

***Irina Mazur***

Entrepreneurship Department  
Taras Shevchenko Kyiv National University

# **Institutionalization of shadow economy in Ukraine**

## **Introduction**

Shadow economy as a component in the economy of any country that does not fit the idea of legalized normal interaction of economic entities, which combines high-quality diversified activities – fully or partially vacant formal norms of economic fixed contracts and uncommitted statistical records. That is, it is the economic reality that is not subject to formal economic rights, as submitted by the laws that apply to all agents of economic activity and contracts relating to only the participants of separate agreements, but objectively exist. “The order may mean the one hand, this system of relations that established standards as required, on the other hand, the structure of relations, which is observed as empirically-effective. In the first case the order – a legal term, in the second case – a real time series“ [Way to the evidence 1998]. This suggests that “light” and “shadow” are always near.

## **Literature background**

Theoretical and practical aspects of problems and development of the shadow economy as domestic researchers examined: A. Bazyliuk, V. Bazylevych, A. Baranovsky, V. Borodyuk, Z. Varnaliy, V. Mandybura, O. Turchinov and others, and foreign scientists: P. Gutmann, E. Feig, S. Yechmakov, T. Koryagina, Y. Latov and others. Analysis of scientific papers mentioned authors can conclude that the lack of methodological basis of this problem.

## **The aim of the study**

Our task is to reveal the causes of institutionalization of shadow economy in Ukraine.

## Methods of the study

For achievement the task of the study in the work are used general scientific and special methods for learning appearance and presses in a sphere of shadow economy. A unity of general and partial is in universal reasons of shadow economy. Historical genetic methods allow see an evolution of views on shadow economy as a regular process. Systematic process gives a possibility to study a shadow economy like emerdzhentist of Market State. Due to synergetic methods is proved self reproduction and self organization of shadow economy.

## Main text of the study

Shadow economy is a complex and multifaceted category, because in the history of scientific thought some of her party at a certain stage of historical development found its reflection in the writings of philosophers, sociologists, lawyers, psychologists, economists, political scientists and politicians.

The first attempts at understanding the roots gnosiological shadow economy have a place already in the works of ancient Greek philosophers (Xenophon, Plato, Aristotle), who believed that the economy based on ethical and religious restrictions and prohibitions is divided into fair and unfair economy becomes hremastixs by “destructive” influence of money that in the modern sense can be interpreted as the concept of “shadow economy”. But it was only the first attempt.

B. Mandeville was the predecessor of this current economic theory, an economic theory of crime and punishment, which in the second half of the twentieth century invited Nobel Prize laureate G. Becker. The main problem is grounded B. Mandeville – immoral actions of individuals may be a basis for welfare of society as a whole, later acquired the name “paradox Mandeville”. He concluded that the criminal wish for greed and normal market economy have the same origin, so their elimination is not possible without ruining the economy. G. Becker, exploring the economic theory of crime and punishment, analyzes the causes, nature and socio-economic impact of the underground (criminal) segment of the shadow economy.

Printed in 1989 Hernando de Soto monograph [1995] has made a revolution in attitudes and foreign researchers on the role and importance of the shadow economy in the modern market economy. That concept de Soto has identified a new paradigm of the theory of the shadow economy in the economic literature. It is based, so to speak, on the synthesis of traditional and new institutionalism. Its essence is that shadow economy can be seen as a manifestation of certain

general patterns that are evident in some of “folk” forms of capitalist enterprise. The reason for this display is the differences between the costs of enforcing the law “and” cost illegal. Typically, costs illegal is much smaller and therefore more profitable to engage in shadow economic activities. “Our research – writes. De Soto – shows that Peruvians readiness to act outside the law is largely a result of rational ... estimate costs law-abiding” [Other way. In risible... 1995, p. 178].

We believe that shadow economy consists of three structural elements: the informal economy, hidden economy and the underground (criminal) economy.

The informal economy is a segment of shadow economy, that is allowed, but not formally registered, hence not included in the statistical reporting economic activity. Its combine with home economics.

The hidden shadow economy includes legal economic activity, which is partially or not recorded in statistical reports, and hence by hiding evading income taxes.

Clandestine or criminal component of the shadow economy – the implementation of prohibited activities. Clandestine or criminal economy belongs to a separate legal unit of research.

Each of these elements has its own structure forming subjects and objects. Collection and correlation of these structural elements, partitioned into separate components based on various criteria, a system which helps reveal the meaning of the term “shadow economy”.

Subjects of shadow economic activity – is the same rational actors seeking to maximize profit under conditions of limited resources. The difference between legal entities and of shadow economic activity is such a thing as the probability of being punished for deviant behavior.

The objects of shadow economic activity may be all legal economic activity. However, you can select the most typical areas of economic activity where more actively thriving informal economic activities.

