

Undeclared Labour in the Construction Industry

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National position on undeclared work.

The interest in the prevention of undeclared labour stems from the nineties when there was a deep recession; concern about the negative effects of the informal economy on society was a starting point for several governmental Action Programmes for the prevention of black economy and economic crime. The first programme (in 1996) included measures to increase surveillance and sanctions, as well as research and information campaigns. The focus was on preventative measures and reduction of opportunities to commit economic crimes. Aim was to minimise damages economic crimes can cause and to prevent harmful practices that have a negative effect on public financing. The undeclared economy was defined in fiscal terms.

At first glance Finland therefore belongs to the countries with a rather narrow legislative definition applied to undeclared labour. There was and is a first limitation to “any work not declared to public authorities in order to avoid paying taxes and fees related to this activity”. The consequence is that taxes and social security fees not paid to public authorities build the main condition for work to be qualified as illegal. Illegal economic activities not directly related to labour, for instance double billing or undeclared income from foreign investment are also belonging to the black economy. Non-compliance with the generally binding collective agreements is unlawful but is not seen as undeclared labour.

A second category is “any form of ‘exploitative’ work discrimination”. A new section 3a dealing with 'exploitative' work discrimination has been added (in 2004) to paragraph 47 of the Penal Code. According to this section, if employees are put in inferior position by an employer taking advantage of their financial or other distress, position of dependence or lack of understanding, or the thoughtlessness of another, the employer or its representative is liable to a fine or to imprisonment for up to two years. It is unclear whether there has been any case law in this field.

Early estimates on the overall size of undeclared labour place Finland in the category of countries with a rather modest level of undeclared activities (4.2% of GDP in 1992).¹ Later on it was estimated that the share of the black economy had remained at the 1992 levels.²

Recently the question of provision of services and free movement of workers has drawn much attention: there are hundreds of (Finnish) companies with establishments in Estonia (after 1 May 2004) and an increasing activity of temporary agency workers. The avoidance of social dumping and the protection of posted workers are important issues since then. Compliance with the construction collective agreement that is rendered applicable to all employees is in the forefront of the political debate.

The national regulatory system relevant for construction.

Construction is an important sector in Finland with 6.5% share of total employment and 5.4% of value-added to the total economy (2002). Both building and civil engineering recovered in 2003 after a period of recession. Latest reports talk about booming business, as economic indicators are currently very good. In 2005 and early 2006 there was a rising demand in construction products. Employment figures are expected to improve throughout the year 2006. In construction labour shortages are predicted. Shortages of skilled labour are considered an obstacle to production increases while contractors indicate that they are operating at full capacity. However, in some sub-sectors structural changes are still causing job losses.

¹ Finnish Ministry of Finance, as quoted in Undeclared work in an enlarged union, Inregia AB and Regioplan BV, European Commission, Brussels, 2004.

² According to VIRKE, referred to in the European Employment Observatory Review, Autumn 2004.

Employment in construction was estimated (in 2005) at 153,000 workers (118,000 building, 35,000 civil engineering) and construction output went up to 20.1 billion €. According to recent figures the industry is dominated by small and medium sized enterprises (with an average of 4 workers). Bigger contractors are coming from outside (as for instance Skanska or NCC). Finnish construction always had the highest R&D intensity, partially caused by the climate conditions.

Notwithstanding the modest figures undeclared labour is, according to several authors, on the rise in Finland with construction on top of the list of sectors concerned. Applicable legislation (taxation, social security, labour legislation) has been recently revised and increased cooperation of authorities is announced.

Legislative changes have been made to create preventative measures and to establish the necessary cooperation.

In 2002 some changes were made to the Penal Code in order to strengthen the fight against 'economic crime'. Some further legislative changes have been made to the Penal Code, the Employment Contracts Act and the Aliens Act during 2004. These legislative changes relate closely to the use of foreign workers and, to some extent, to undeclared work.

Section 6a of paragraph 47 of the Penal Code has also been amended. Now, an employer or its representative that hires or employs a foreign national not in possession of the requisite work permit is guilty of the use of illicit foreign labour and liable to a fine or to imprisonment for up to one year.

