ევროკავშირი საქართველოსთვის
The European Union for Georgia

TWINNING

GEOSTAT
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STATISTICS DENMARK

Twinning Project

Strengthening the Capacity of the Georgian Statistical System

Component 2: "Enhancing methodological soundness in the National Accounts in line with the EU standards"

Sub-component 2.4: "Evaluation methods of non-observed economy"

MISSION REPORT

Activity 2.4.A "Assessment of current state of play and method selection"

Mission carried out by
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February 24th – February 27th 2020

Version: Final

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1. General comments

This mission report was prepared within the EU Twinning Project "Strengthening the Capacity of Georgian Statistical System". This was the first mission within the sub-component 2.4: "Evaluation methods of non-observed economy" and was mainly devoted to Assessment of current state of play and method selection.

The purpose of the mission was to present, discuss and work on the below mentioned subjects:
- ➢ Overview and assessment of currently used methods for measuring non-observed economy (NOE);
- ➢ Identifying possible areas of NOE in the country by NACE rev. 2 activities;
- ➢ Identifying relevant methods for measuring NOE by NACE rev. 2 activities in the country;
- ➢ Preparatory works for the special surveys in Education and Real estate activities.

The consultants would like to express their gratitude to all officials and individuals met for the kind support and valuable information which they received during the stay in Georgia and which highly facilitated the work of the consultants.

The views and observations stated in this report are those of the consultants and do not necessarily correspond to the views of the European Union, GEOSTAT, Statistics Denmark, or other statistical institutions involved in the implementation of the project.

2. Assessment and results

At the beginning of the mission it was agreed to introduce Eurostat Tabular Approach with N1-N7 non-observed economy categories in Georgia. The Eurostat Tabular Approach contains following NOE categories:

N1. Producers deliberately not registering – underground;
N2. Producers deliberately not registering - illegal;
N3. Producers not required to register;
N4. Legal persons not surveyed;
N5. Registered entrepreneurs not surveyed;
N6. Producers deliberately misreporting;
N7. Other statistical deficiencies.

N1. Producers deliberately not registering – underground

Definition: Producer deliberately does not register to avoid tax and social security obligations. Most often, this refers to small producers with turnovers that exceed thresholds levels above, which they should register. They are non-registered small producers avoiding registration not to lose social benefits, not to pay taxes and social and health insurance contributions. They are found in the area of small crafts, maintenance, repairs and construction activities.

Assessment: GEOSTAT presented estimation procedure of the Labour Input Method (LIM) and all data sources used. Main data source for the LIM are the Labour Force Survey (LFS) and Structure Business Statistics (SBS) and other data sources for demand side of labour. Discussion started with the LFS, where expert from the Social statistics responsible for the survey was invited. She described the methodology of the LFS: questionnaire, survey sample, response rate and calibrations. LFS is conducted according to ILO methodology since 1998. Until 2016 the LFS was integrated into HBS (sample size 3500 households). Since 2017 the LFS is a separate survey, there is a new questionnaire and survey methodology from 2020 and onwards. Currently sample size is 6000 households where 25% of the sample is changed every quarter. Discussion continued with the Demography expert, who explained current approach for population statistics

which is important for LFS coverage. Then the SBS expert was asked for all available data about employment from this survey and way of calculation of full time equivalent (FTE) data.

Results: Current LIM approach cover only employees, self-employed persons are not taken into account. Comparison is made with different employment concepts (national vs. domestic). Institutional households are not covered by LFS data (missing employment in comparison). In the LFS data are women on maternity leave, should be deducted in LIM. Secondary jobs are included in LFS data but as number of jobs without calculation into FTE.

N2. Producers deliberately not registering – illegal

Definition: Producers deliberately does not register as a legal entity or as an entrepreneur because it is involved in illegal activities. Type N2 excludes illegal activities by registered entities or entrepreneurs that report (or misreport) their activities under legal activity codes. They are non-registered units, because their business is out of the law (drug trade, sex-business, illegal production of alcohol and cigarettes, smuggling of goods).

Assessment: GEOSTAT described methods for estimation of main illegal activities with highest impact on GDP (drug trade, sex-business). Smuggling of alcohol and cigarettes are missing. There is a space for improvement of current results. Main data sources for drug trade estimations available on internet were presented (www.emcdda.europa.eu and www.unodc.org). The non-profit organisation Women for freedom, which helps to sex-workers in Georgia, could have possible information for estimation of sex-business.

Results: Arrangement of meetings with experts from organisations the Alternative Georgia (https://altgeorgia.ge/) for estimation of drug trade and from the Woman for freedom (https://www.nswp.org/members/europe/women-freedom) for estimation of sex-business will be necessary on next mission.

N3. Producers not required to register

Definition: Producer is not required to register because it has no output for market. Typically these are household producers that engage in production of goods for own consumption, for own fixed capital formation, and construction of and repairs to dwellings. Or, producer has some market output but it is below the level at which the producer is obliged to register as an entrepreneur. They are non-registered units. The category contains: informal sector, individual housing construction, own-account production of agricultural goods.

