

The Hidden Economy in Bulgaria: 2011-2012

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Economic Program*



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Macroeconomic Overview

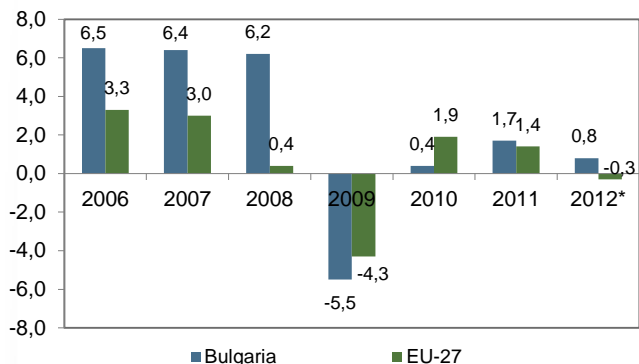
Main Economic Trends

Overview

- ❑ Bulgaria is one of the 24 countries that **improves its competitiveness** in the last two years
- ❑ Yet, it is **still one of the least competitive economies** from the 59 countries ranked in the IMD's 2012 World Competitiveness Yearbook report
- ❑ Main positive competitiveness boosting factors are **Bulgaria's fiscal stability and the low labor and productivity costs**
- ❑ Main concerns are related to **the deep structural problems of the Bulgarian labor market, corrupt management practices and weak institutional framework in the country**

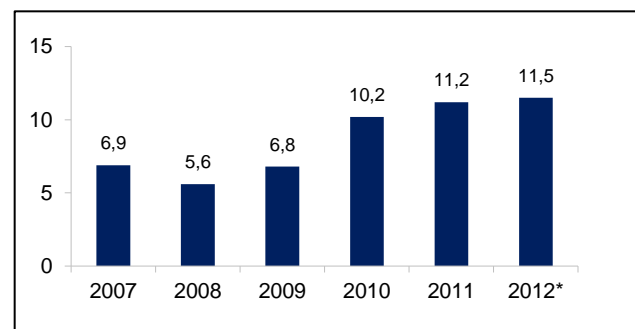
Main Economic Trends (cont.)

Figure 1: Real GDP Growth - BG vs. EU-27 (% growth)



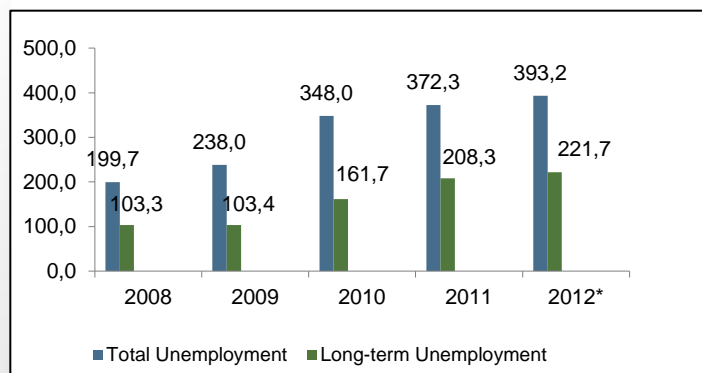
Note: * projected
Source: Eurostat.

Figure 2: Rate of Unemployment (%)



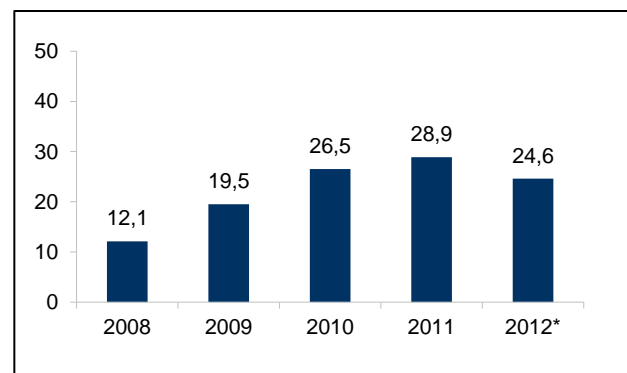
Note: * as of Q3 2012
Source: NSI.

Figure 3: Share of Long-term Unemployment (in '000 ppl)



Note: * projected
Source: NSI.

Figure 4: Share of Youth Unemployment (%)



Note: * as of Q3 2012
Source: NSI.

