working on their own account, while for larger units it tends to be cooperation with various employment agencies and subcontractors.

As far as the different customers are concerned, it depends often on the kind of person doing the undeclared work:

- illegal foreign workers are working mostly either for smaller construction firms (self-employed) or for work agencies,
- regular company employees, in the form of second jobs, may work for his/her own employer, another employer, but also for various individual clients (private households),
- persons with welfare benefits and others not economically active are mostly working for smaller firms, self-employed, households,
- self-employed persons, occasionally performing undeclared work, are mostly working for households or as subcontractors.

Regional differences in the proportion of persons regularly employed in construction are minimal, according to figures from a labour force survey (based on NUTS2) between 9,2% and 10,5% with a national average of 9,7% of total employment, and so there evidently will not be significant differences in the regional distribution of undeclared work in construction. There may however be differences in the internal structure of the main actors in undeclared work: work by illegal foreigner workers is more concentrated in large centres (Prague) and border regions, while work by persons receiving welfare benefits (unemployed people) is found in regions with high unemployment, etc.

C.5. Reasons for undeclared work

There are many reasons for undeclared work in construction, applying both to companies using that kind of work, and the actors themselves. And due to the advantages of the system of undeclared labour both for the firms and the clients, the tendency of societal “goodwill” of the population towards undeclared labour is probably continuing over time.

For the companies, the reasons may be purely administrative, but often more of an economic or practical nature. Sometimes they concern the relatively complicated and demanding regulations for founding regular companies or trades, the complicated process of obtaining work permits for foreigners, difficulties encountered in finding suitable regular employees for less attractive jobs, the opportunity to evade the relatively strict regulations of the Labour Code (dismissing employees, working hours, leave of absence, health and safety at work). Economic reasons tend to prevail, making companies more competitive – they do not pay tax, social insurance or health insurance contributions; they only pay minimum wages, etc.

For workers engaged in undeclared work, the reasons are likewise of an administrative and practical nature. Foreigners working illegally are confronted with the difficulty or impossibility of acquiring work permits. Combined with ignorance of local regulations and the situation on the labour market, undeclared labour is the simplest way of obtaining paid work. For illegally working people in general undeclared labour is an opportunity to earnings, or at least additional earnings alongside their regular wages or welfare benefits, without paying tax and social security contributions, etc.

D. Functioning of undeclared work in construction

Given the various kinds of actors on undeclared labour market in construction, the overall organisation and functioning of that market is also different. The illegal labour market for foreigners is organised quite differently from the illegal market for local workers.

a) In case of foreigners

The most common form of entering the labour market is the clientele system, by means of various legal or illegal employment agencies:

- Foreigners sometimes seek employment in cooperation with relatives, but especially through informal contacts with various agents after arriving as tourists, with tourist visas valid for 90 days at most. Those agents often make contact with individuals seeking work in the latter's country of origin. It is simpler for foreigners interested in working in the Czech Republic to contact agents in the country of origin, and pay them to arrange all administrative matters, including a promise of work. In Ukraine, that entrance service costs in the range of 600-1000 Euro. This process strengthens the foreign worker's ties to the agent, which can only be severed in the foreign country with difficulty. Leaving that relationship is associated with the loss of work and of entitlement to residence.
- In addition to securing work, the use of service of agents that arrange illegal employment, whether direct employment by a construction company, or for a subcontractor or a licensed agency, often results in the abuse of workers (the fee for mediating comprises a substantial part, around 50%, of the foreigner's wage; failure to observe health and safety standards; low-quality and unhygienic accommodation) and frequently extortion, which is facilitated by the fact that foreign workers only know their own language, and are not aware of their rights and the opportunities to exercise them.
- Czech companies are more inclined to trust subcontractors and employment agencies than individual foreign workers. The use of employment agencies or subcontractors releases a construction company from the administrative matters associated with employing foreign workers, and in the event of an inspection by the state authorities; it is the subcontractor or employment agency's duty to provide evidence of the legal employment of foreign workers working on a construction site.

