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Informal Employment or Decent Pension? Which One is More Desirable?

Abstract

The informal economy, along with informal employment as its core component, remains a critical issue for policymakers in Azerbaijan. According to the International Labour Organization (ILO), informal economies are often associated with high poverty rates and significant decent work deficits. The formalization of the economy is essential to ensure equitable distribution of opportunities and resources within society. In its 2002 resolution, the ILO defines the informal economy as encompassing all economic activities by workers and units not adequately covered by legal or institutional frameworks. In the literature, the informal economy is also referred to as the shadow, underground, or grey economy. Addressing informality is pivotal for sustainable development and labor market efficiency.

Keywords: *informal economy, informal employment, decent work, ILO, shadow economy, economic formalization*

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Qeyri-rəsmi məşğulluq və ya layiqli pensiya? Hansı daha arzuolunandır?

Xülasə

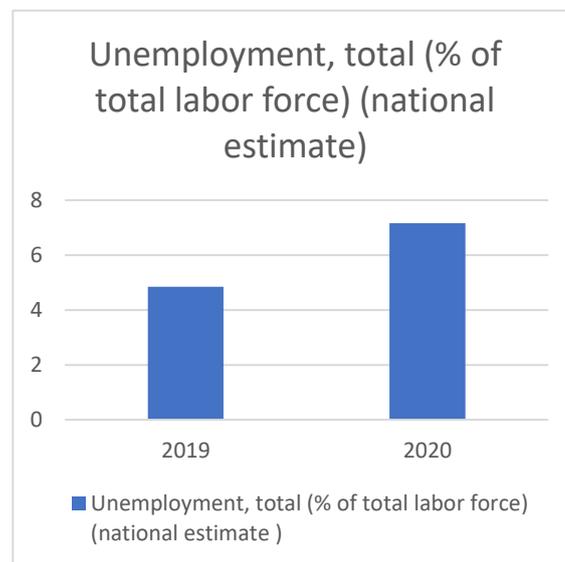
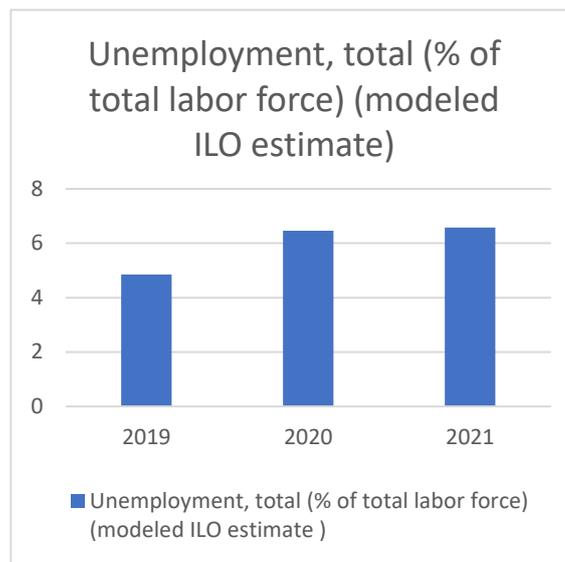
Qeyri-rəsmi iqtisadiyyat və onun əsas hissəsi olan qeyri-rəsmi məşğulluq Azərbaycan siyasətçiləri üçün vacib məsələlərdən biri olaraq qalır. Beynəlxalq Əmək Təşkilatının (ILO) məlumatına görə, qeyri-rəsmi iqtisadiyyatlar adətən yüksək yoxsulluq səviyyəsi və ciddi layiqli əmək çatışmazlığı ilə xarakterizə olunur. İqtisadiyyatın rəsmi formaya keçirilməsi cəmiyyətdə imkanların və resursların ədalətli bölüşdürülməsi baxımından mühüm əhəmiyyət kəsb edir. ILO-nun 2002-ci il tarixli “Layiqli əmək və qeyri-rəsmi iqtisadiyyat haqqında qətnaməsi”ndə qeyri-rəsmi iqtisadiyyat, hüquqi və institusional mexanizmlərlə yetərinə əhatə olunmayan bütün iqtisadi fəaliyyətləri əhatə edən anlayış kimi təqdim olunur. Ədəbiyyatda bu iqtisadiyyat növü kölgə, qeyri-rəsmi və ya boz iqtisadiyyat adlandırılır. Qeyri-rəsmi iqtisadiyyatın aradan qaldırılması davamlı inkişaf və əmək bazarının səmərəliliyi üçün vacibdir.