Hidden Economy Index 2012: Components and Dynamics

Hidden Economy Index 2012: Components and Dynamics

- 1) The size of the hidden economy summarizes the subjective perceptions of business representatives of the scope of hidden economy in the country in general, as well as in their respective sectors
- 2) Hidden employment captures the practice of hiring workers without formal employment contracts or under contracts with underreported remuneration (i.e. envelope wages).
- 3) Hidden turnover includes the incidence of various practices of concealing turnover in the respective industry or sector
- 4) Hidden redistribution encompasses the practice of tax, customs and excise duty evasion or non-payment, as well as the existence of VAT fraud schemes

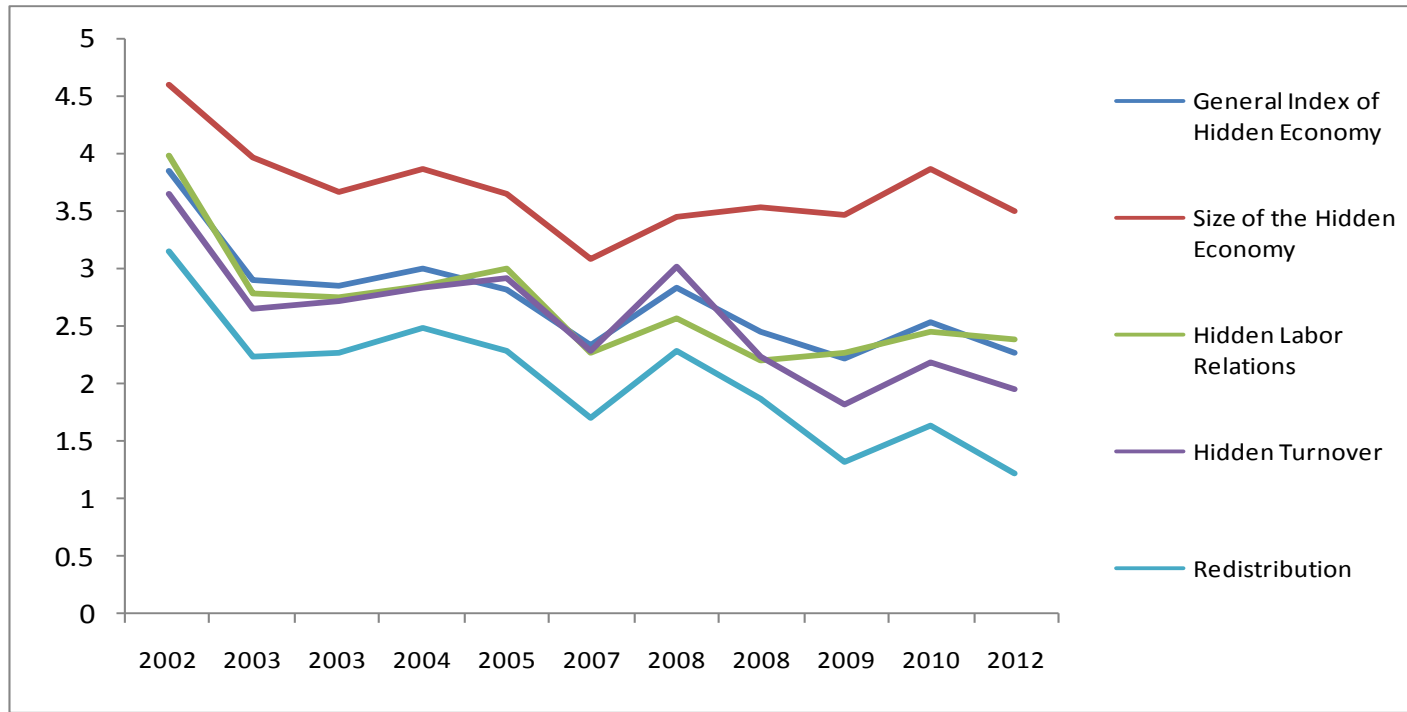
Hidden Economy Index 2012 - Main Findings

Decreasing Trends

- Both the 2012 Hidden Economy Index for the businesses and the Index on Unreported Economic Activity of the population display decreasing trends.

Hidden Economy Index 2012 - Main Findings (cont.)

