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# The social consequences of government intervention in labor management in Russia

### **Abstract**

The article discusses the problem of the proliferation of informal employment in Russia as a result of state regulation of the labor market. The purposes of this article are: the search for patterns of informal employment; identification of factors that determine the willingness of employees to this particular form of employment. That will predict the consequences of government intervention in the labor sphere. The empirical base of the work were the results of sociological research 2006-2016 in the Tyumen region. The methods of cluster, correlation analysis and Mann-Whitney U-Test are used. It is shown that informal employment is divided into two fundamentally different clusters: the forced work that way due to lack of experience, education, social relationships and consciously chosen form of informal employment as a more profitable for themselves. The article shows the difference between these groups by type of motivation, the level of social well-being, ways of involvement in informal employment and reaction to the government impact.

**Keywords**: state administration of work; informal employment; the labor market.

JEL CODE: J46.

## Społeczne konsekwencje interwencji rządu w zarządzaniu pracą w Rosji

#### **Abstrakt**

W artykule omówiono problem rozrostu nieformalnego zatrudnienia w Rosji w wyniku regulacji rynku pracy. Celami niniejszego artykułu są: poszukiwanie wzorców zatrudnienia nieformalnego oraz identyfikacja czynników wpływających na gotowość pracowników do tej formy zatrudnienia. To pozwoli przewidzieć konsekwencje interwencji rządu w sferze pracy. Empiryczną podstawą artykułu są wyniki badań socjologicznych z lat 2006-2016 przeprowadzone w regionie Tyumen. Wykorzystano metody klastrowe, analizę korelacji oraz test U Manna Whitneya. Wykazano, że nieformalne zatrudnienie jest podzielone na dwa zasadniczo różne klastry: przymusowe zatrudnienie wynikające z braku doświadczenia, edukacji, relacji społecznych oraz świadomie wybierane nieformalne zatrudnienie, którego

powodem są większe zyski. W artykule przedstawiono różnice między tymi grupami według rodzaju motywacji, poziomu dobrobytu społecznego, sposobów zaangażowania w nieformalną pracę oraz reakcji na działania podejmowane przez rząd.

Słowa klucze: państwowa administracja pracy; zatrudnienie nieformalne; rynek pracy.

### Introduction

The 1990s Russian reforms led to the unemployment release and the dual job holding acceptance. The government made labour sphere a specific market and turned a blind eye on a large number of infringement of employees' rights which has led to the growth of illegal processes on the labour market and the expansion of informal employment. The result of this policy was the systematic underfunding of the state budget and Compulsory Medical and Pension Insurance Funds. It is difficult to evaluate the size of these losses due to the specificity of informal employment and its concealed nature. Using various evaluation methods, the researchers give different evaluations which vary widely from 15 to 45 percent of total labour force (Barsukova 2003; Varshavskaya, Donova 2003; Gimpelson 2013; Malysheva 2016). For example, the Russian Federal State Statistics Service (Rosstat) evaluates the difference between expenses and registered income of the households and claims that the concealed income is about 10 trillion roubles. Submitted by the Ministry of Finance, the project "Guidelines for Fiscal policy" planned for 2017-2019 points out that the size of illegal salaries is about 5 trillion rubles a year (Ministry of Finance, 2016). The government pays more attention to this phenomenon due to its wide proliferation. The Ministry of Finance declares one of the priority measures the need to combat the phenomenon of illegal salaries.

Despite the growing attention to informal employment, from both the scientific community and the institutions of state authority, not all aspects of this problem have been studied well. Most scholars focus on estimating the spread of informal employment and "count the losses" caused by it (Feige 1990; Hart 1999; Xue, Gao, Guo 2014; Williams, Horodnic 2015; Bologna 2016; Malysheva 2016). Since the phenomenon has the informal nature and the researches use different methods of estimation the results often vary widely. Yet, to solve the problem we should pay more attention to understanding the mechanisms that lead to the problem and provoke its proliferation rather than its accurate evaluation. The purpose of this article is to search for patterns of informal employment and determine the factors that make employees the part of this particular form of employment. If we know the

specificity of formal and informal employment in the country we can give a more accurate estimation of the consequences of the government's intervention in the labour sphere (Kaźmierczyk 2008). The objectives of the study are: to build a social portrait of an informal worker, to analyse the work motivation of employees with different types of employment, to compare their social feeling with their attitude to state institutions. The main hypotheses of the study: 1) people working on conditions of informal employment have a lower level of education than officially employed; 2) self-assessment of the financial situation and social well-being of informally employed is significantly lower than among officially employed; 3) informally employed workers will most often demonstrate a motivation to attainable type work.