These include:

- Productive and distributive activities, including productive capital;
- Investment activities;
- Banking, stock exchange activities, insurance activities;
- Resources mining and distribution activities;
- Service – in the sphere of education, medicine and so on;
- Any mediation and more.

Summarizing it should be noted that all components of the organizational structure of modern shadow economic activity have a complex structure of interdependencies, which essentially is the system factor of shadow economic activity.

To characterize the structure of the shadow economy allocate their criterion (Table 1).

**Table 1**

Classification of shadow economy by the nature of its subjects

Parts of the classification	Features of the shadow economic activity		
Nature	Informal economic activities	Hidden activities	Underground economic activity (Criminal)
Aim	Sometimes the purpose is related with survival	The purpose related to surviving and development	Directional own business for enrichment
Motive	Optional	Forced	Deliberate
Consequences	Safety implications	Illegal, but not a significant threat to society	Antisocial has a criminal nature, is dangerous to society

Source: Made by author.

First place by shadowing the list of countries, following F. Snyder and take the economy of Georgia, Ukraine, Russia, Latvia and Estonia. For comparison: the shadow economy in Ukraine makes up half of all farms in Poland – a nearly 30% of the economy. So Poland today at the rating of the World Bank opens twenty countries, where most of the “shadow”. Interestingly, the lowest turnover in the informal economy are Switzerland – only 8.4% and the USA – 9%. And even in the richest countries of the Organization for Economic Cooperation and Development (OECD), the shadow zone on average 18.7% of GDP. In the eastern region of Europe – 38%. Experts believe that the shadow economy will continue to spread<sup>1</sup>.

The World Bank’s study, published in 2010 *Shadow Economies All Over the World*, shows the increase in shadowing in Ukraine over the past 10 years from 51.7 to 58.7% of GDP [Golovin 2010 – Table 2].

Given the above dynamics of the shadow economy, there is a lawful question: “What ensures the growth of shadow economy in Ukraine’s GDP?”.

The main factors determining the existence of the shadow economy in Ukraine include:

1. Ineffective state regulation of economic processes.

One reason for the spread of the shadow economy in Ukraine is the inconsistency of system transformation processes. Formation in Ukraine massive shadow over the years of independence largely provoked the loss of state levers of ef-

<sup>1</sup><http://pressa.obozrevatel.com/info/438417.htm>

**Table 2**  
Shadow and the official economy of Ukraine

Years	The volume of the official GDP billion grn.	The percentage of informal sector GDP (%)	The volume of the Shadow economy, billion grn.
1999	130.44	51.7	67.43
2000	170.04	52.2	88.76
2001	204.19	53.0	108.22
2002	225.81	53.7	121.26
2003	267.34	55.0	147.04
2004	345.12	55.9	192.92
2005	441.45	57.0	251.63
2006	544.15	57.5	312.89
2007	720.73	58.15	419.11
2008	948.06	no data	
2009	912.56	no data	
2010	1095.0	no data	

Source: State Statistics Committee of Ukraine 2010, the World Bank.

fective regulation of economic processes, deficiencies in the economic and legal policy, including the poor state of economic legislation.

Under conditions where state regulatory policies are contrary to the interests of important groups of economic subjects, the shadow economy is on the field and scope of activity and acquires mass expression. Economic actors, guided by their own interests, searching for more favorable ways to use the resources available to them, including going beyond existing legislation. This encourages them to establish new rules for conducting business transactions in which the regulating and controlling role of the state is gradually replaced by informal agreements between them.

The overarching result of a long period of poor economic governance process was the destruction of the institutional environment which determines the basic norms of conduct and public entities to other entities, partners, suppliers and customers, and state regulators.

## 2. Not banking currency.

According to different estimates in Ukraine rotates from 10 to 20 billion dollars from here it becomes evident that the shadow area of payment deficit does not feel. No problems here with timely payments. Therefore, the shadow economy becomes more attractive for entrepreneurs versus legally.

### 3. The inefficiency of the tax system.

Experience shows that Ukraine has failed to create an efficient tax system. Applicable tax laws of Ukraine do not stimulate economic entities to invest money in legal economy. Experts estimate that the overall tax burden in Ukraine is almost twice the figure in the group of countries to which it belongs in terms of GDP per capita, and that just stimulates the beginning of the “shadow”. Violations and abuses in the tax system has become almost the most important disaster for the budget system.

Using tax breaks as a powerful lever of economic regulation in the world, in Ukraine they are still one of the mechanisms of accessing the “shadow”. The tax burden among the subjects of economic activity is distributed unevenly, which also contributes to the possibility of the entities to evade taxes.

Exemption of certain companies or products from tax in a massive scale resulted in a significant redistribution of tax burden on the legally operating entities. Law Abiding Taxpayer, which provides budget revenues, welfare driving in shadow or ruins.

Tax credits are generally not stimulate either growth or investment and innovation processes.