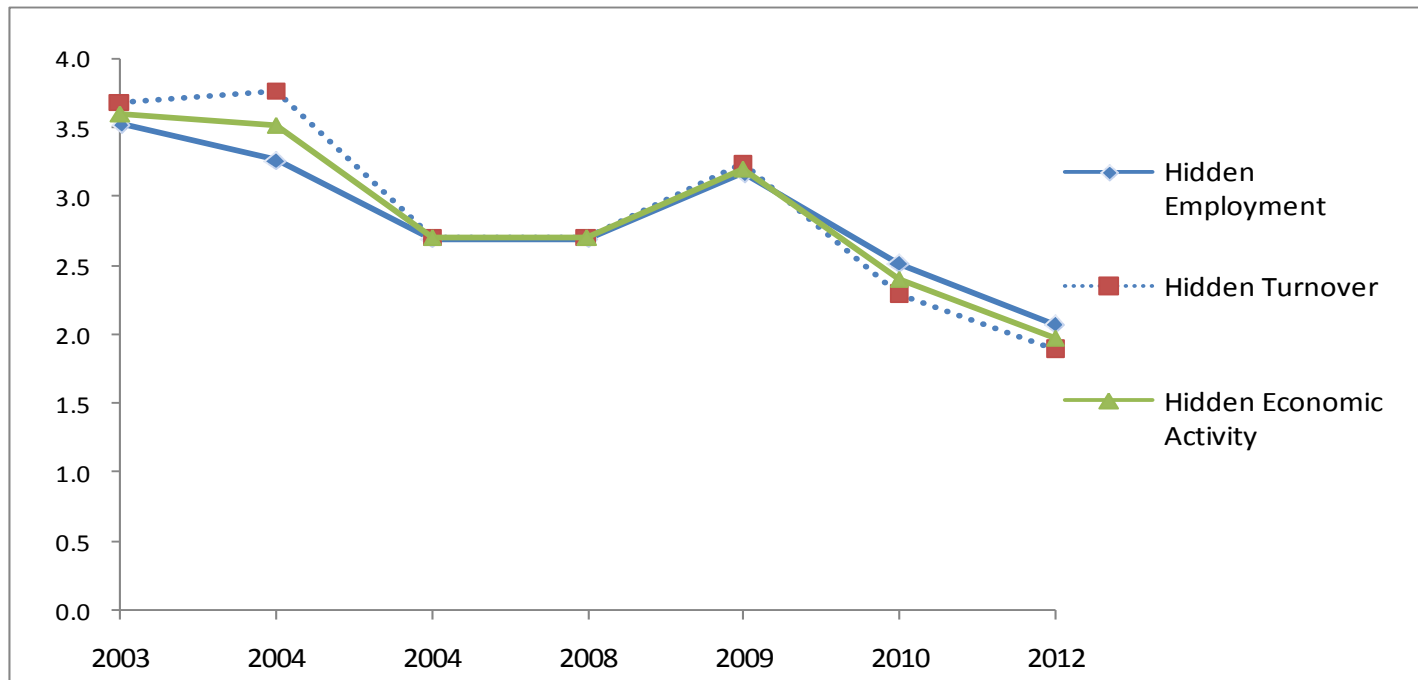
Figure 5: Hidden Economy Index 2002-2012



Source: Vitosha Research, CSD, Hidden Economy Survey on the Business

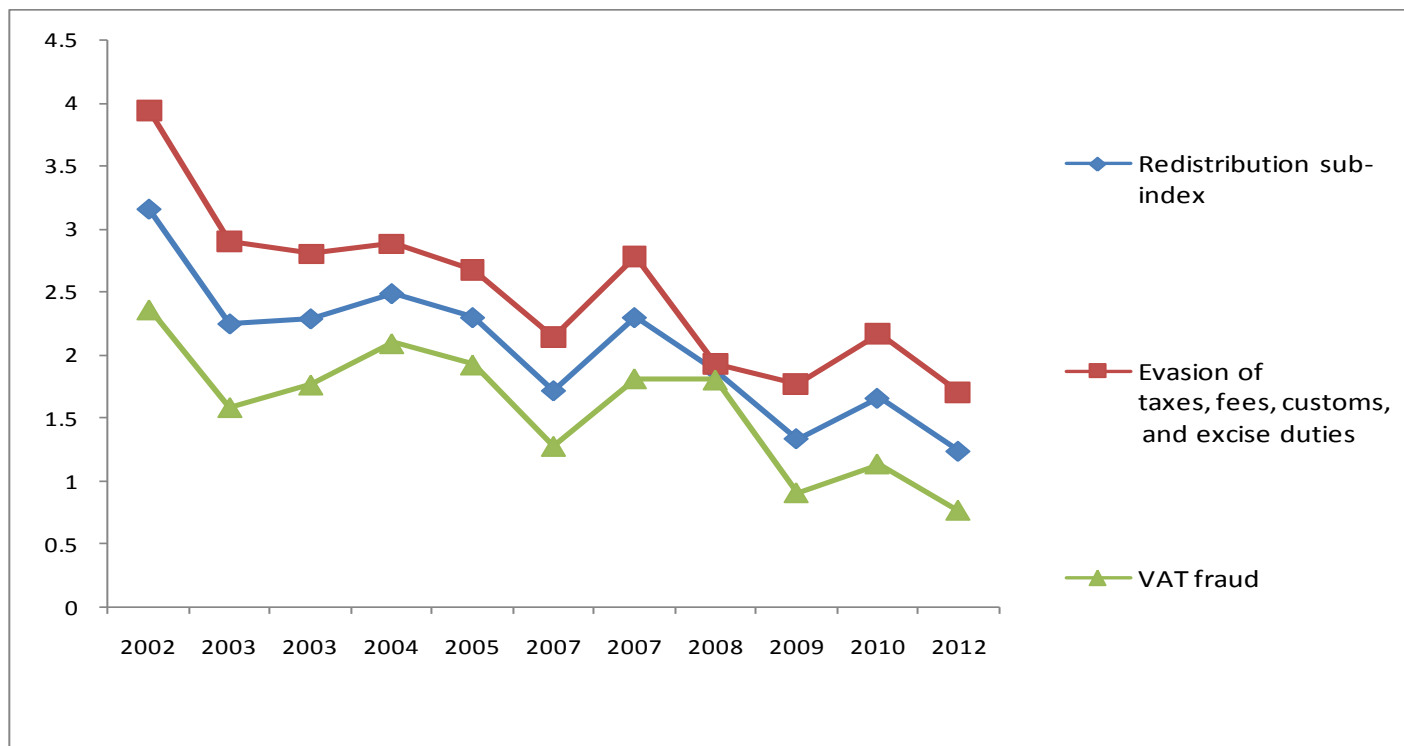
Hidden Economy Index 2012 - Main Findings (cont.)