Assessment: It seems that the agriculture production is fully covered. Concerning individual housing construction (IHC), GEOSTAT conducted special survey which is base for IHC. Estimation method is established, only margins are not applied properly.

Results: Estimation of the IHC should be improved on next mission. Data about household production for own final use from agriculture and processing of the agriculture production should be compared with the Household Budget Survey (HBS) data on next mission.

N4. Legal persons not surveyed

Definition: Legal persons not surveyed due to several reasons such as: the business register is out of date or updating procedures are inadequate; the classification data (activity, size or geographic codes) are incorrect; the legal person is excluded from the survey frame because its size is below a certain threshold etc. This leads to (systematic) exclusion of the legal person from surveys when in principle they should be included. It's about

the non-coverage of the Business Register. They are registered units. It's about the quality (updating) of Business Register. It contains active units not surveyed due to an insufficiently update register.

Assessment: Discussion shows that the statistical registers are regularly updated.

Results: There is no need for other adjustment.

N5. Registered entrepreneurs not surveyed

Definition: Registered entrepreneurs may not be surveyed due to a variety of reasons: the statistical office does not conduct a survey of registered entrepreneurs; the registered entrepreneur is not in the list of registered entrepreneurs available to the statistical office, or if available, is systematically excluded from it; the registered entrepreneur is not in the survey frame because the classification data (activity code, size code, geographic code) are incorrect. It's based on decision of individual national statistical institutes, which activities are not observed by surveys (e.g. "free jobs" like: actors, sportsmen's, journalists).

They are registered natural persons engaged in arts (sculptors, painters, writers), journalists, professional sportsmen and in other, less frequent freelance occupations. Natural persons with incomes from the author's royalty or rent.

Assessment: Seems that free jobs are not included in statistical registers. Further discussion with Tax Authorities is needed if data about their incomes are available in Tax Declarations.

The main discussion was about missing incomes from renting of dwellings. GEOSTAT is ready to establish special survey and results will be available in the second half of the 2020. In this case, instead of random sample survey it was recommended to do a quota sample based on census data about rented apartments or snowball sampling. The purpose of the survey should be collect information about rental prices, not data about share of rented dwellings (or amount of rental output). Rental prices can then be used both for estimate of rental and imputed dwelling services.

Results: Arrangement of meeting with the Tax Authority experts for clarification of the "free jobs" current tax practice will be necessary on next mission.

N6. Producers deliberately misreporting

Definition: They are registered units. Gross output is under-reported and/or intermediate consumption is overstated, in order to evade income tax, value added tax (VAT), other taxes, or social security contributions. Misreporting often involves maintenance of two sets of books, payments of envelope salaries which are recorded as intermediate consumption; payments in cash without receipts, and VAT fraud. It's about misreporting of the declaration of taxes (intentional distortion of tax reports). It contains the under-reported amount of income and the over-reported amount of expenses.

Assessment: GEOSTAT presented current approach and need to update weights for misreporting. The source of currently used weights is unknown. GEOSTAT is using many special surveys to collect data about misreporting in selected activities. These surveys only copy questions from HBS and differences are considered as misreporting of the data. In fact differences could represent only different sample and grossing up of the results. There is room for improvements with more appropriate methods.

Results: Arrangement of meeting with the Tax Authority experts for possible cooperation with the N.6 estimation will be necessary on next mission. The survey "Expert opinion about intentional distortion of business accounting" between tax auditors and bookkeepers will be prepared on next mission.

N7. Other statistical deficiencies

Definition: Type N7 is subdivided into N7a – data that are incomplete, not collected or not directly collectable, and N7b – data that are incorrectly handled, processed or compiled by statisticians. The following areas should be investigated: handling of non-response; production for own final use by market producers; tips; wages and salaries in kind; and secondary activities.

They can be found by register units and these contain: tips, wages and salaries in kind (benefits provided to employees for free or reduced price in case these benefits are main production of the unit).

Assessment: There are no methods used in Georgia.

Results: We agreed create at least methods for estimation of tips.

3. Conclusions and follow up

The assessment of the current NOE estimations in the NA department in the GEOSTAT was done. Main recommendations for future NOE estimations are:

➢ It is recommended to use proven methods for estimating N.1 and N.6 NOE categories in all economic activities rather than concentrating all types of NOE by one activity. This is time-consuming and it can be done in detail once the estimations of NOE categories (N.1-N.7) in general are established.