### 4. Gaps in the budget system, inadequacies in budget planning and controls over the use of public funds.

The main drawback of the budget process, which creates conditions for outflow of funds in the shadow area are:

- Unsatisfactory level of revenue and justification of budget expenditures;
- Violation of the law in the formation and implementation of the State Budget of Ukraine and local budgets;
- Imperfect mechanism for the supply of the planned budget allocations;
- Lack of control over budget expenditures and accountability in all levels of the government of targeted and effective use of budget funds;
- Lack of transparency of the budgets of all levels.

Experts estimate that the loss of state revenues in the shadow of the public sector annually exceed 12–13 billion<sup>2</sup>.

Ineffectiveness of fiscal policy and fiscal system in Ukraine reduces readiness and public entities to pay taxes because of uncertainty in the productive and target their use.

---

<sup>2</sup>*About internal and external situation of Ukraine in 2003 year.* The President’s message to Verchovna Rada of Ukraine. Part. Strategy of withdrawal from shadow of Ukrainian economy. Derzhkomstat of Ukraine, 2004, p. 149.

5. Disorganization and economic management of state property and state enterprises, inefficient state property privatization.

Shadow sector by exploiting the assets, in particular – fixed assets, accelerating wear it without further compensation. This deprives the state related revenues – amortization.

Typical schemes of abuses associated with the use of state property are:

- Reduction of state stakes in joint stock companies by issuing additional shares;
- Artificial payable, bring enterprises into bankruptcy following their purchase at prices that are significantly below market;
- Forced sale of property companies;
- The Company – “clone” of the following appropriation of her liquid assets and profits of parent company from losses leaving the balance of the latter;
- Monopolize the supply of raw materials and sell finished products intermediary structures;
- Non-fulfillment of investment obligations and more.

It is widely used imperfection of the current relevant legislation:

- Blocked by the general meeting of shareholders, including through the mechanisms injunctions;
- Competitions contested in courts by individuals, including those that have no relation to the undertaking;
- There are cases by courts opposite decisions on the same dispute;
- Registrar and management companies deliberately delayed the transfer of ownership of shares and so on.

Is not the best state and corporate administration in the national (public) joint stock and holding companies. Managers of large public companies are actively collaborating with commercial entities, assumed various violations of law, falsifying reports and more.

The quality of corporate owned by the state, remains low. Flaws of the management of public property used for shady businessmen alienation of state property and the withdrawal of income from use of shadow turnover.

Therefore necessary to ensure the proper management of state property privatization process and bring into line with state interests. Solving this problem is possible under laws on holding companies, joint stock companies, state property management and more.

6. Corruption in the executive branch and local government, legal insecurity entities from arbitrariness and abuse of officials.

The majority of Ukrainian and foreign experts, corruption is one of the main problems affecting the economy of Ukraine and remains one of the biggest obstacles to its integration into the global community, civil society development.

In terms of national security corruption as a mass phenomenon is a real problem for the whole country, directly affecting its internal processes and external relations, creating conditions for social upheaval with unpredictable consequences.

We believe this institution shadow economy, which is more efficient, creating more favorable conditions for solving economic problems than through legal institutions, which are accompanied by high costs.

Recognizing that most of the problems associated with studying the shadow economy, correspond with uncertain methodological framework to analyze it believe that it is time to consider the shadow economy in terms of qualitative change – the institutionalization of the shadow economy.

According to D. Nort new institutions emerge when society believes that maximum profit can not be obtained under the existing institutional system. In other words, if production factors provide the opportunity to increase revenue, and institutional prevent this, then there are big chances for the emergence of new institutions [Nort 1997, p. 6]. Gives out has indicated the problem may be described as actual and not covered in the literature.

Institutional approach to the analysis of shadow economy in the center puts research system of formal and informal rules of behavior patterns of their development, approved a mechanism for implementation.

In the 70's of the twentieth century. When Western scholars began to study causes and spread of the shadow economy not only in the “third world” but also in developed, it was noted that the stages of initiation and propagation were not certain institutions as special rules of conduct shady business relations system interaction and organizations associated with shadow economic activities. Subjects shadow relations began to seek for themselves such form of activity and behavioral norms that would become for them Best in conducting shady operations.