Açar sözlər: *qeyri-rəsmi iqtisadiyyat, qeyri-rəsmi məşğulluq, layiqli əmək, ILO, kölgə iqtisadiyyatı, iqtisadi formallaşma*

Introduction

For several years “Azerbaijan had the second largest shadow economy with 33.8 (41) percent of GDP” in the list of former Soviet Union countries (Schneider, Enste, 2000).

Also, the World Bank datasets indicates the statistical data on current informality rate in Azerbaijan as followingly:



Additionally, in accordance to the Country Profile report of Azerbaijan (Enterprise Surveys, 2019) 29.9 percent of firms demonstrate informality in terms of acting as unregistered firms while starting to business. Thus, some firms try to avoid official rules and regulations, including tax obligations set by government. For this purpose, they do not register their business and “remain in the informal sector”.

Informal employment is key aspect that causes to the informal economy.

Due to State Statistics Committee, currently total population of Azerbaijan is 10 156,4 thousand people, while 6 984, 5 thousand of them are at working age. Actually this number does not mean that all these people are contain a labor force.

Research

Thus, only 5303,9 thousand people are considered an economically active population (www.stat.gov.az, n.d.). So, only about half of the population does not contain a labor force and does not create a threat to formality of the economy.

Informality problem occurs while analyzing the number of total employed people and number of people working with labor (employment) contracts.

The Article 1.1.9 of the “Law of the Republic of Azerbaijan on Employment” determines the definition of “informal employment”.

In accordance to this Law the informal employment is –

- ✓ performing certain activities without concluding an employment contract in accordance to the Labor Code of the Republic of Azerbaijan or;
- ✓ performing certain activities without concluding civil legal agreement in accordance to the Civil Code of the Republic of Azerbaijan
- ✓ carrying out entrepreneurial activities and use of land suitable for agriculture in the property without formalization in accordance to Tax Code of the Republic of Azerbaijan;
- ✓ obtaining profit (income) as a result of organizing a family farm without keeping records in local self-governing bodies (Azərbaycan Respublikası İqtisadiyyat Nazirliyi yanında Dövlət Vergi Xidməti, n.d.).

Employment contracts vs Employed people in Azerbaijan

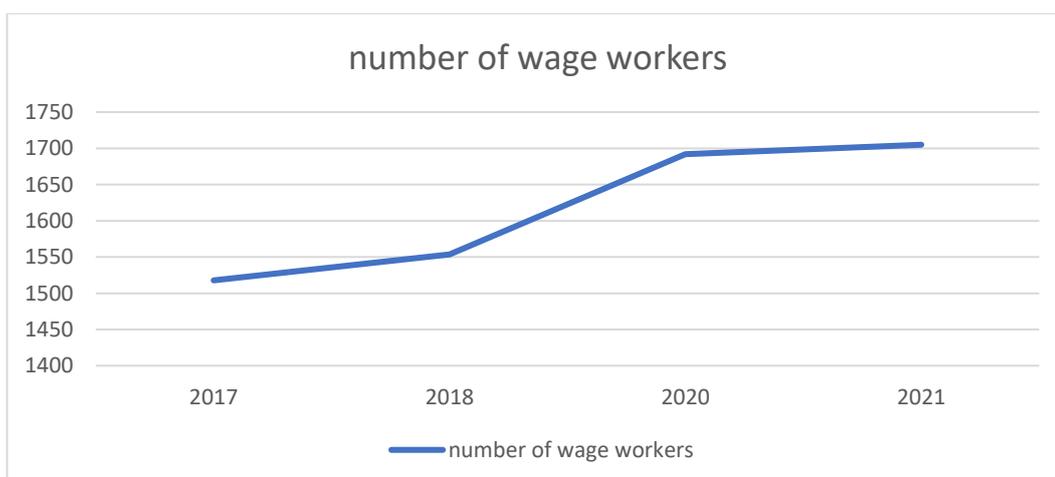
The 1704.9 thousand out of 4 988,2 thousand people of Azerbaijan who are total employed people, are considered wage workers. In other words, only 1704.9 thousand people of Azerbaijan (2021) works with employment contracts (www.taxes.gov.az, n.d.)

Note: in some sources this number is 1 741 468 (report.az, n.d.)

Here we encounter with mystery.