Section 16 of chapter 11 of the Employment Contracts Act prescribes the right of employees to receive a payslip. An employer or its representative that fails, on request, to provide a payslip to an employee is liable to a fine for violation of the Act.

According to paragraph 73 of the revised Aliens Act (301/2004), an employer that hires a 'third-country' employee must without any delay report this to an employment office and also inform the workplace shop steward and industrial safety delegate about the recruitment of the foreign worker and the collective agreement that applies.

Finland has a legal mechanism for extending collective agreements to make these agreements generally applicable. According to the Collective Agreements Act a collective agreement is defined as any agreement concluded by one or more employers or registered associations of employers and one or more registered trade union, concerning the conditions to be complied with in contracts of employment or in employment more in general (Bruun, 2006). The agreement is binding upon the signatory parties, registered associations that are subordinated directly or through one or more intermediaries to the signatory parties and individual employers and employees who are members of these associations. A contractor has to observe the provisions of the national collective agreement for construction that is normally made generally applicable with a national coverage. The agreement defines the terms and working conditions of the employment relationship. It stipulates the minimum rate of pay that an employer has to pay for a certain work or to a employee in a certain category. The agreement applies also to a posted construction worker.

The Finnish government reached a settlement in April 2006 with both sides of industry regarding new legislation on subscriber liability. This settlement outlines the matters that a business must investigate when using outside labour. The aim is to ensure that subcontractors and employment agencies discharge their obligations and comply with minimum employment terms. Under the proposed subscriber liability law, a business that uses outside labour will have to investigate whether any subcontractor or employment agency that it uses is registered in Finland for income tax withholding, employment and value-added tax purposes.

Documentation such as an extract from the trade register and a certificate of clearance for tax payments and employment pension contributions will also be required. The investigation will likewise cover details of the applicable collective agreement or of the principal terms and conditions of employment.

Corresponding information will also be required for foreign enterprises. However, there will be no duty to investigate the operations of established subcontractors and employment agencies or of national or local public authorities, public limited companies, State commercial institutions or organisations of comparable standing. A partner may be considered established, for example, when it has engaged in substantial business operations for about three years.

The new subscriber liability legislation will also include a provision requiring the subscribing business to notify its shop steward and labour protection delegate of any agreement on the use of outside labour. This notification will have to give details such as the amount of labour to be used, the length of the agreement and the applicable collective agreement or principal terms and conditions of employment.

The new law will apply whenever agency workers are used for longer than a total of ten working days, or if the value of a subcontracting agreement exceeds 7,500 euros. A subscriber enterprise that fails to investigate the circumstances of its partner will be liable for a penalty fine of between 1,500 and 15,000 euros. The local labour protection authority will determine this fine. The Finnish government will seek to introduce subscriber liability legislation before the end of the year

Authorities or institutions involved.

Institutions involved are the custom and tax authorities, the police and trade associations. As part of the National Action Plan the government wants to promote cooperation between the authorities and to rectify shortcomings in the legislation. The aim is to make monitoring easier and to increase information provision to foreign workers.

At the beginning of 2004 a new body was set up at the National Bureau of Investigation with the purpose to control the use of illegal foreign labour.

Social partners have established a strong cooperation with labour protection officials, the tax administration and the police and custom offices. The problem is poor staffing, weak control rights and few resources. Both unions and employer organisations are striving for regulations in collective agreements. Also the government is involved (seen the results of tripartite talks). However, a majority of employers is not organised and therefore the position of the employer's organisations is relatively weak. Arrangements between the social partners are only effectively covered by organised firms, leaving unorganised out. Notwithstanding this fact there have been joint initiatives on better information provision and on training of shop stewards and employees. The construction social partners have been cooperating for a long time to curb undeclared work in their sector. This cooperation has resulted in an agreement on procedures to curb such practices, whereby: companies demand proof of payment of tax liabilities and pension contributions from prospective contractors when they call for tenders; information on contracts is delivered quarterly to the tax administration; and electronic access pass systems are used by workers at building sites. The social partners have also jointly written a guide on how to use foreign labour in the construction sector. The Finnish Construction Trade Union (Rakennusliitto) has unilaterally conducted inspections of building sites to gather details of outsourced operations and their adherence to collective agreements.