Figure 6: Unreported Economic Activity of the Population 2003-2012



Tax Evasion and Avoidance of Fees, Customs, and Excise Duties

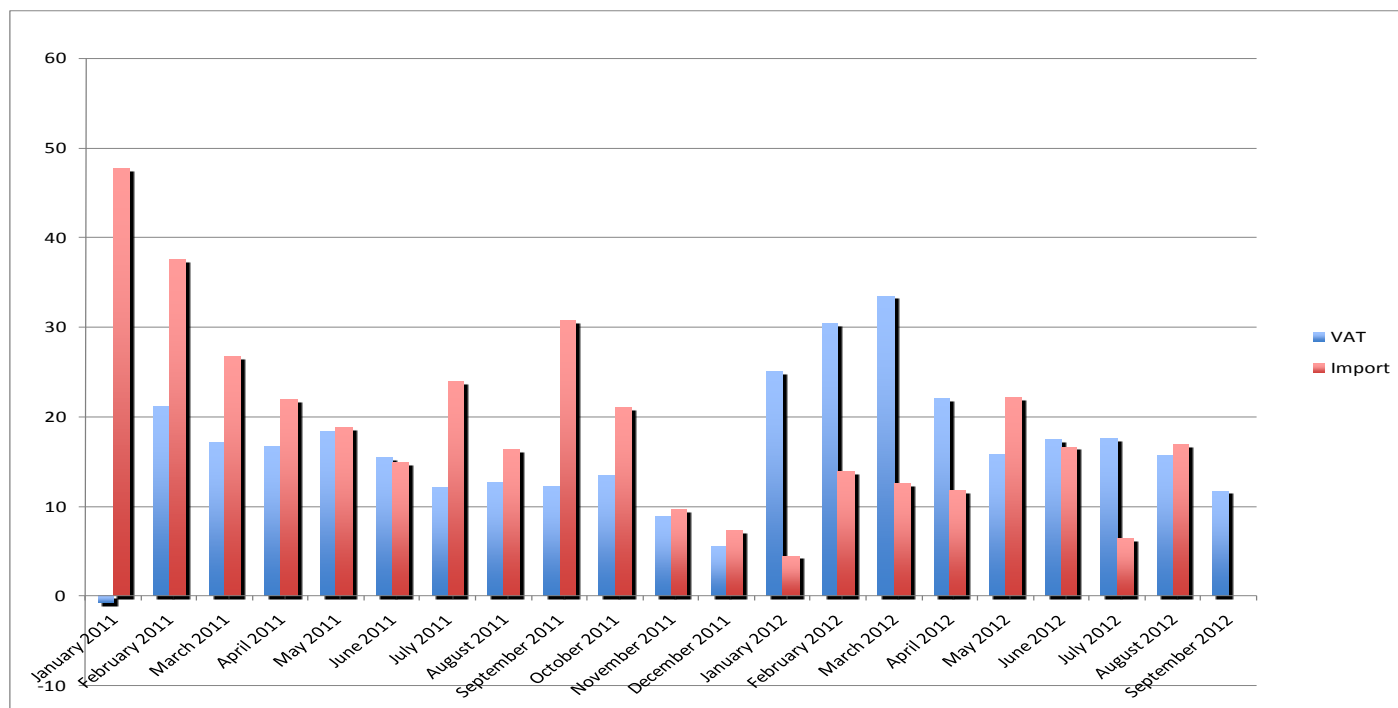
Figure 7: Dynamics of Sub-index Redistribution



