

Chapter 3

The Concept of the Survey of Businesses and Entrepreneurs Operating Informally

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3.1 Aim and Content of the Survey

The principal aim of the survey of businesses and entrepreneurs operating informally in Serbia is to assess the various forms of the shadow economy, as well as to analyse the forms of the shadow economy according to the relevant characteristics of business entities. In addition, the survey provides insight into the causes and motives of businesses operating in the shadow economy, which is important when drafting recommendations for shifting businesses from the shadow to the formal economy. The sample consisted of 1,251 business entities (businesses and entrepreneurs), and the survey was carried out from 16 to 22 October 2012 throughout Serbia.

This survey has, for the very first time, made it possible to explore the shadow economy in Serbia from the point of view of businesses, as all previous research has been based on household surveys (Krstić et al. 1998, 2001).¹ Research on employment in the shadow economy has recently been conducted in many countries (EC 2007) in addition to standard and regular Labour Force Surveys, but similar studies on the informal operation of businesses have been relatively rare, as will be discussed in greater detail in Chap. 6. This is due to the substantial risk that business owners/managers will refuse to take part in such a survey, or, when they do take part, will provide misleading answers to questions regarding their involvement in the various forms of the informal economy such as shadow employment (evasion of wage tax and social security contributions); shadow trading (evasion of value added tax); and evasion of other taxes, customs duties, and the like. This concern is also present when surveying the general population, but seems to be less pronounced.

¹ The surveys were carried out in 1997 and 2002, respectively.

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This is borne out by the results of this study, which show that activities in the shadow economy are more acceptable where individuals rather than legal entities engage in them: legal entities are thus less likely to report such activities in interviews than individuals. Similar results were obtained in a Eurobarometer survey covering 26,755 people aged 15 and over in 27 EU member states, where undeclared work by individuals for private households is deemed more acceptable than undeclared work by businesses (EC 2007).

Notwithstanding the risks inherent in such measurement, the survey of businesses and entrepreneurs operating in the shadow economy in Serbia was successfully carried out on the planned sample, with a large percentage of respondents answering nearly all the questions posed in the questionnaire.

Most of the respondents were either owners of business entities or entrepreneurs. The data were collected using face-to-face interviews.

To reduce the impact of the concealment of undeclared work on the results of the survey, the content of the questions and their wording and order in the questionnaire, as well as the approach employed by the interviewers, were tested in a pilot study² and were subsequently adjusted so as to affect respondent bias as little as possible. Various techniques were used that had in previous research shown their effectiveness in eliciting answers that were as honest as possible (e.g., Gerxhani 2007; Kazemier and van Eck 1992; Hanousek and Palda 2004; Krstić et al. 1998). This entails, among other things, gradually introducing respondents to the most sensitive questions, which will usually be posed after the less sensitive ones. The title of the survey (Survey on Conditions for Doing Business in Serbia) was carefully worded so as not to be perceived negatively by the potential respondents i.e., representatives of businesses.

In addition to questions relating to the participation of the surveyed businesses in particular forms of the shadow economy, questions were also asked regarding the subjective attitudes of business owners/managers to the participation of other businesses from the same sector in these activities. This approach has been described as a method that yields more honest responses (Gerxhani 2007) and was used in the studies carried out by Hanousek and Palda (2004), Sauka (2008), and Putninš and Sauka (2011). For the most significant forms of the shadow economy, the same questions were posed to business owners/managers regarding the participation of their own business in the shadow economy and their perception of the participation of other businesses from the same sector in these activities. Sauka (2008) found that, although the questions were posed indirectly, owner/manager responses could be applicable to their own businesses. In this study we assumed that data obtained on the basis of biased owner/manager responses regarding the participation of their own businesses in informal operations could be considered the lower limit of the extent of the shadow economy, while the data obtained on the basis of their subjective perceptions on the participation of other businesses from the same sector could be considered the upper limit.

² The pilot study encompassed ten businesses and ten entrepreneurs.

