

# Shadow economy from business perspective: causes and solutions

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Latvijas Tirdzniecības  
un rūpniecības kamera

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# *Introduction: from discussions among entrepreneurs*

1. “If I pay fairly all the taxes I am not able to compete because half of market participants acts in the grey area”
2. “They [public administration] only make promises that life for entrepreneurs will be easier, but they do not want to listen to us!”
3. “They [public administration] anyway squander all the money paid in taxes”



# *LCCI Entrepreneur Plan 2010: what do entrepreneurs wait from the state?*

## **Pre-conditions for competitive business in “white” area, including:**

- transparent, predictable, internationally competitive business environment;
- business-friendly tax system and administration;
- low corruption in the state;
- effective and non-repressive monitoring/administration system;
- confidence between managers and subordinated bodies, incl. constructive dialogue between entrepreneurs and state.



# *Transparency?*

- Passing forward issues important for entrepreneurs to the CoM in urgency procedure without coordination with entrepreneurial organizations;
- Limited involvement/ information of entrepreneurial organizations in the dialogue with IMF/EC;
- No lobby regulation – no regulation on participation of entrepreneurs in decision-making.



# *Predictability?*

- What fiscal consolidation measures will be taken in budget 2011?
- What tax changes will be introduced in 2011-2013?
- Will the state provide support for particular sectors, and if yes – what will happen with other sectors?
- Will the euro be introduced in Latvia in 2014, and if yes – what it will cost us?
- ***Conclusion: “bad news” – after elections***



# *Internationally competitive business environment?*

- Latvia in World Bank's *Doing Business* rating scale - **No.27** (among 189 countries)
- *Global Competitiveness Report* – **No.70** (among 139 countries)
- GCR 2010 key obstacles to business:
  - tax regulation and rates;
  - non-effective public administration;
  - corruption;
  - political instability;
  - non-availability of financial resources.



# *Business-friendly tax system and administration*

- High taxes on labour costs do not stimulate transition of entrepreneurs from “grey” to “white” area
- Combating of VAT schemes – combating consequences; insufficient political will to perform considerable VAT administration reforms
- Vague medium-term tax policy + frequent tax regulation changes do not facilitate confidence in state administration



## *Low corruption in the state?*

- Transparency International 2009: Latvia No. 56 (among 180 countries), No. 22 among EU countries
- Corruption: misuse of public resources to gain private benefit
- Reduced financing for public procurements = intense competition among entrepreneurs = corruptions risks in public procurements





## *Effective and non-repressive monitoring/administration system*

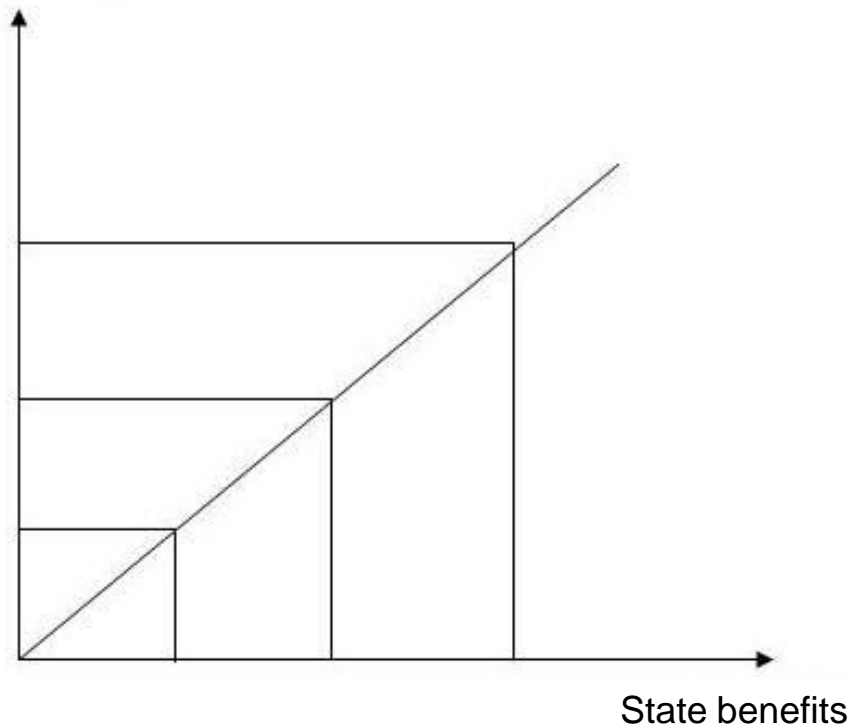
- Entrepreneur deals with 59 state public bodies in the course of its business activities
- Compliance with requirements causes disproportionately high costs = corruption risk
- Legal proceeding lasting for years does not ensure “reasonable” term of administrative process
- Ineffective public procurement control system



# *Confidence between the state and entrepreneurs*

Start: all entrepreneurs are “white”!

Company's growth



# *Tasks for the new government (I)*

- Listen to entrepreneurs = searching together for a way-out from the shadow economy, incl. introduction of already made decisions
- Transparency of decision-making = adopt a lobby regulation
- More predictability = dialogue about drafting state budget 2011, incl. tax changes



# *Tasks for the new government (II)*

Medium-term tax policy based on positive impact on Latvian business environment and sustainable development, incl.:

- a) introduction of reverse VAT payments = “poison” of VAT scheme;
- b) reduction of taxes on labour costs = reduction of “envelope” wages;
- c) maintenance of CIT allowances/credits and introduction of new ones = profit is not artificially reduced.



## *Tasks for the new government (III)*

International competitiveness = in mutual cooperation performed targeted measures increasing competitiveness of Latvia/entrepreneurs and improving business environment (*Doing Business* and *GCR*)

- Authorisation of PPB to impose administrative punishments for violations in public procurements = risks of squandering state property reduces
- Develop state “benefit package” for entrepreneurs to encourage participation in registered economy and fulfillment of the state obligations



# Thank you for attention!

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