Items related to the nature and features of undeclared work in construction.

In construction, informal economic activity has been estimated as representing (in 1998) between 9% and 16% of the industry's production, which corresponds to between 17.000 and 23.000 person-years (the annual work of 17.000-23.000 people).

Recent estimates (in 2005) calculate that the grey economy accounts for around 11% of the Finnish construction industry, generating a sum of EUR 700 million, and with a cost to society of EUR 200 million in lost tax revenue.

Undeclared labour in construction is strongly male-dominated. Although the majority of the illegal workers in construction are Finnish nationals, growing numbers of foreign workers are entering the 'clandestine' labour market. The general feeling is nowadays that illegal foreign work is the dominant shape of undeclared labour. There are no estimates of the overall involvement of legal or illegal immigrants, though recent discussions have paid increasing attention to the challenges raised by the eastwards enlargement of the EU in May 2004 as regards the informal economy. The Finnish Construction Trade Union suspects that only half of the sector's estimated 9.000-10.000 foreign workers are working legally. The employers so far have not given an estimate of the number of illegal workers. The employers' organisation in the sector, the Confederation of Finnish Construction Industries (Rakennusteollisuus, RT), however, puts the number of foreign nationals working legally substantially lower than Rakennusliitto's estimate.

Following EU enlargement in 2004 the issue of temporary agencies has become more marked as nationals of the new member states have had free access to the Finnish labour market through agencies while those looking for work independently still need work permits. Agency work is on the rise as a result of the activities of foreign agencies, and actually to even a larger extent of Finnish agencies. These agencies often not comply with collective agreements and create widespread problems with undeclared work. Most of the foreign agencies are based in the Baltic States and especially in Estonia. A large proportion of Estonian agencies are actually owned by Finns, and a survey executed by the Finnish Construction Trade Union, during a period of seven months in 2004, showed that of the 21 Estonian based companies 10 were owned or founded by Finns.

Industrial disputes have taken place in situations where there has been disagreement about foreign workers' work permits or the appropriateness of their working conditions. There are also cases where the target of action on the issue of undeclared work has been a specific firm, and cooperation has involved the police and/or tax authorities. Only in 2005 the construction union has initiated 50 industrial actions against undeclared practices with foreign labour. The bulk of the informal economic activity in the construction industry takes place in building one-family houses and holiday houses, in renovations that households have ordered and in chains of subcontractors on large building sites. It has reportedly become common practice for these companies to forge receipts and outsourcing contracts in order not to disclose the true amount of work performed at their sites. This allows them to pay part of the wages non registered. By setting up a new firm with a clean record, breaches of tax and pension contribution payments can be easily hidden. It is very easy to establish a new company and this is commonly done in the construction industry.

The functioning of the undeclared construction market.

Recent inspections in southern Finland found twenty percent of construction companies with foreign employees lacked proper documentation of their work permits or citizenship. Labour inspectors say the actual situation is probably much worse, because the companies they

looked into were well-known outfits. Smaller, less visible companies are more likely to rely on illegal labour.

The industry is criticized for using cheap illegal labour and sometimes circumventing stringent Finnish labour laws. Illegal workers - especially from the Baltic's and Russia but from as far away as China - frequently slip into the system. Most of these employees work under sub-standard contracts with few benefits. Latest inspections revealed that a fifth of construction companies couldn't guarantee that all of their foreign labour was above-board.

Another phenomenon has been the increase in self-employment. To a certain extent, self-employment is also associated with undeclared work. At the level of the whole economy, the scope of the problem is likely to be rather small, but in construction the phenomenon is certainly more widespread. The first trend towards more self-employment (outside agriculture) started in the early 1990s (see Table 1). Self-employment was from that moment seen by respective governments as an integral part of the labour market reform and as an alternative for unemployment. In the Labour Policy Strategy 2003-2007-2010, as adopted 23-10-2003, the increase of self-employed was one of the five strategic principles. Finally in the National Action Plan for Employment 2004 self-employment was, in accordance with the EU's employment guidelines, embraced as part of the development strategy towards entrepreneurship. In recent figures it is said that some 40% of all undertakings (overall) are single-person enterprises.