The empirical base of the work was the results of sociological research 2006-2016 in the Tyumen region. The methods of cluster and correlation analysis, Mann-Whitney U-Test are used. It is shown that informal employment is divided into two fundamentally different clusters: the forced work that way due to lack of experience, education, social relationships and consciously chosen form of informal employment as a more profitable for themselves. The article shows the difference between these groups by type of motivation, the level of social well-being, ways of involvement in informal employment, reaction to the government impact (Kaźmierczyk 2013; Kaźmierczyk, Nowak 2013). In this work reviewed articles were taken from following databases: Ebsco, Emerald, Elsevier, eLibrary.

The article discusses the problem of the proliferation of informal employment in Russia as a result of state regulation of the labor market. Based on the analysis of socio-demographic characteristics of informal workers and the characteristics of their work motivation, the main mechanisms of involvement in informal employment are highlighted. This is 1) discriminatory when employees are forced out of the formal labor market and 2) entrepreneurial in which informal employment is a way of reducing the costs of "law-abiding". Accordingly, each of these mechanisms forms its own specific cluster of informally employed workers. A description of these clusters is given.

### An overview of the concepts of informal employment

An attempt was made to study publications, addressing the problem of informal employment in different countries (Xue, Gao, Guo 2014; Bologna 2016; Fernández, Meza 2015; Binay 2015; Magidimisha, Gordon 2015; Selwaness, Zaki 2015; Lopez-Ruiz, Benavides, Artazcoz, Vives 2016; Sahoo, Neog 2016; Williams, Horodnic 2015). Primarily,

the phenomenon of informal employment, was perceived by the researchers as a sign of poverty and underdevelopment of the labor market, that typical for developing countries (Hart 1999; De Soto 1995). Nowadays, this opinion is shared by some researchers (Sahoo, Neog 2016). However, considering the fact that informal employment is detected almost everywhere, including countries with developed market economies and even in the former USSR (Grossman 1977; Portes, Castells, Benton 1989; Williams Horodnic 2015), this assessment is overly simplified.

It is possible to arrive at an erroneous conclusion when comparing the results of the studies because the different authors' opinion may not coincide. That is why, primary, we need to define the studied phenomenon clearly (Gutmann, 1979). Almost all the informal employment conceptions put an emphasis on the specificity of person's attitude to state and law. For example, D. Gershoni says that the informal employment indicators are the conclusion of a contract bypassing state laws and regulations and the concealment of the financial operations of an enterprise (Gershoni 1999, p. 344). E. Feige claims that informal employment is the conclusion of the labour contract avoiding administrative measures of regulation of labour relations (Feige 1990, p. 992). Thus, it is emphasised that the informal employment is not registered or recorded.

But what does it mean "not registered"? There are two approaches. In the first, the financial operations of the enterprise are not registered. In this case, informal employment includes all workers employed in the informal (shady) economy (Latov 2001; Bologna 2016). In the second, the fact of employment is not registered. Within this approach, informally employed are the employees working without labour contract. These may be both formally and informally employed people, such as workers who have only a personal agreement with the employer or self-employed persons (Magidimisha, Gordon 2015; Lopez-Ruiz, Benavides, Artazcoz, Vives 2016; Williams, Horodnic 2015). Synthetising these two approaches, we provide a more developed definition. So, the informal employment is not declared one, when the real employee's income exceeds the officially registered (Barsukova 2003; Zaslavskaya, Shabanova 2002). Special attention is paid to the role of social ties in the labor market (Granovetter 1992). In this article, the informal employment is defined as a relationship between the employer and the employee, based only on the personal agreement.