Source: Vitosha Research, CSD, Hidden Economy Survey on the Business

Monthly Cumulative VAT Revenue and Import Growth (y-o-y, %)

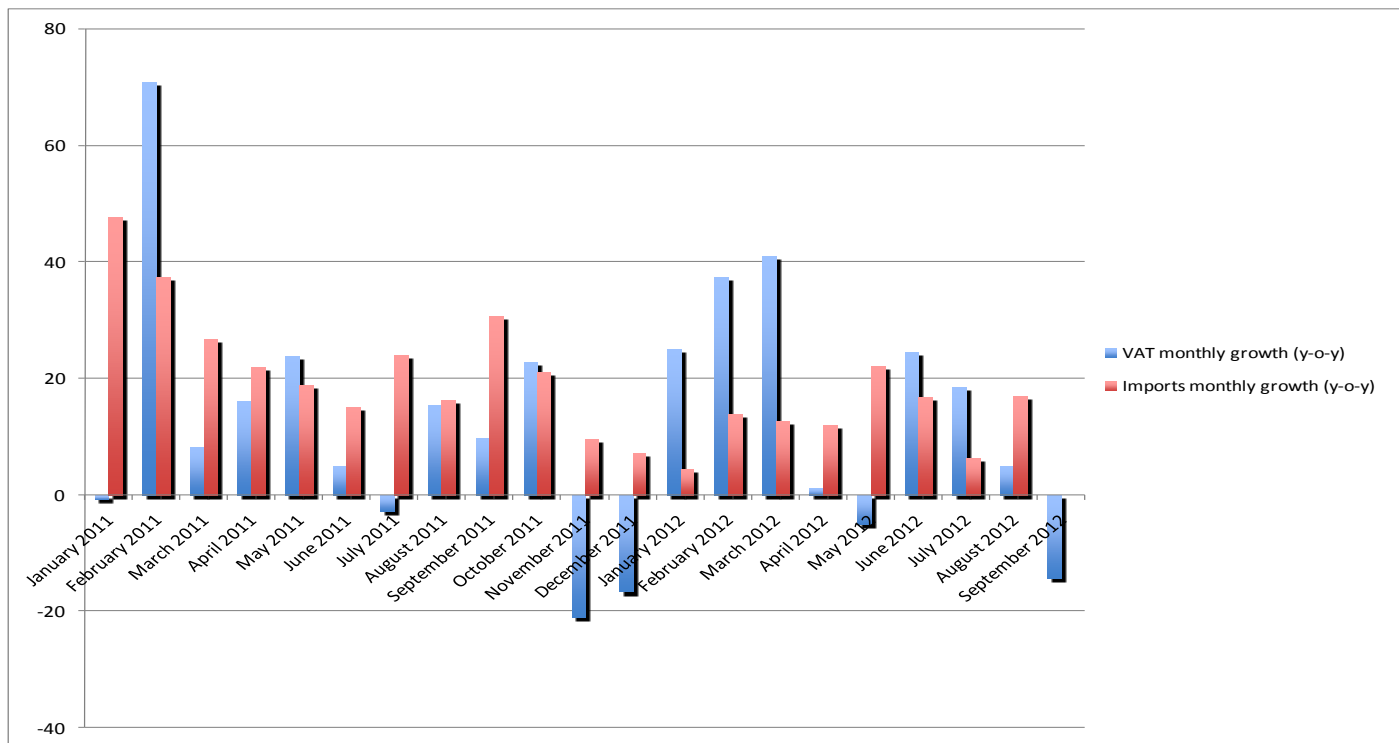
Figure 8: Monthly Cumulative VAT Revenue and Import Growth (y-o-y, %)



Source: CSD based on data from the Ministry of Finance and BNB

Monthly VAT Revenue and Import Growth (m-o-m, %)