Table 1: Self-employment as a percentage of total employment by industry, 1989, 1993 and 1997

Industry	1989	1993	1997
Agriculture, forestry, fishing	65	64	67
Manufacturing, mining, quarrying, energy supply	5	6	6
Construction	16	19	19
Trade, repair of vehicles and household goods	17	18	20
Hotels and restaurants	13	17	14
Transport, storage and communication	12	13	14
Financial, real estate, business services	11	13	13
Education, health care and social work	3	2	2
Personal services and other community services	19	22	20
All non-agricultural industries	9	10	10
All industries	14	15	14

Source: Statistics Finland Labour Force Survey.

According to the Labour Force Survey of Statistics, the number of both wage earners and self-employed persons grew during the period 2005-2006. Employment increased in manufacturing, construction, transport and social services. Official data show only a slight increase of self-employment and in the overall figures (all industries) self-employment stabilises at the level of the nineties (Table 2). There are no recent figures for construction with regard to self-employment available.

Table 2: Changes in the labour force 2005-2006 (in thousands).

	January 2006	January 2005	Change, % 1/05 - 1/06
Employed total	2 353	2 299	2.3
- wage and salary earners	2 034	1 995	2.0
- self-employed and assisting family members	318	304	4.8
Employment rate, %	66.6	65.3	1.3²
Unemployed¹	226	249	-9.3
Unemployment rate, %	8.7	9.8	-1.1²
Labour force, total	2 578	2 547	1.2
Labour force participation rate	65.2	64.6	0.6²
Economically inactive, total	1 377	1 394	-1.2
- students	372	394	-5.4
- persons performing domestic work	87	93	-6.6
- economically inactive persons in disguised unemployment	114	96	18.3

¹ Based on the recommendations of the International Labour Organisation (ILO)

² Percentage points.

Source: Statistics Finland's Labour Force Survey.

The high tax wedge has contributed to tax evasion or unjustified claims for social benefits filed by people working clandestinely. In early estimates (1994) it has been calculated that some 3 to 4% of the recipients of unemployment benefits work on the black market.

According to several surveys, the unemployed do not work in the black economy more than the employed. The black economy is assumed to be bigger in absolute terms during periods of high economic activity and is also thought to reflect the effect of better opportunities. In terms of capabilities and contacts, a better education and a higher level of income seem to be positively related to a high incidence of undeclared work. Finally, according to a survey commissioned by the National Board of Taxes in 1996, 16% of the respondents reported that they had carried out undeclared work during the preceding year. Moreover, 19% of the respondents said that during the preceding five years, they had bought goods or services on which statutory dues had not been paid.

The effects of undeclared work in construction.

The social partners agree that undeclared labour is creating a distortion of competition and has negative socio-economic effects. Undeclared labour puts pressure on social provisions and benefits and it can have an undermining effect on industry wide provisions.

Transactions in the shadow, rather than the official, economy keep state revenues lower than they otherwise would be, and in turn reduce governments' ability to provide goods and services. Higher taxation, especially when combined with a perceived deterioration in the quality of public goods and public administration motivates even more strongly to move into the shadow economy, perpetuating the cycle.

The general impression is that there is less acceptance to earn income without paying taxes than in the 1990s, according to an opinion poll of SAK.

In recent years the enforcement policy of increased control by tax and labour market authorities has been combined with increasing public attention for an efficient monitoring of the working conditions of foreign workers. This policy is developed with a view on the mix of shaping factors, different actors and circumstances, and the effects of undeclared labour. The acceptance in society of this range of institutional arrangements is growing.

Measures taken.

Both trade unions and employers' organisations regard undeclared work as a cause of concern. Trade unions have taken part in all nationwide activities against undeclared work (see above), and have taken an active role at the local level. In the context of EU enlargement, trade unions have demanded a right to institute, without their authorisation, legal proceedings on behalf of foreign workers posted to Finland, as regards their wages and other terms of employment. Employers emphasise that the most important point in this respect is to combat criminal activities and to carry out measures that prevent deliberate law breaking. Employers are not in favour of measures that increase bureaucracy and make regular companies' operation more difficult.