#### Materials and methods of research

The empirical base of the work was the results of the sociological research carried out in 2006-2016 in the Tyumen region by survey method. The opinion of the ordinary people as the representatives of the labour market was studied to identify the groups of respondents employed without the labour contract. 1500 people were interviewed in 2006, 1560 in 2009 and 1514 people in 2016. The structure of the sample was modelled in a precise conformity with the structure of the general sample according to these parameters: sex, age, type of settlement (city-village) and the level of education. The sampling error on one indication is less than 3% (2,5-2,6%) which provides high representativeness of the research results.

Various statistical methods were used to analyse sociological data. The Mann-Whitney-Utest was used to estimate the value of the difference between subsamples with formal and informal employment. The associations between variables were determined through the correlation analysis. The informally employed population was segmented through the cluster analysis.

### Main results

Respondents were asked: "If you work today do you have a labour contract?" 64% of the respondents said "yes" in 2006, 63% in 2009 and 62% in 2016. The absence of the labour contract was noted by 8% of the respondents in 2006 and 2009 and by 11% in 2016, i.e. one person in ten can be referred to the informally employed. Besides, the situation has not really changed over the last decade. Interestingly, about 30% of the respondents had no answer or even refused to answer this question. Firstly, it could happen because the employees didn't want to expose their involvement into illegal economics, or, secondly, because the informal employment has the seasonal nature. In the third, as S.Y. Barsukova claims, this could be a sign of a paradoxical interdependence of the formal and informal employment (Barsukova 2003, p. 4), i.e. the workers do not know what to answer in a situation when the labour contract seems to exist but it's a total fiction and the main part of their salary is paid "cash-in-hand".

The informal employment prevails among the private enterprises, where one person in five doesn't have a labour contract (Table 1). However, the private sector is not the only source of the informal employment. Six per cent of those working in state-owned enterprises

and budget institutions do not have the labour contract either. The share of informally employed in the area of trade (22%) and services (18%) is higher.

Table 1. Informal employment among workers of different types of companies and spheres of activity  $(\%^*, N=1514, 2016)$ 

	Do you have a written employment contract at your main job?		
	Yes, I have a written contract	No, I do not have a written contract	I do not know, refusal of an answer
Company type			
Budget organization or institution	88	6	6
State enterprise	86	7	7
Joint-stock company with state participation	90	3	7
Joint-stock company without state participation	93	4	3
Enterprise/company (your personal property)	78	17	5
Private enterprise (not your property)	76	20	4
Individual work activity	51	36	13
Sphere of activity			
State and Municipal Administration	89	4	7
Social sphere (education, health, culture)	87	6	7
Sphere of activity (except for mining industry)	80	10	10
Mining	74	16	10
Industry Services	78	16	6
Services to the population	75	18	7
Trade	71	22	7
Agriculture	65	15	20
In general	62	11	27

Source: survey research.

The type of the human capital excluded from the legal economics and perspectives of its formalization can be determined by identifying demographic characteristics of the informally employed population. Sex, age and the level of education determine the possibility of involvement into illegal economics (Magidimisha, Gordon 2015; Lopez-Ruiz, Benavides, Artazcoz, Vives 2016; Sahoo, Neog 2016). The studies carried out in the early 2000s (including ours) show that men employ informally more often than women (Varshavskya, Donova 2003, p. 45; Tarasova 2004, p. 214). This gender difference remained in the 2006 study: the informal employment among men was 1.4 times higher than among women. However, the difference almost disappeared by 2008 (it was less than 3%), and in 2016 the proportion of informal employment between men and women became the same – 11%.

People under the age of 25 (18% of all working young people) and over 50 (14% of the whole group) are more often involved in the informal employment. The spread of informal

employment among other age groups is within 9%. The higher involvement of extreme age groups can be explained by the following reasons. Young people do not have work experience, what can be an obstacle to getting an official employment. In addition, the issue of forming a future pension, as one of the main advantages of official employment, is less actual for young people, what increases the willingness to work not officially. Older people are being squeezed out of the formal labour market, but to ensure a more or less acceptable standard of living, many of them try to work anywhere, even without proper registration of their activity.