The Annual reports of Ministry of Labor and Social protection of Population of the Republic of Azerbaijan emphasize that (The World Bank, n.d.):

- ✚ in 2017 the number of wage workers was 1517.8 thousand people.
- ✚ in 2018 the number of wage workers increased 2.1 percent in comparison to previous year and reached 1553.6 thousand people.
- ✚ in 2020 the number of wage workers increased 2.7 percent in comparison to previous year and reached 1691.8 thousand people. 53.8 % of them were directed to state sector of the economy and 46.2 % were directed to non-stat sector.
- ✚ in 2021 the number of wage workers increased 1.2 percent in comparison to previous year and reached 1704.9 thousand people. 905.7 thousand of them were employed in public sector, while 799.2 thousand people employed in the non-state sector.



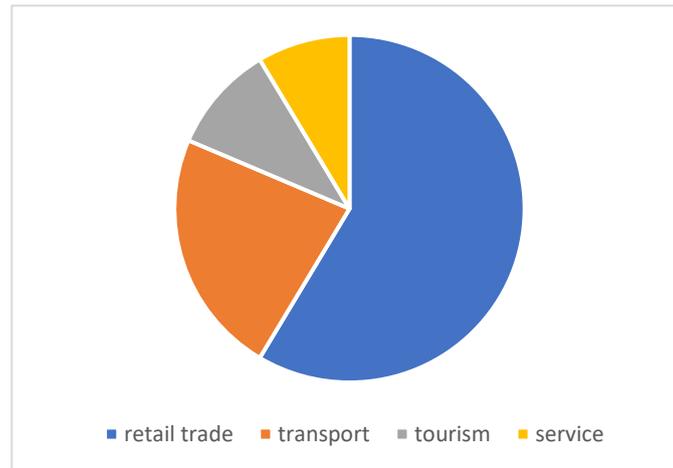
Taking into account that, around 1.7 million people could work in agriculture and about 1.5 million people could be considered as self-employed. Then the rest of employed population will be evaluated as informally employed people.

Here the question arises: why the number of labor contracts contains only 35 percent of employed people? This question illustrates the issue of informal employment in Azerbaijan.

Reasons and consequences

Informal economy may cover either wage workers or own-account workers. “Workers in the informal economy are not recognized, registered, regulated and protected under labor legislation and social protection.” (International Labour Organization (ILO, 2002) **Workers subjected to the informal employment cannot demand the implementation of their fundamental rights as to work in relevant working conditions, to have social or health security, to benefit from various financial mechanisms as mortgage, bank loans etc.** Therefore, appropriate research and urgent and pointed approach to diminish informal employment in Azerbaijan is inevitable.

Currently, the high level of informal employment in Azerbaijan could be observed especially in the following fields of economy:



High rate of informal employment negatively interacts with transparency of the country’s economy.

As far as employers keep their worker under the umbrella of mystery of informal employment they may easily avoid to meet the requirements of government on taxes, social insurance plans, etc. **Such employers meaningfully may violate the international labor standards** when designing or realizing working conditions, requirements.

Moreover, workers employed without labor contracts **don’t earn the official employment experience (years of work experience), which further negatively affects to calculation of pension amount** of this worker.

Government and international responses

In international level the **International Labor Organization** is a principal body who has relevant mandate in the field in accordance with the ILO Declaration on Fundamental Principles and Rights at Work, 1998 and Decent Work Agenda (International Labour Organization (ILO), 2002).

In its “**R198-Employment Relationship Recommendations, 2006**” ILO obliges the States with certain requirements on formulation of “National policy of protection for worker in an employment relationship”, “Determination of the existence of an employment relationship”/ “monitoring and implementation” (International Labour Organization (ILO), 2002).

Especially, in “**R204-Transition from Informal to the Formal Economy Recommendation, 2015**” ILO provides guidance to Member States

- a) “to facilitate the transition of workers and economic units from informal to formal economy;
- b) promote the creation, preservation and sustainability of enterprises and decent jobs in formal economy;
- c) prevent the informalization of formal economy jobs.”

In nation-wide, starting 2017 Azerbaijani Government applied several tools to address the informal employment.

First and foremost, in 2017 Azerbaijani Government adopted **“The Action Plan for the prevention of informal employment in the Republic of Azerbaijan”**. (Approved by the Decree of the President, dated 09.10.2017, Number 3287) (Report.az., 2022)

The reasons caused to necessity of this Action plan was the aim:

- to legalize employer-employee relations,
- to improve the control mechanism on organization of labor payment,
- to realize an effectively coordinated policy between related governmental bodies.