As an example, take the southern Italy, including Sicily. This region is sufficiently studied by economists and can be used as the most striking example of the emergence and development of shadow institutions, in particular the Mafia. Historically, the minimum impact on the state (first Spanish and later Italian) could not ensure the protection of life of people and their property rights. Hence the need alternative mechanisms of specification of property rights and contract enforcement. During this period the first mention of the mafia as an institution, alternative country-specific and the protection of property rights [Gambetta 1993, pp. 91–97]. “Mafia – a rather special type of behavior and a special type of power relations, not a formal organization” [Arlacchi 1986, p. 16]. That comes to a certain institution as a set of rules that allow individuals to coordinate their activities in economic, political and social spheres. Competitive advantage associated with the Mafia, appearing on the basis of creating local monopolies and limit competition, not because of its action [Arlacchi 1986, pp. 104–108]. Mafia



operates on the principles of flexible and easy to changing conditions around the network (networks) focuses the main economic activities of the Mafia, which uses a high potential of trust between “ourselves” [Kopp 1992, pp. 365–381]. Often descriptions of economic activity using mafia networks (network, “Multi-player relations”), created on the basis of trust in family or family-friendly and client relations (more detail by us in clause 2.1.). Thus, the family remains the foundation for the mafia for any activity, including contract. But this is not about nuclear family, but the totality of relationships built on trust normally localized within the family by family and closest friends, which is called “their”. Therefore, potential partners are divided into “their” and “alien”. In between “their” social operating mechanisms to prevent opportunism, using standards and mutual trust, and to “strangers” opportunism becomes the norm [Olejnik 2002, pp. 172–173]. This is double standards.

Some of shadow institutions gradually died not finding wide support, but some remained, gaining steady character, and were included in the “culture of shadow behavior”. As an example, the kickbacks, invasions, etc. conversion centers.

In the late 80’s of the twentieth century shadow economy of developed countries takes appropriate organizational forms, which led to its special status – social institutions. In the 90’s underground economy gained stability and consistency in its development in Ukraine.

Considering the institutionalization of shadow economy in Russia in the post, and L. Kosals and R. Ryvkina [2001] determined that shady institutions heterogeneous and grouped them into two groups. The first included the institutions that have directly within the legal structures and operate in all spheres (political, legal, economic) of social life in the process of economic reform in the country. The second group included institutions that have emerged as new forms of informal behavior that best satisfy – qualify subjects shadow economic relations.

And R. L. Kosals Ryvkina the first group of institutions shadow economy includes:

- Misuse of funds – directing funds from the state budget for other purposes. These include the use of funds for other purposes, and to overcome some current problems. For example, allocated money for paying teachers to cover the local budget. Or – ordinary theft of public funds and transfer them abroad for their own accounts of officials. This could be a high enough level of efficiency of planning the distribution of public funds and the immorality of certain business executives. From our point of view of this institution can be attributed only to the criminal component of the shadow economy subjects which in any case must bear the punishment;

- Cashless transfer of money in cash. This operation is based on informal agreements with firms to banks, such as wages “in envelopes”; small wholesale purchases and so on. Typically, this operation is to hide income from state enterprises, i.e. tax evasion. Over the years this institution was even set the percentage for payment of services – from 30 to 10% (the percentage reduction depends on the amount of increase), which businesses pay banks for transferring money in cash. It says sustainability and notoriety shadow services [Klamkin 2000].

It turns out that consumers need in the performance of certain functions and services producers pushing for the creation of appropriate institutions shadow not only in economics but also in all spheres of society.

The second groups of scholars include such shady institutions that have their own name and got: “cap”, “hit”, “racket”, “rollback” and so on.

“Cap” – is, so to speak, “authority” (such as include criminal gangs, and legal institutions, such as police), which controls the business activities of one or more firms. In exchange for “representation” in government, they receive a payment from the profits of the firm. In fact, it centers monopoly in the market. Use ROOFS “eliminating a competitor in the market and reduces costs for entering the market”. »Cap« is required to prevent so-called invasion – additional measures of pressure on debtors (competitors). From the economic point of view these institutions suppress incentives for economic growth, the introduction of technological innovation, impede the protection of human owner.

“Racketeering” – this is an informal gathering to “deliver” to entrepreneurs in the form of compulsory deduction of income. This institution shadow economy forces businesses to hide (or reduce) their income from state and, therefore, evade taxes. Otherwise they would be bankrupted. Sometimes it is more profitable businesses than state pay taxes because they just have some “protection”. However, protection from the state they have only conditional.

“Rollback” – fee received as a rule, public order, concessional loans, grants, subsidies, budgetary loans, grants that pay a percentage depending on the size of loans: The more – the greater the percentage, but with a smaller size of funds issued – less percent. In terms of formal rights “rollback” is a form of corruption. Often the “rollback” has the character of sustainable economic relations between officials and businesses or between businesses themselves.

Conversion Centre (KC) – consisting of fictitious (example, dealing with transfer of funds from the clearing account into cash) firms and other divisions. KC managed set of informal rules, first, internal organization, and secondly, interactions with clients; thirdly, relations with authorities of different levels. In order to adapt to conditions that are constantly changing (changes in legislation in the economic situation – inflation, etc.), KC had to change the rules of conduct.

They occurred in three areas: reduction in fees for services, upgrade and expand the range of the past, reducing their risks and risk customers. The current commission rate equal to KC – 4–5% of the amounts received from client accounts KC. These rules ensure the stability of its existence and generate revenue by providing illegal services to customers [Vetkin 2005, pp. 12–19]. So, KC – is a means of tax evasion, and that is the basis of the shadow economy.