Young people employ informally the most because, on the one hand, lack of experience makes their formal employment difficult, on the other hand, the formation of a future pension, as one of the main benefits of the official employment, is not a matter of a great importance to them. Older people evicted from the official labour market try to earn money just to provide a decent living standard and usually do not conclude the labour contract.

The level of education varies significantly in the groups of respondents with formal and informal employment. People with high level of education generally conclude the labour contract. Among the informally employed, 6% have higher education and only 2% have a postgraduate education (for comparison: 11% of respondents are employed informally), according to the 2016 survey.

The informal employment is generally associated with poverty and infringement of employee's rights. So, it is hypothesized that the informally employed persons estimate their financial standing and social feeling lower than the formally employed ones. However, this hypothesis has not been confirmed. This is due to the fact that the composition of informal workers group is not very homogeneous and includes not only low-status workers whose rights are discriminated, but also high-status employees who consciously choose informal employment for tax evasion.

The analysis showed that there is no statistically significant difference between employees with different types of employment. They estimated their social feeling equally by such parameters as: financial standing, life satisfaction, social optimism, safety, consolidated indicator of social feeling. The informally and formally employed people answer the question "Have your right to labour ever been abused?" in the same way. It's surprising because informal employment itself can be seen as an infringement of rights. The informally and formally employed equally often face an infringement of rights (27% in both groups). And 65-66% of respondents have never been abused in their rights (again, the situation is the same

in both groups). Both groups of respondents estimate the importance of respecting the right to labour in the same way (88-89%). This situation is connected with blurring of boundaries of formal and informal employment in Russia. An employee reports the violation of his rights not when there is a violation of the requirements of the labour legislation, but only when the employer ceases to comply with the initial agreement with the employee. As S. Yu. Barsukova has noticed, the agreement between the employer and employee does not always determine the real conditions of the labour transaction. External formal hiring can be informal in its nature. The likelihood of compliance with the terms of the original agreement (formal written or oral informal) is virtually independent of the degree of formalization of the labour transaction. In the case of oral hiring, the terms of the contract compliance are observed at least as often as in the case of a formal contract (Barsukova 2003, p. 4-8).

The informally employed population is diverse, so the use of averaged estimations is not representative. The cluster analysis identified two groups of informal workers different in their structure and characteristics. The first group consists of people from 25 to 40 years of age who are the entrepreneurs, business leaders, highly-qualified professionals, self-employed with the high level of education. So, their financial standing and social feeling are considerably higher. The second group consists of employees of middle and low qualification who do not have higher education. Exactly this group of people is the most vulnerable on the labour market: they are 1.5 times more likely to face the infringement of the right to labour, comparing with the "informals" of the first cluster. This group of informals shows a low level of trust (Figure 1) to the employers, the business community and the state's institutions.

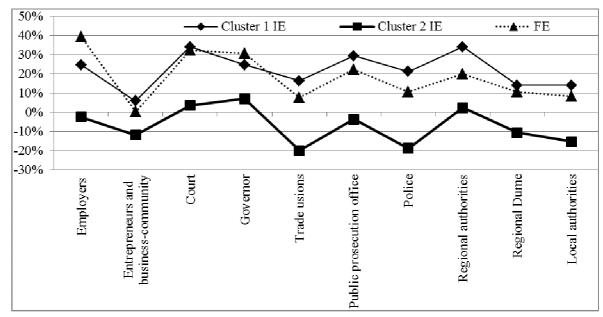


Figure 1. The level of trust\* to the employers, the business community and the state's institutions among groups of informally (IE) and formally (FE) employed people

Notice: \* The trust level is calculated as the difference between the trust and the non-trust shares (%) Source: survey research.

It has been hypothesized that informal employees are more active on the labour market. However, the market motivation characterises only more educated informals: 28% of them are ready to become entrepreneurs (and 15% among formally employed). Low-skilled informals (cluster 2) are motivated to have a small but constant earnings and more spare time (28%).