Most desired consequences was to improve the legal base on prevention of informal employment, to provide worker’s right to social protection, to stimulate employers to avoid from informal employment, to motivate employers to legalize the labor relations of workers and so on.

To reach these consequences several amendments to various legislative acts was offered to be done by this Action Plan. So, per such fundamental change policy some amendment made to the Tax Code of Azerbaijan.

Starting January 1 of 2019 tax reform was implemented and the income tax (in amount on 14 percent) for employees working in non-oil and non-state sector has been abolished. So, the employees of non-oil and non-state sector, whose wage was up to 8,000 thousand AZN per month were exempted from income tax for seven years period as a pilot Project. The goal was to motivate employers of non-oil sector to formalize their employer-employee relations. In other words, this tax policy was intended to gradually remove shadow economy and decrease unofficial employment via **“whitening the employment contracts”**.

Later in 2020 next legislative act was adopted. So, due to **“the Rule for carrying out and coordinating control measures in the field of legalization of informal employment”** (approved by the Decision of the Cabinet of Ministers of the Republic of Azerbaijan dated 17.03.2020, number 96) (The World Bank, 2019) the three governmental bodies - like the Ministry of Labor and Social protection of Population of the Republic of Azerbaijan, the Ministry of Economy and the State Agency for Service to Citizens and Social Innovations under the President of the Republic of Azerbaijan are determined as principal agencies to realize the control over legalization of informal employment. They tasked (The World Bank Group, 2019):

- ✓ to prevent and control the informal employment,
- ✓ to research the fields wherein the informal employment is in highest level
- ✓ to realize monitoring and evaluation

Simultaneously, a single electronic information system was created and named **“Control of informal employment”**.

Also, upon the next decree of the President, the list of relevant information systems that needed to be integrated to the system of **“Control of informal employment”** was determined. The most interesting point is that, 25 different systems of 18 governmental bodies was listed as necessary information sources to help to detect and manage informal employment. Interestingly, even relevant data base of **“Azerishig”** and **“Azersu”** was considered as role-playing features in this process. Somehow **an ideal net of electronic sources was maintained in order to effectively collaborate and control and prevent informal employment.**

Numerous **awareness raising programs** on negative consequences of informal employment was distributed and displayed via social media.

Simultaneously, in accordance to Ministry of Labor and Social Protection of Population (Dövlət Statistika Komitəsi, 2022).

In 2019

- 103 thousand unemployed people were provided with relevant jobs (permanent and temporary jobs);

In 2020

- 100 thousand unemployed people were provided with relevant jobs (permanent and temporary jobs);
- 12 thousand people involved to self-employment programs;
- Some people directed to professional trainings;

In 2021

- Azerbaijani Government jointly with the UN Development Program (UNDP) implemented a program of “Creation of inclusive and decent jobs for socially vulnerable groups of population”;
- Also, the relevant Ministry and World Bank realized the project of “Support to the Employment in Azerbaijan”.

Unfortunately, all above-mentioned policy elements was not sufficient to reach a full elimination of informal employment in Azerbaijan.

Conclusion and Recommendations

Conclusion

In my assumption, here two sided approach is necessary to be applied in order to reach full formality.

- In respect to employers
- In respect to employees.

Guiding by the ILO’ “R204-Transition from Informal to the Formal Economy Recommendation, 2015” should be priority for the Government of Azerbaijan to diminish the informal employment rate in the country in terms of forcing employers to formalize their businesses.

Simultaneously, more transparent and prosperity-proving policy should be applied to new beginning businesses, especially to medium and small-sized entrepreneurs.

The new tax reform needs to be applied to reach complete digitalization of the tax payments.

Moreover, payment of salaries should be fully switched to electronic systems, which will help to reduce informal employment.

Model of European Countries (where the informality is in its lowest rate in the world) in fight against informal economy, especially the policy to focus on worker that tend to be invisible could be examined.

Also, the implementation of the unemployment insurance system should be accelerated. Thus, availability of the Unemployment Insurance Fund (UIF) should be increased. The procedures to obtain relevant benefit from UIF should be simplified.

Furthermore, in my assumption people would prefer to formalize their employment in case if they will meet their expectations in progress in pension system of the country.

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