An important element of life and self shadow economy is a shadow of its investment mechanism. Typically, he works in the short term, because such investments are latent in nature. Shadow investing mechanism appears in the absence of formal guarantees of effective protection of property rights. The mechanism of shadow is short-term investment at a time when there are new technologies that do not require large investments to quickly create new products, which enjoys high demand in the market, through which you can get much higher income than the competition. Such enterprises are created by small period of time to “skim the cream” on products and do not show their income. Upon receiving them, they disappear.

Corruption as an institution of the shadow economy – widespread phenomenon that affects not only developing countries or in transition, but also the developed world.

Corruption – is the commercialization of their officials duties [Mazur 2005, p. 70]. High level corruption undermines the credibility of economic agents in the state, which in turn negatively displayed at the investment and hence on the level of economic growth.

Corruption is defined as the abuse of public power for private benefit; sale of state property by officials for personal needs, the actions that deviate from the norms of conduct for public servants under the influence of special interests (wealth, power or career); entities that receive payments from individuals or legal entities and private abuse of public property, this obstruction of economic reform and democratization; effective way to overcome the consequences of state intervention in the activity in the free economic agents [Gnatienco, Ledomska 1997, p. 29].

Considering what is the cause and existence of corruption in Ukraine.

Corruption, on the one hand, actually reduces the transaction costs of entities that define the existing institutional framework. This occurs in the form of bribery, bribe to the official when the tax service can reduce the amount of tax payable. Or may occur in the form of extortion – when too high official discretion (to decide at its discretion) or too weak law enforcement mechanisms allow it freely to overstate the transaction costs of economic agents (to the level and which constitute the actual transaction costs according to current institutional framework) and complicate access to this or that good, but that he (the officer) did not, economic agent resorting to bribery.

Given the weak institutional environment, corruption mitigated to some extent possible separate entity as an agent, and the economy. It appears only in the short term, in circumstances where corruption can improve efficiency relative to the economy, ignoring the laws. This is a situation where the passage of a legal procedure is so complicated that only a violation of the law and use of “corruption contracts” is the only option for a successful and quick passage of this procedure or get a permit. However, corruption lowers transaction costs compared to only those actually provided effective institutional framework. However, it minimizes them completely. When other institutional frameworks transaction costs can be significantly lower even without corruption.

In the long run corruption leads to harmful consequences for the economy. It promotes the growth of transaction costs in the economy. If one economic agent bribing transaction costs are reduced, then its competitors, they can significantly improve. On the other hand, corruption contributes to the inefficient distribution of income and resources. Free access to a resource can get someone who will give more bribes. Therefore we are talking about creating additional barriers for other agents in the distribution of resources official. Corruption undermines the budget policy, reducing the effectiveness of budget expenditure [Verestuk 2001, pp. 72–73].

A gift is in turn defined as a tool of corruption through which resolved corrupt deal. Bribe can be in the form of tangible and intangible (service) good.

There are political, economic, cultural and historical causes of corruption in Ukraine.

By separating the notion of political reasons, rights to control rights to the business of money-generating business, which means that the state itself. The existence of their bureaucracy, usually accompanied by corruption. Officials in the fuzzy definition of various legal procedures have to be treated at the discretion of law and for it to receive bribes. Businesses that are paid off, expect a positive resolution of their problems at a time when not as full and unconditional implementation of formal rules [Verestuk 2001, pp. 66–74]. In this regard, absolutely impossible to eradicate corruption. So the question is the level of corruption in society and how it raises (or no) loss of society? In Ukraine, corruption has reached such a state that political power was nayrentabilnishym kind of business. In the ranking for 2010, prepared by global anti-corruption NGO Transparency International, Ukraine has got 134 by level of corruption among 178 countries. These are the results of a study published on TORO, which is the contact group Transparency International in Ukraine. In the ranking, where the corruption level measured on a scale from 0 to 10 points, where 0 means total corruption of the state, and 10 – in fact its absence, Ukraine received 2.4 points (2.2 – in a year 2009), this suggests that Ukraine has a total corruption, says Transparency Inter-

national. While in 2006 Ukraine, with evaluation of 2.8 points, took place 99–104 of 163 countries where research was carried out, in the 2009-meters with a score of 2.2 points Ukraine has already placed at a spot 180 among 146–153 countries. In 2010, the estimate 2.4 Balla, except Ukraine, got another 8 countries: Azerbaijan, Bangladesh, Honduras, Niheryya, Philippines, Sierra Leone, Togo, Zimbabwe<sup>3</sup>.