The questionnaire was made up of multiple modules. The first module was devoted to general information about the business (type, size, ownership, year of incorporation, sector of activity, turnover, etc.). The second module was designed to capture data on the activities of each business, starting from less sensitive questions and ending with those dealing with cash payments. The next set of questions related to the position of the business in the market, relative to its competitors. In this part of the questionnaire the business owner/manager was expected to present his or her own subjective view of the participation of other businesses from the same sector of economic activity in the shadow economy (trading, employment, and the like) and the ‘justification’ of informal operation (individuals vs. legal entities). The last part of this section contained questions that the pilot survey revealed as the most sensitive and the least likely to be answered by respondents. These questions dealt with informal employment (whether any workers were employed in this manner, and, if so, what their number and wages were). The third part of the questionnaire related to the causes of informal operation and the motives of participants in the shadow economy, while the fourth part dealt with the abilities of tax and inspection authorities. These were followed by a section relating to remittances from abroad received through both formal and informal channels by the households of the entrepreneurs interviewed. The final section of the questionnaire covered proposals to develop policies leading to a reduction in informal operations.

3.2 Research Methodology

3.2.1 Definition of ‘Shadow Economy’ Used in the Survey

Although the subject of this survey was the participation of businesses and entrepreneurs in the shadow economy, the term ‘informal operation’ was used rather than the expression ‘shadow economy’. Where respondents asked for clarification of this term, they were shown a card containing the following definition: “Informal operation is operation that is not fully in compliance with particular laws and regulations governing the operation of businesses, or is not fully governed by law.” This definition is rather broad and general in scope so as not to overly discourage respondents from providing answers that are as honest as possible. It corresponds to the definition used in the macro assessment of the shadow economy in Serbia (see Chap. 5), which states that the shadow economy comprises all market-based legal production activities that are deliberately concealed from public authorities for one or more reasons: to evade payment of income, value added, or other taxes; to evade payment of social security contributions; to evade certain legal labour market standards, such as minimum wages, maximum working hours, safety standards, etc.; and to evade certain administrative procedures, such as completing statistical questionnaires or administrative forms (Schneider et al. 2010).

We need to underline that the survey encompassed only formally registered businesses and entrepreneurs, while unregistered companies and/or small privately owned businesses not formally incorporated as legal entities were not covered. In other words, the survey encompassed only a portion of businesses in the shadow economy, the portion involving businesses operating in the formal sector (registered businesses). Shadow economy practices by businesses in the informal sector (unregistered businesses and/or small privately owned businesses not formally incorporated as legal entities) and in households were not examined. It should be borne in mind that estimates of informal employment prepared by the ILO (2011) for nearly all of the world's countries show that employment in unregistered businesses exceeds informal employment in registered businesses and households.

The definition of the shadow economy used in this study is based on the concept of activities that may be declared or undeclared (with tax authorities and other government bodies), rather than on the concept of declared or undeclared businesses or jobs. The first definition has become predominant in Europe and other developed countries as it includes those forms of the shadow economy inherent to a larger degree in developed economies, such as the under-reporting of income by self-employed people and formal businesses, or the payment of a portion of wages in cash (so-called 'envelope wages') that are not covered by the business-based or job-based definition, since the worker is in a formal job and the work takes place in a registered business (Williams et al. 2008).

The shadow economy can be divided into two parts. The first part involves undeclared employment, where entrepreneurs or businesses do not report their employees or declare only a portion of their wages in an attempt to evade or reduce the tax burden (informal employment). These activities are at their most common in the sectors of construction, agriculture, and services performed for households. Another part of the shadow economy entails the underreporting of income, which is most frequent in small shops owned by entrepreneurs that charge in cash and in businesses trading in cash without paying taxes. Schneider (2011) estimated that in Turkey, Spain, Italy, Germany, and Poland the first part accounted for on average two-thirds of the total shadow economy and the second part for the other third.