The most common cases concern the work agencies or subcontractors founded by citizens of Ukraine or of other former Soviet Union countries. The agencies or subcontractors conclude contracts through personal contacts with the management of construction companies, sometimes even in the form of public competitions (both agencies and subcontractors are legally founded bodies, with at least a part of their employees working on a legal basis). The agency is legally lending its employees in accordance with the law (it is the purpose of its activity), while the subcontractor is lending them practically too, however in the form of a subcontract of some construction activity. The agency is then sending invoices for the lending of workers, the subcontractor is invoicing for the fulfilment of a contract. In both cases undeclared labour occurs, when part of the employees is working illegally or the subcontractor has only workers, and no means of production.

b) In case of local workers

Most common form is a system of subcontractors or bogus self-employed people who, instead of working in a regular employment relationship, perform various kinds of work as subcontractors.

Czech workers also enter the illegal labour market in other ways, on the basis of informal relations between citizens, with illegal employment in the form of civic assistance or small-scale construction work. Illegal ties are however often used in the form of bogus enterprise. Illegally employed workers enter the labour market under subcontracts, where a subcontractor or agency is used to implement a specific project. There is often a chain of subcontractor relationships, where the company that is last in line actually works on the project. This system is used to conceal illegal employment, and to complicate the identification of illegal workers on a construction site, and also for “tax optimisation” (a sum is paid to further subcontractors, who are only formally connected to the system and do not provide any work, which is lower than that for which the invoice is issued).

E. Effects of undeclared work in construction

The consequences of undeclared work in construction are closely associated with the reasons why companies use that form of work, and why the actors themselves use the system. The consequences for society as a whole tend to be serious, and can be briefly recapitulated as follows:

- interference with the competitiveness of construction companies or small traders,
- lower revenues for public budgets from income tax and corporation tax, value-added tax, and social insurance and health insurance contributions,
- failure to comply with regulations under the Employment Act, the Labour Code, Trade Law, Commercial Code, wage regulations and the relevant provisions of collective agreements, and therefore inadequate safeguarding of workers’ rights,
- undermining the objectives of social protection of the welfare benefits system,
- creating the idea among the public that performing undeclared work is normal, something that does not greatly bother anyone.

It emerged from research and discussions with experts that employers often breach the regulations because they can dismiss illegally employed persons at any time and have no obligation to them; they do not pay social insurance and health insurance for them, and thereby reduce their wage expenses. In the illegal employment of foreigners, a significant factor is that they are willing to work for lower wages than legally employed foreigners, and for substantially lower wages than Czech employees, and they work more hours than regular employees. According to research and discussions with experts, other motives are the fact that for illegally working foreigners in particular, accommodation and catering standards need not be observed, and that those persons cannot complain about anything, and can easily be transferred to other jobs as required. Company trade unions, especially in smaller companies, agree with employing foreigners, as they work in jobs that local workers do not want, and wages for local workers can be increased if foreigners are paid low wages.

F. Measures taken

Measures to combat undeclared work are found in the relevant labour law regulations (especially the Employment Act), and are elaborated in more detail in the National Action Plan for Employment 2004-2006 (Guideline 9), in connection with the European Employment Strategy. These measures are not sector-specific.

In addition to producing thorough analyses of the forms, causes, individual actors, extent and consequences of undeclared work, including proposals for possible solutions, measures taken focus on the following areas:

- Legislation; by simplifying and accelerating procedures to establish companies and trades; reducing corporation taxes (gradually: from e.g. 45% in 1993 to 31% in 2000-2003 and 24% at present); reducing income taxes for the individuals (in cases of the first two lowest wage bands from 15 and 20% newly to 12 and 19%, along with the possibility of common taxation of couples when this is more advantageous); planned reform of welfare contributions; regular valorisation of minimum wages (in 2000 minimum wage equalled 33% of average wage, in 2005 it was already 38% and in 2006 it is expected to achieve almost 40% of average wages in the whole economy); opportunities for unemployed people to work while receiving unemployment benefit, to a level of 50% of regular working hours or half the minimum wage.
- Restrictive measures; inspections in companies and at the workplace by employment offices and labour inspectorates, in collaboration with revenue authorities, the Aliens Police, etc.; the introduction of financial penalties levied by employment offices for undeclared work (up to a level of CZK 2.000.000 – more than EUR 70.000 – for companies, and CZK 10.000 – EUR 350 – for individuals working illegally, with a fine of up to CZK 5.000 for individuals who refuse to provide evidence of their identity, or other documents requested), foreigners who do not submit their work permits will be expelled from the country, and unemployed persons will be taken off the register of job seekers and forfeit unemployment benefit. Overall, however, the system of penalties appears to be largely ineffective, as in practice fines imposed on companies are very low, more symbolic in nature, and for individual persons working illegally are practically impossible to recover.
- Education and raising awareness; by attempts to establish a general awareness of the fact that working illegally is not normal (articles in the national press, speeches by politicians at central and regional level, provisions in collective bargaining, the creation of a corresponding atmosphere in companies, etc.).

G. Good practices

As various kinds of individuals operate on the market for undeclared work, and for all kinds of reasons, it is difficult to anticipate any specific and generally positive measures. According to the nature of undeclared work, and on the basis of experience in combating undeclared work, the emphasis in the Czech Republic is more on a combination of diverse measures aimed at individual aspects. It often happens of course that well-meant measures may yield contradictory results. For instance: a measure against undeclared work by the unemployed, a new provision in the Employment Act which allows unemployed people to work up to 50 % of regular working hours, or for up to half the minimum wage, while retaining unemployment benefits. It was anticipated that the measure would legalise any illegal work by unemployed people (in the form of normal employment contracts, or regular enterprise). In practice it has often been the case that an unemployed person who was formerly working illegally (with an element of fear concerning potential inspections and penalties) has continued working, some times full time, still in the form of undeclared work, while receiving full unemployment benefits (in many cases without any fear, due to the difficulties of controlling compliance with permitted working hours or earnings).

To improve the control of possible illegal work by unemployed people, an experiment is currently underway in three selected districts, in which, as in a number of EU member countries, payment for work is not in the form of money, but special vouchers. Companies buy the vouchers from a specialised company and use them to pay unemployed people for their work; the employment offices broker work between companies and individual unemployed people, and also repurchase the vouchers from the unemployed at their full value. From those payments in the form of vouchers, unemployed people do not pay any fees

to the state (insurance, tax), and may only earn a limited amount in that form (about 40% of the minimum wage), while receiving full unemployment benefits. Although that system does not yield any direct revenues for the state, it significantly improves the system of controlling potential illegal work by unemployed people. According to an assessment, it is anticipated that this will be introduced nationwide next year; as it concerns essentially unskilled manual labour, it is anticipated that the system could be applied to construction as well.

At present, the following can be regarded as generally successful measures, especially in larger companies: agreements between social partners on illegal work and collective bargaining to combat unfair competition; the existing register of prices for construction work and materials that companies use; control work by employment offices, labour inspectorates, revenue authorities and the Aliens Police, aimed in particular at illegal work by foreigners; and inspections carried out in cooperation with trade unions of compliance with health and safety at work regulations.

Under the circumstances of undeclared work in the Czech Republic the activities of the established special Interdepartmental Body for Control of Illegal Employment of Foreigners proved very useful too (consisting of representatives of Ministry of Labour and Social Affairs, Ministry of Interior, Ministry of Industry and Trade and of Ministry of Finance), coordinating the respective activities of these ministries and their organs.

This Interdepartmental Body concentrates at the same time at the fulfilment of tasks of the “Action Plan for Combating the Illegal Migration”, adopted by the Government in 2004. The Action Plan includes a whole series of concrete tasks like the expansion of the competence of custom authorities and improvement of the performance in inspections of illegal employment and business. The aim is to find and implement measures that would minimise illegal migration on the territory of the Czech Republic and thus in its consequences contribute also to the reduction of undeclared work of foreigners.

As most measures announced in the Action Plan were recently introduced it is still rather early to assess the concrete effects.

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