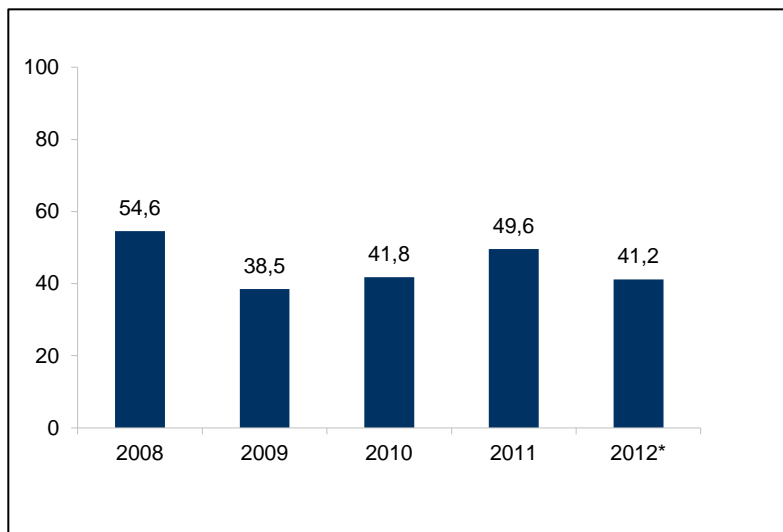
Figure 9: Monthly Cumulative VAT Revenue and Import Growth (y-o-y, %)



Source: CSD based on data from the Ministry of Finance and BNB

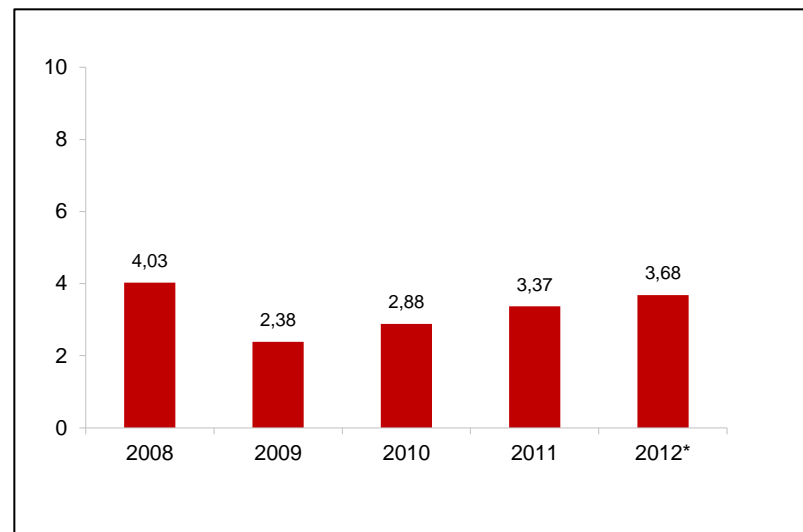
Total Volume Imports vs. Import VAT (2008-2012)

Figure 10: Total Volume Imports 2008-2012 (BGN bn)



Note: * projected
Source: BNB

Figure 11: Import VAT 2008-2012 (BGN bn)



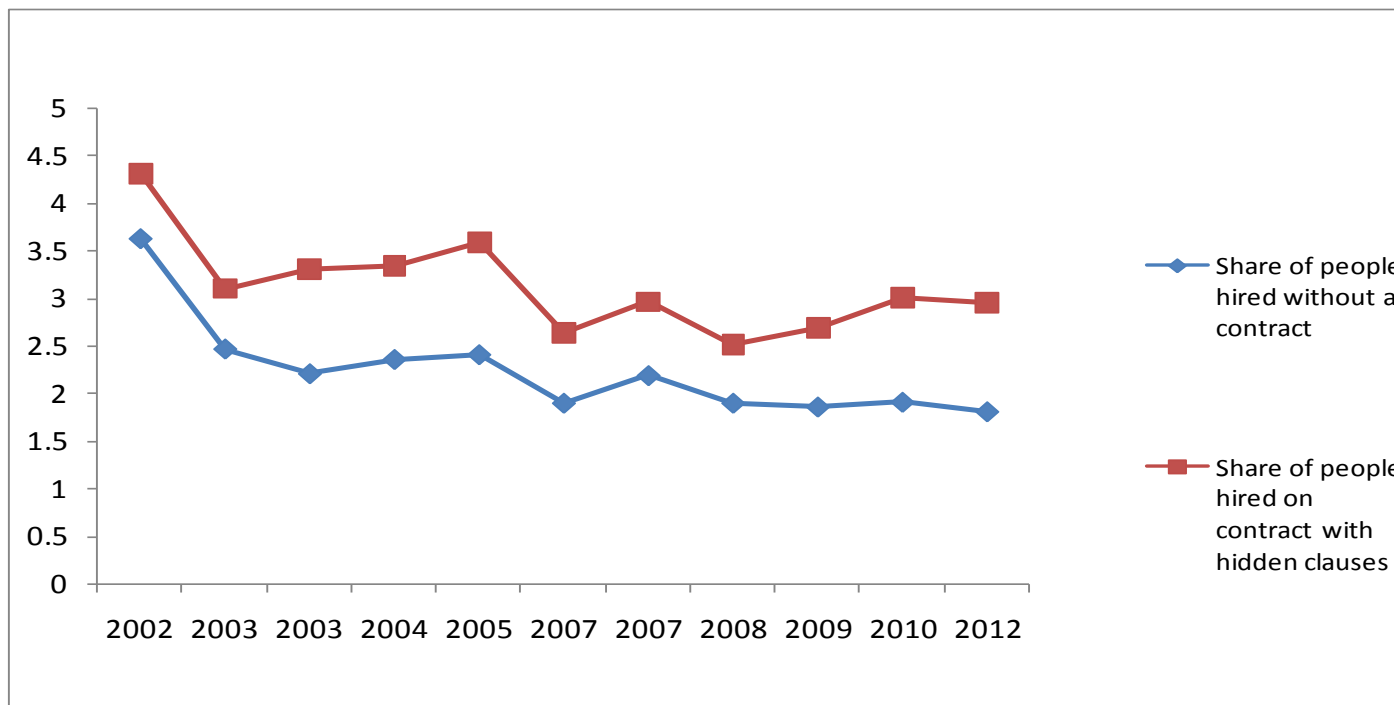
Note: * projected
Source: Customs Agency