➢ GEOSTAT already prepared household surveys for NOE in Education and Real Estate activities. The field works are planned in 2nd quarter 2020. However, it's experimental focus for small part of economy only. These surveys don't address the individual NOE categories and they may result in overlap and double couting. Moreover, such surveys are time, capacity and financially demanding. For future development, it's recommended to use all capacities, which are invested in the new separate surveys, into improving the current household surveys (e.g. HBS). Finally, there will be a decrease in the response burden and financial savings. The improvement of the household questionnaires for the NOE reasons should be done in accordance with the project activity 4.2.C (reduction of very extensive questionnaires for households surveys and concentration of the questions for relevant use).

Actions needed for moving forward:

Action	Deadline	Responsible person
Arrangement of the meeting with experts on illegal activities (for N2)	Before the Activity 2.4.B	GEOSTAT NA Department
Arrangement of the meeting with Tax Authorities experts (for N5 and N6)	Before the Activity 2.4.B	GEOSTAT NA Department
Research in internet available data for illegal activities estimations	Before the Activity 2.4.B	Mr. Kermiet Mr. Vopravil
To conduct special survey on NOE in Education	Before the Activity 2.4.C	GEOSTAT NA Department
To conduct special survey on NOE in Real estate activities	Before the Activity 2.4.C	GEOSTAT NA Department
Proposal for additional questions on NOE in existing household surveys (HBS etc.)	Before the Activity 2.4.C	Mr. Kermiet Mr. Vopravil

Plans for future works (in accordance to the main objectives of the sub-component 2.4):

Activity 2.4.B: Further preparation of identification and methodological documentation
- ➢ Continued discussion on NOE categories in activities of NACE rev. 2 revealed during 2.4.A
- ➢ Preparatory works for identifying and systemizing NOE according to Eurostat's Tabular Approach to Exhaustiveness
- ➢ Meetings with illegal activities experts (drug trade, sex-business, smuggling) and Tax Authorities experts
- ➢ Data collection for the LIM, illegal activities
- ➢ Description of methodology for estimation of N.3, N.5 and N.7 in Georgia
- ➢ Preparation of survey on N.6
- ➢ Proposed date: 2 STEs x 5 working days between July 20th and July 24th 2020

Activity 2.4.C: Analysis of progress in special survey and preparation of methodological documentation
- ➢ Preparation of methodological documentation regarding methods used for measuring non-observed economy in the country, according to the tabular approach of Eurostat
- ➢ Analysing progress of conducting special surveys regarding measuring non-observed economy
- ➢ Calculation and analysis of LIM
- ➢ Estimation of N.2 (illegal activities)
- ➢ Estimation of N.3 and N.5
- ➢ Description of methodology for estimation of N.1 and N.2
- ➢ Proposed date: 2 STEs x 5 working days between August 31st and September 4th 2020

Activity 2.4.SV: Study visit to get inspiration from MS experience
- ➢ Study visit to the Czech Republic to gain insight into the estimation of NOE and the method of evaluation of NOE in the Czech Republic
- ➢ It will be decided whether a study visit is needed on sub component 2.4 or not. A possibility is that subjects under sub-component 2.5 and 2.4 are discussed on the same study visit
  Proposed date: 5 persons x 3 working days + 1 RTAA/Interpreter (the date will be decided after COVID-19 situation)

Activity 2.4.D: Additional mission for finalizing of NOE estimations (proposal)
- ➢ Final estimation of N.6
- ➢ Recording of all NOE estimations into the NA system
- ➢ Final methodological description of all NOE estimations in Georgia
- ➢ Proposed date: 2 STEs x 4 working days in 1st quarter 2021 (preliminary proposal)

Annex 1. Terms of Reference

Mandatory results and benchmarks for sub-component 2.4:

- Evaluation methods of non-observed economy improved

Indicators of Achievement (baseline and targets):

- Availability of an estimation framework according to NACE 2 as an internal tool
  - **Baseline:** 2019 – Estimation framework of non-observed economy according to NACE 2 not available
  - **Target:** December 2020 – Framework for estimating non-observed economy by sector according to NACE 2 available

Activity 2.4.A "Assessment of current state of play and method selection"

1. Purpose of the activity

To present, discuss and work on the below mentioned subjects:

- Overview and assessment of currently used methods for measuring non-observed economy;
- Identifying possible areas of non-observed economy in the country by NACE rev. 2 activities;
- Identifying relevant methods for measuring non-observed economy by NACE rev. 2 activities in the country;
- Preparatory works for the special surveys in Education and Real estate activities.

2. Expected output of the activity

- Possible areas are identified and needed actions for measuring non-observed economy are planned;
- Questionnaires for the special surveys in Education and Real estate activities constructed;
- Sampling methodology for the special surveys outlined;
- Mission report written;
- ToR for next activity prepared.

Annex 2. Persons met

Geostat
Mr. Levan Karsaulidze, Head of National Accounts Department
Ms. Tinatin Papiashvili, Quarterly Accounts Division, National Accounts Department
Ms. Irma Gvilava, Head of Labour Force Division
Ms. Tinatin Ksovreli, Business Statistics Division
Ms. Lia Dzebisauri, Deputy Executive Director

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