The economic causes of corruption can be attributed [Mazur 2005]:

- Uneven development of market economy. While strengthening economic crisis such negative phenomena as inflation, unemployment, etc., are favorable conditions for growth of the shadow economy. That is, under these conditions reduced the effectiveness of the regulatory role of the state, leading to growth of corrupt actions of officials;
- The contradiction between the rapidly changing conditions of market economy and law. Gaps are created by such contradictions, shadow filled “game rules”, where double standards are beginning to act through the distribution of population in “their” and “alien”. Through bribes, can be “their” solve many problems. Even in developed countries, economic processes ahead of current legislation. Therefore, improving the legal base should have a permanent character in response to changes in the economy;
- Stratification of society into rich and poor. Due to state property has been enriched a small group of people in Ukraine, which had direct or access to it, or through corruption. Later, the group called oligarchs. Thus, the oligarchs in Ukraine are due to shadow privatization of state property. Business has to become economically strong and independent from government. In Ukraine, yet he lives under the authority of officials.

To cultural and historical reasons, corruption can be attributed to inherited Soviet-era practice of bribery and nepotism (in the west – clientyzma). Bribery and nepotism are deeply rooted in the everyday culture of our society. For example, settling down to work, an official of any level immediately finds himself assistants among relatives, godparents or other “its”. That is so, who did not betray during corruption schemes, as they also are “trusted” party and therefore also have a share in the redistribution of illegal proceeds. Unfortunately, today this practice is rampant.

Thus, the total cause of corruption may be ineffective institutional framework of society. This inefficiency can be both formal and informal rules and their enforcement mechanisms, and total inefficiency of the whole institutional matrix – its relevance to culture and ideology of society.

<sup>3</sup><http://podrobnosti.ua/power/2010/10/26/72606/.html>

We distinguish formal and informal legal as a hidden, forbidden. Meant by informal legal practices, culture, etc., that established historically in certain areas. We believe that this should form the basis of formal. Under the informal or hidden prohibited understand how relationships between officials and “their” in their practice, and legal fine (customized) manufacturing or services which are hidden and not paid income taxes. That is, households engaged in fruitful event of the year – sell their own surplus product, repair of apartments at his free time work, tutoring teachers and so on.

Data on the shady institutions are more indirect, as obtained by interviews with the population, because these institutions are not subject to the formal socio-economic study of latency through their actions, but because – lack of information.

With certain institutional approach to the definition of shadow economy, structuring and classification of the causes of its existence, we can develop an effective system to counter this complex socio-economic phenomenon.

Overcoming high levels of corruption lies in the political sphere required strict control and punishment for corruption and bribery. According to A. Olejnik, punishment costs include two elements: the manifestation of costs and expenses offender punishment of violators. Just the latest deals J. Buchanan as “ungood”. Penalties must be imposed upon («ex post»), although the punishment should be selected – to («ex ante»). In terms of J. Buchanan no punishment can not return full loss does not give a status quo ante [Bubeken 1997, p. 380]. But punishment in his view should be used because they prevent the abuses that otherwise could be taken in the future. Therefore, an effective political regime requires effective law enforcement – not only through effective fear of punishment, but for its inevitability<sup>4</sup>.

Thus, the total cause of corruption may be ineffective institutional framework of society. This inefficiency can be both formal and informal rules and their enforcement mechanisms, and total inefficiency of the whole institutional matrix – its relevance to culture and ideology of society.

We distinguish non-formal and informal legal as a hidden, forbidden. Meant by informal legal practices, culture, etc., that established historically in certain areas. However, should raise the official income level officials, especially those in whose jurisdiction the broad discretionary powers. You also need to eliminate conflicts that are in the legal system, which significantly reduces the possibility to manipulate the law.

---

<sup>4</sup>GRECO: Ukraine made a struggle with corruption. [http://lb.ua/news/2011/05/28/98689\\_GRECO\\_Ukraina\\_provalila\\_recomen.html?print](http://lb.ua/news/2011/05/28/98689_GRECO_Ukraina_provalila_recomen.html?print)

Thus, institutionalization of the shadow economy – is fixing the behavior of subjects in some shadow organization supports forms that are recognized by all parties to such activities.

We have mentioned only some elements of the institutionalization of the shadow economy, yet without their complex research can not fully explore the changes in socio-economic relations in Ukraine.

The shadow economy – a system of relations between economic subjects, which organizes itself, covering all stages of the process of social production to an economic advantage which results or ways to achieve for various reasons or arose or reduced, or totally concealed from both participants, and the law [6].

Taking this approach to determine the shadow economy, the following conclusions:

- Informal economy is part of the socio-economic system;
- The very shadow economy is a system of several institutions that provide its existence. So it must be considered comprehensively, including its institutional environment;
- A system of shadow economy organizes itself, but not self regulating, indicating the necessity and importance not only a comprehensive approach to its neutralization, but the complexity and simultaneity of measures to regulate its volume by the state, as some measures for prevention (eg., reduction) shadow economy can only suspend its operation only to better adapt to specific complications from the state, but does not overcome her;
- If the system of shadow economy as a system of economic relations between economic entities, the sector to reduce the shadow economy to change the system of economic relations;
- If the informal sector covers all stages of social production, the need to develop measures to reduce the shadow component, including production, exchange, distribution, redistribution and consumption.