Hidden Employment

- Hidden employment has decreased in Bulgaria during the period between 2010 and 2012 due possibly to businesses' initial reaction counteracting the effects of the crisis and laying off employees with no formal contracts which coupled with the lack of labor force re-entry after the end of the recession transferred into productivity rise and in turn temporary reduction of labor costs
- The practice of hiring of workers with no labor contract flattened out and saw little change downwards from 2010 to 2012 while instances of employment under a contract with hidden clauses (envelope wages) have also been on the decrease since 2009
- In the analyzed period, 10% of the population reported having received remuneration higher than the one stated in their contract with the primary employer
- The tendency to underreport actual remuneration continues to be pervasive, having important negative implications for the social security system.

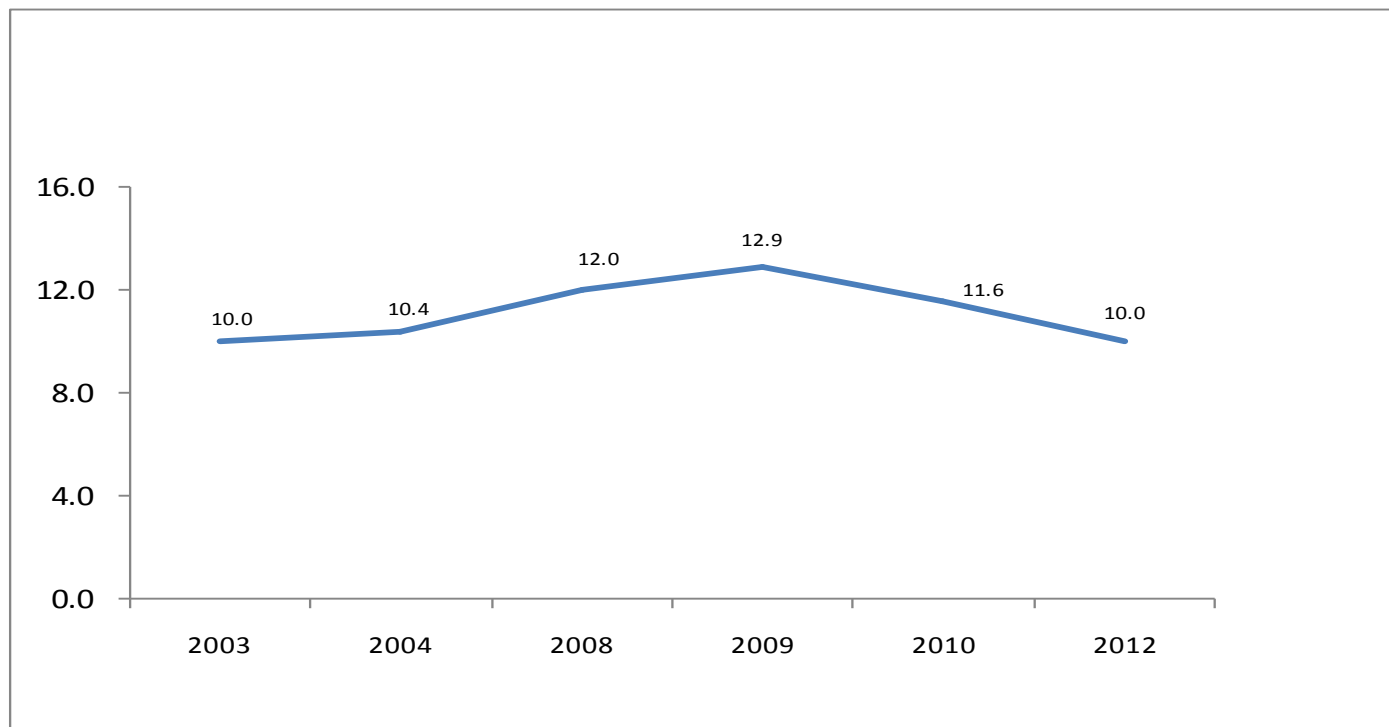
Hidden Employment (cont.)