Taking this concept as the starting point, both of these aspects of business participation in the shadow economy were examined. Business owners/managers were posed questions about the two most important forms of the shadow economy present at their firm: informal employment and evasion of value-added tax i.e., transactions made in cash. The following groups of questions were designed to capture this information:

- Is informal employment present at the company—the most important types of such employment being employing workers without a formal contract, i.e., undeclared employees, and employing workers with a contract but declaring only a portion of their wage? What is the number of such employees? How much do they earn?
- Are payments made through bank accounts, or are payments made partly in cash? What is the frequency of such payments? What is the estimated share of

cash payments in the total? What are the other characteristics of payments made in cash?

In addition to these questions (deemed to be the most important) other forms of the shadow economy were examined by looking at the subjective views of the respondents regarding participation in the shadow economy by other businesses in the same sector of economic activity. The practices analysed included evading property tax or customs duty, and infringement of individual laws and regulations governing business operations.

The percentage of answers to questions posed in the survey was very high, ranging from 92 to 98 %. An exception was the question regarding the number of informally employed workers and their wages, with between 57 and 77 % answering.

3.2.2 Sample

The survey was carried out on a single-stage stratified sample of business entities. The entities were selected from a list of business and entrepreneurs registered with the Business Registries Agency and classified by stratum. The stratification was based on:

- Region: Šumadija and Western Serbia; Southern and Eastern Serbia; Vojvodina.
- Size of entity: up to 4 employees; between 5 and 19 employees; between 20 and 49 employees; between 50 and 249 employees; more than 250 employees.
- Sector of economic activity: agriculture; manufacturing; construction; trade; transportation; catering; other services.

The total sample was allocated by stratum in proportion to the size of each stratum in the initial sample. A simple random sample was used, without replacement by stratum. The sample is representative at the level of Serbia and by stratum (size of entity, sector of economic activity, and region).

3.3 Basic Information on the Business Entities Surveyed

A total of 606 businesses and 645 entrepreneurs were surveyed and the results were presented after weighting by stratum to make the sample representative at the level of Serbia and by stratum.

Most of the respondents were business owners (82 % of all businesses surveyed), with far fewer managing directors (13 %) or chief financial officers (6 %). The sample made it possible to survey business entities of varying sizes. The final sample contained 83 % companies with a few workers (i.e., up to four employees), 13 % with slightly more employees (5–20), while larger companies were less

Table 3.1 Main characteristics of the business entities surveyed (%)

Characteristics of business entities	% of business entities surveyed
<i>Number of employees</i>	
Up to 4	83.3
5–19	13.2
20 or more	3.5
<i>Ownership structure</i>	
Private	97.0
Socially owned	1.9
State	0.4
Other	0.6
<i>VAT payer</i>	
Yes	56.0
No	44.0

Source: Own calculations. Survey on Conditions for Doing Business in Serbia, FREN, 2012

represented (Table 3.1). Just as expected, entrepreneurs were to a greater extent micro-enterprises with fewer than five workers (89 % of all entrepreneurs), since they almost never employ more than 20 workers. According to ownership structure, 91 % of all businesses and nearly 100 % of all entrepreneurs were privately owned (97 % of the total sample), while their equity was nearly always of domestic origin (in 98 % of all cases).

The sample was constructed taking into account the sector of the business entities' economic activity. Most entities represented were engaged in wholesale and retail trade or auto repair (30 %) or other services (26 %) such as: information and communications; financial and insurance services; real estate; public administration; scientific and technical activities; administration; education; healthcare and social security; and other services. These were followed by manufacturing (17 %), construction (9 %), transportation (10 %), catering (7 %) and agriculture (2 %).

Around half of all business entities (56 %) were VAT payers: 83 % of all businesses and 45 % of all entrepreneurs.

Respondents estimated that only 24 % of all businesses and 46 % of entrepreneurs saw their sales increase in 2011 relative to 2010, while all other business entities reported a decline in sales.

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