Based on the definition of “shadow economy”, the reason for its existence is the economic benefit is obtained through concealment or reduction of official indicators of income (profits) from the state. Thus, the object of reforming the social and economic relations should be and ways to get revenue.

Last in the definition of “the shadow economy” is that economic benefit is protected from both direct participants in economic relations and the law. This suggests that changes in the economic relations should be conducted so that they (the relationship) are transparent, possibly with fewer intermediaries and more.

The scale and mass action in the informal sector not only physical but also legal entities can deduce the presence of not only individual difficulties in reforming Ukraine’s economy, but also can talk about the big problem which is the level of confidence of economic agents to such an institution, as a state. Distrust

of the state initiated unskilled and corrupt actions of those who personify a state power – politicians and public servants.

The strategy of building confidence in the state and its representatives and trust between the citizens should include measures of interrelated tasks that can be grouped into two groups.

The first group relates legislative, judicial and institutional problems. They apply in Law in accordance with the norms of democracy and market economy dominated by private ownership. This will ensure confidence of economic agents, protecting citizens from tyranny and corruption of state officials and worthy of trust of its citizens.

The second group includes problems related areas that may be described as ideological and behavioral. The most important of them connected with mentality of people. You must overcome the legacy of the past – in the minds of people formed a strange combination of trust and suspicion. Post-socialist period there was a moral muddle: along with the old, new approaches that absolutely do not mix. Change the mentality of people is unlikely to succeed quickly. This process can only accelerate at a time when the old give way to a new generation whose moral norms and behaviors are composed in a new era, responsible market economy.

24.05.2011 in Strasburg at the Europe's Group of States Against Corruption (GRECO) was announced about failure of Ukraine in the direction of legislative control of corruption and disparity of European Standards of struggle with corruption [Mandybura 2001].

As shown at this meeting in 2009 due to the results of GRECO, Ukraine hadn't unredeemed recommendations. They were fulfilled or in the process of coming to the end. Thought half a year Ukraine became a first Member State of European Anticorruption Initiative, in which experts of GRECO decreased a level of implement recommendation on three positions.

To positive at this meeting were related 4 results of activity of new leadership of Ukraine. Among them were: adoption of statute *About judicial system and judgement status*, making a High Judgement Board of Experts, coming into force of statute *About access to public information*, adoption of new statute *About Government Purchases 2010 y.*, and also through the progress of Ukraine was new statute *About banning and struggle with legalization of money-laundering, which received through criminal case or financing of terrorism*. However GRECO didn't accept these actions enough for anticorruption policy in Ukraine.

All anticorruption documents, which were worked out were blocked and even disavowed.

Complaints, which were lodged by GRECO to Ukraine:



- not shown the system of administrative responsibility for corruption affairs in a such way that corruption could consider as criminal case at the same time;
- Ukraine should increase independence of Office of Public Prosecutor from political impact and specify its authorities, concentrate its on management of pre-trial detection and criminal case;
- Ukraine should provide a responsibility of juridical persons for corruption violation of the law, including effective, proportional and current sanctions and should built a system of registration of juridical persons, who were instituted criminal proceedings (company register, who instituted criminal proceedings). There is one of the main demands of GRECO and one of the main European standards.

More over GRECO not fixed 10 points of anticorruption initiatives. Among them: not accepted model codex of government official conduct and not reconciled a dispute of interests of officials, connected with general family or business interests; not protected rights of intelligencers – officials, who should inform of controlling units about subdivision and some corruption actions of their colleagues etc.

Drago Kosa, head at the meeting in Strasburg, noted only 13 discrepancies with European standards of corruption struggle in Ukraine.

Such an information is an evidence that there are conditions of favorable existence of shadow economy in Ukraine

The current stage of institutionalization of the shadow economy in Ukraine is complex and requires careful while state socio-economic policy. This can “civilize” creating deshadowing economy policy of the State, which should include the following political, economic and legal conditions for business entities that would be much more beneficial for legal economic activity than the shadow.

## Conclusion

Shadow economy inherent in all stages of social development: pre-industrial, industrial and postindustrial. Speaking first as unfair economic activity, the shadow economy was the criterion for religious precepts that understood as the restrictions and prohibitions.

Shadow economy emerged as a hidden economic activity with the advent of commodity-money relations.

Under the new paradigm of shadow economy E. De Soto Industrial Revolution, which marked the beginning of modern capitalist industry, the result can be seen as anti-capitalists “nonconformists” with mercantilism state. Willingness to

act outside the law is the result of the ratio of “cost of implementation of the law” and “out-of legality” in favor.