Figure 12: Dynamics of Indexes “Hired without Contract” and “With Contract with Hidden Clauses”



Hidden Employment (cont.)

Figure 13: Hidden Contract Activities Index



Source: Vitosha Research, CSD, Hidden Economy Survey on the Population

Hidden Employment (cont.)

Table 1: Base Amount for Payment of Social Security Contributions under Primary Employment 2003-2012 (%)

Type	2003	2004	2008	2009	2010	2012
The minimum social security threshold, although sum of my remuneration is higher	12.1	13.4	13.5	12.9	10.3	9.0
The minimum social security threshold, which is what I am actually paid	10.3	14.3	9.5	12.6	5.9	7.0
The amount stated in my contract even though the total sum of my remuneration is higher	6.7	8.3	15.0	15.5	8.4	13.0
The amount stated in my contract, which is what I am actually getting paid	68.3	63.4	61.8	56.2	67.0	67.0
Other	2.6	0.6	0.3	2.8	1.5	4.0
Base	348	314	378	395	466	420

Table 2: Share of Employed under no Contract 2003 - 2012 (%)

Type	2003	2004	2008	2009	2010	2012
Without labor contract- primary employment	6.0	5.9	5.6	5.9	3.4	3.0
Without labor contract- secondary employment	77.4	59.1	51.5	51.0	38.1	29.0

Countering the Hidden Economy in Bulgaria: How Efficient Are Regulatory Agencies

Assessment of the Report Capacities of Regulatory Agencies

- National Revenue Agency (NRA)
- Chief Labor Inspectorate (CLI)
- Bulgarian Food Safety Agency (BFSA)
- Executive Forest Agency (EFA)
- National Construction Control Department (NCCD)
- Bulgarian Drug Agency
- Regional Health Inspectorates
- Regional Inspectorates on the Environment

Assessment of the Report Capacities of Regulatory Agencies (cont.)

Observations, conclusions, recommendations:

- Not all regulatory agencies have built up adequate basic public accountability mechanisms, such as publishing an annual activity report
- None of the agencies provide a comprehensive efficiency and impact analysis of its work
- NRA have started reporting on some impact indicators
- Certain elements need to be present in order for visibility and quality control to be assured. Some of these elements include:
 - details about staff, budget, type of governance;
 - watchdog function
 - report on the service of information center, including fraud signals by citizens;
 - actions taken as a result of citizens' signals and complaints related to informal/not allowed activities
 - report on auditing revisions and results of specific regulatory actions;

Policy Actions on Hidden Economy - Recent Developments and Recommendations

Policy Actions on Hidden Economy - Intended Actions

- **Goals set up by European Commission:**

- National level
- EU level
- International level

- **Reforms envisaged by Bulgarian government (Budget 2013)**

- Customs Agency will continue monitoring the excise goods storage and measuring devices
- Rates of the direct taxes will be kept unchanged, which together with increased control will stimulate the entry into official economy

Policy Actions on Hidden Economy - Recommendations

As suggested by CSD before, the use of 'carrots' rather than 'sticks' could serve as the main vehicle for improving the long-term prospects in the fight against the hidden economy.

Successful measures to reduce the level of hidden economy may include:

- indicators across government regulatory agencies
- tackling corruption through the introduction of e-services in administration
- speeding-up VAT refunds and reducing control checks on law-abiding companies
- administrative reform to speed-up payments on European programs
- better legal framework on late payments and business-to-business private debt
- special focus on improving legislature in terms of filing for bankruptcy in a retroactive manner
- promoting free enterprise and competition through improving the enforcement of the anti-monopoly legislation.

Thank You!

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