During the research, one has put forward a hypothesis that informally employed workers will most often demonstrate motivation to work of attainable type. The results show that the motivation for achievement is characteristic only for educated informally employed employees: among them almost every third (28%) is ready to have their own business and to lead it at own risk (among officially employed 15%). But among the low-skilled informally employed workers (2nd cluster), the avoiding failures motivation predominates. 28% of the informally employed workers agree to have a small but constant earnings and more free time.

The need for money is considered to be the cause of the employees' involvement into the informal economics. However, by analysing the respondent's answers, the focus moved from the need for money to the distrust to the state's institutions and the unimportance of the social guaranties. V. Gimpelson and R. Kapelushnikov argue that the distrust to the formal institutions, the dissatisfaction with the quality of regulation and the absence of the unified rules of the game provoke the growth of the informal employment. Nevertheless, this relation is bilateral: informality encourages the institutional erosion (Gimpelson, Kapelushnikov 2014,

p. 8). The formal and informal employment are interdependent and their relations are complicated and miscellaneous. Therefore, the formal labour market may suffer in case we put a pressure on the informal one (Gimpelson 2013). But it is not taken into account the state employment policy.

As a result of the informal employment growth, there is a significant underfunding of the state's budget. Therefore the state is in search of the combat measures. Nowadays, in Russia there is an administrative liability for evasion of conclusion the labour contract: from 10 thousand roubles for self-employed entrepreneurs to 100 thousand roubles for companies. If the employee breaks the law again he will be fined 5 thousand roubles. E. Malysheva said: a set of measures is developed to formalise the self-employed. It is stated that the Ministry of Labour and Social Affairs managed to formalise more than 2 million people in 2015. However, the Rosstat claims that the share of the informally employed increased from 20,8 to 21,2% in one year (Malysheva 2016). The government's regulation is ineffective.

#### **Conclusions**

Despite all of the government's efforts, the informal labour market in Russia is still growing. The difference between formal and informal employment is not clear. The formal employment does not always guarantee the respect for the rights of employees; however, informal employment is not necessarily mean that the employees are deceived. Between the formally employed and informally employed workers there is no statistically significant difference in the assessment of violations of their labour rights. Employees usually consider their rights not being abused if the personal agreements with the employer are compiled regardless of whether these agreements meet the requirements of the law or not. The absence of the labour contract is usually viewed not as a breaking of the law but an everyday practice (perhaps not what the employee wanted, but what he is familiar with).

The informal labour market is heterogeneous and its parts vary greatly in their demographic characteristics. For some, illegal employment means the reduction of income and the absence of social guaranties, yet it serves as a peculiar protection from unemployment and greater need. For others, it is an opportunity to develop their business when the government regulates the market too strictly. As soon as the business becomes successful they give it a legal basis. Thus, on the one hand, informal employment helps people to adapt to new economic conditions, on the other hand, it destabilises the society and doesn't give a new market system a chance to strengthen.

The current Russian state's policy restrains the growth of the most effective sectors, hinders competence development, worsens the future of the economics which increases employee's economic uncertainty and supports the existence of the informal labor market. The government continues to regulate the labor market using such administrative measures which have proved to be ineffective. That is why the government's regulative measures have often adverse social and economic consequences.

The hypotheses put forward by the research are not confirmed if we consider the set of informally employed workers as a whole. There are no statistically significant differences between informally and formally employed in any of the positions considered. However, if we divide the informally employed workers into two clusters (informally employed with a high status and with a low one), then these differences are immediately clearly manifested. The assumptions claiming that informally employed workers have a lower level of education, a lower level of social well-being self-esteem and financial position are characteristic only for a cluster of the low status informally employed. This cluster includes the most discriminated and vulnerable groups in the labour market (young people, older people, wage workers with low qualifications and no higher education). But the motivation for attainable type work is more typical for a group of high status informally employed (entrepreneurs, self-employed and professionals with a high level of skills and education in active working age). This is what significantly differs them from both: the low status informally employed and formally employed employees.

The work was supported by the Russian Foundation for Humanities Fund, a project No. 16-030-00500. Tyumen State University.

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