In the transitional stage of social development business activity increases, but the institutional environment does not meet this growth, including hidden economic activity increases several times. Thus, in transformational economies of the post shadow economy has a large amount, due to the same transformation.

## Literature

- ARLACCHI P. *Mafia et compagnies. L'éthique mafiosa et l'esprit du capitalisme*. Grenoble: Presses Universitaires de Grenoble, 1986.
- BARANOVSKY A. *State economic security*. Financial Ukraine, No 22, 1996.
- BAZILUK A.V., VOLYK V.F. *What does it mean a shadow economy, reasons of appearance and conditions of development*. Organized labour of Ukraine, No 2, 1997.
- BAZYLEVYCH V.D., MAZUR I.I. *Methodological aspects of shadow economy scale valuation*. Economy of Ukraine, No 8, 2004, pp. 36–44.
- BAZYLEVYCH V.D., II in V. V. *Metaphysics of economy*. – K.: Knowledge, 2007.
- BUBEKEN G. *Selection theory. Series: «the Nobel Prize laureate on economy»*. – M.: Taurus Alfa, T. 1, 1997.
- ECHMAKOV S.M. *Shadow economy: analysis and modeling*. – M.: Finance and Statistics, 2004.
- FEIGE E.L. *Defining and Estimating Underground and Informal Economies: The New Institutional Economics Approach*. World Development – Vol. 18, 1990.
- GAMBETTA D. *The Sicilian Mafia. The Business of Private Protection*. Cambridge: Harvard University Press, 1993.
- GNATIENKO G., LEDOMSKA L. *Some aspects and phenomena of corruption and its follow on economy of Ukraine*. Econ. herald, No 9, 1997, pp. 15–31.
- GOLOVIN V. *Shadow from a distance seems bigger* // LB.ua from 6.08.2010.
- GUTMANN P.M. *The Subterranean Economy*. Financial Analyst Journal, Vol. 33, 1977.
- II in I.A. *Way to the evidence: Comp.* – M.: ltd publishing house ESMO-Press, 1998.
- KLAMKIN I.M., TEMOFEEV L.M. *Shadow economy of Russia: Economic – sociological investigation*. – M.: RGGU, 2000.
- KOPP P. *La structuration de l'offre de drogue en reseaux*. Revue Tiers Monde, 1992, Vol. XXXIII, No 131.
- KORYAGINA T.I. *Plan and Market in Soviet economy*. Top secret, No 1, 1989.
- KOSALS L., RYVKINA R. *The Institutionalization of the Shadow Economy: Rules and Roles* // Explaining Post-Soviet Patchworks / K. Segbers (ed.). Pathways from the Past to the Global. – Ashgate Publishing, 2001, Vol. II.
- LATOV Y. *Evolution of investigation of informal sector of economy in abroad*. Shadow economy: economic and social aspects: Problematic subject collection RAN UNION. I.Y. Zhylina (ed.). – M., 1999
- MANDYBURA V.O. *Shadow economy of Ukraine and directions of legislative strategy and its limitation*. – K.: Parliamentary Press, 1998.

- MANDYBURA V.O. *Shadow economy of Ukraine: theoretical methodological aspects of research and problems of practical limitation*. – K., 2001.
- MAZUR I.I. *Corruption like institution of shadow*. Economy of Ukraine, No 8 2005, pp. 68–75.
- NORT D. *Institution, institution changes and functions of economy*. B.Z. Milner (ed.), A.N. Nesterenko (translation from English) – M.: Fond of economic book «Principia», 1997.
- OLEJNIK A.N. *Institutional economy: school-book*. – M.: INFRA-M, 2002.
- SOTO H. *Other way. Invisible revolution in third world*. – M.: Catallaxy, 1995.
- TURCHINOV O.V. *Shadow economy: theoretical basis of study*. – K.: ArtEk, 1995.
- VARNALIJ Z.S. *Shadowing of small-scale enterprise (economic and legal aspects)*. – K.: Institute of Private Law and Enterprise AprN Ukraine, 1998.
- VERESTUK S. *Corruption: definition, reasons of evidence, follow on economy*. Economy of Ukraine, No 3, 2001, pp. 66–74.
- VETKIN A. «*Convervation centrums*»: *institutional features and a role of shadow economy*. Economy of Ukraine, No 8 2005, pp. 12–19.

## **Instytucjonalizacja szarej strefy na Ukrainie**

### **Streszczenie**

W opracowaniu rozpatrywano istotę szarej strefy. Badano różne podejścia naukowe przyczyn pojawienia się szarej strefy i jej instytucjonalizacji. Zostało podniesione pojęcie korupcji oraz poddano analizie przyczyny jej powstania. Zaproponowano również drogi ograniczenia instytucjonalizacji szarej strefy.