Besides subscriber liability, mentioned above, social partners are also seeking to combat the grey economy by such methods as extending taxation and supervision of foreign agency labour, requiring foreign enterprises to be listed in the tax withholding register and securing the permanent status of the foreign labour surveillance unit at the Finnish National Bureau of Investigation. Finally they cooperate in campaigns in the industry and in informing construction firms about the proper use of foreign labour. In May 2004, they published a guidebook on the subject.

As of May 1 2006 Finland will no longer restrict the free movement of labour from the new Member States of the EU. The past two years of restricted entry rights have been put to good use by allowing time for control mechanisms against the grey economy and abuse of foreign labour to be put firmly in place. The core of the new legislation will be the subscriber liability law mentioned before. Labour market parties and the Finnish government have reached an agreement on what exactly this should cover. Companies will have more obligations to investigate their subcontractors' way of handling taxation and social security payments and the working conditions of subcontractor employees.

In the present EU it is fully possible for an undertaker condemned by court to a prohibition to conduct any business by reasons of grave misconduct to establish himself in another country and conduct activities as services provider by use of posted workers in the Member State where the prohibition is in force. In order to tackle this the government introduced legislation prescribing a requirement of a legal representative.

New legislation on taxation of foreign labour sent by agencies, based outside of Finland, is also underway. Under current Finnish legislation, Finland cannot tax foreign agency labour that works in Finland for a period of less than six months. However, treaties with other Nordic countries and the Baltic States allow to tax foreign agency labour for even short periods of work in Finland. The government wants to tighten control over foreign agency labour. It will require all foreign employees coming from other EU Member States to register at an employment bureau within two weeks of arrival.

Good practices.

The electronic pass system and the requirements for disclosure of company information contribute probably to a reduction of undeclared activities. For this, the monitoring of company activities not only have to be made more extensive but also needs to take place in electronic form and as close to real time as possible. At present the informal economy is always one step ahead of the supervisory agencies and successful raids on building sites require good timing and large personnel resources. A further step in the right direction has been the tax administration's online and SMS service, which allows any company's

prepayment registration status to be checked in real time. This used to be done by making firms provide a printout certificate, and these were frequently forgeries.

According to a recent report by the public authorities, assessing the state of the clandestine economy in Finland, the electronic pass system proved the most effective of the measures in the construction industry. It has made it possible effectively to monitor all contractors and workers at building sites. As a result, illicit activity is now easier to detect.

Other agreed measures have been less successful. It is still very easy to start a new company with a clean record in construction and hide breaches of tax and pension contribution payments.

Since 1st February 2006, employees on construction sites, have to wear visible identifiers. This is decreed in a new provision of the 2002 Occupational Safety and Health Act. The only ones exempt from this ruling are people transporting goods to the sites. Identifiers must also be worn on sites where old buildings are undergoing renovation. The identifier has to include its holder's photograph, name and his or her employer's name.

The identifier covers house building, conservation and special contracting, such as heating, plumbing and air conditioning, electrical installations as well as civil engineering. The use of the identifier shall apply to all construction sites that have workers with several employers and independent workers. According to the provision, the promoter has to ensure and secure with his own measures that everybody has the identifier visible. By giving the responsibility to the promoter, the aim is to ensure that the identifiers are really used. Usually it is professional builders and professional house managers that act as promoters. The promoter must in an agreement with the main contractor take into account the obligation of using the identifier, and also ensure that the main contractor's parties to the agreement take corresponding account of the obligation to use the identifier in their own subcontracting agreements.

The act was prepared by a working group consisting of representatives from several ministries, the central labour market organisations, the workers' and employers' organisations representing the building trade, and the Federation of Finnish Enterprises.

Its aim is to prevent grey economy and illegal labour.

The Construction Trade Union regards the reform as an important step in the fight against the grey economy and illegal employment. It will also improve occupational safety, the union emphasises. The Union has itself decided to increase the resources it spends on monitoring construction sites. Monitoring usage of identifiers will be one of the new challenges. An open question is how to tackle fake identifiers that eventually will be used by some of those involved in illegal activities. According to the new order, those responsible for neglect against it may be fined.

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