The Grey Economy
2014
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THE GREY ECONOMY 2014

This publication addresses current themes related to the grey economy and its prevention on an annual basis. The 2014 publication deals with different forms of the grey economy, assessing and measuring the extent of it, and recent prevention measures. The case presentation highlights the latest Supreme Court stages of a major trial on false invoicing. The judgements involve tax frauds related to withholding tax and employer social security payments. The decisions are important as preliminary rulings.

The work of the Grey Economy Information Unit reveals many different phenomena. The unit’s purpose is to produce information about these phenomena and look for indicators to assess the size of the grey economy.

One way of investigating the grey economy is to concentrate on the characteristics of certain groups and the incidence of grey economy in them. The target of investigation can, for example, be a specific industry or group of companies or debtors. In addition to the incidence of grey economy, the unit strives to assess the impact of prevention measures and the need for legislative changes aimed at increasing the effectiveness of such measures. The reports show that the probability of grey economy is increased by matters such as missing returns in taxation, business tax debts, certain key business figures and, in some cases, links between the responsible persons of companies and other business. The investigation and measurement of grey economy is addressed in section 2 of this publication.

In practice, the prevention of grey economy aims at ensuring that the financial benefit of the acts is slight, the risk of being caught high and the punishment for the acts involves quick and correctly dimensioned administrative or criminal sanctions. The methods used to reach these targets include legislative changes such as the obligation to provide a receipt for purchases, a tax number and a tax debt register. Recent prevention measures are presented in section 3.

Although the majority of neglect related to the grey economy concerns taxes and other statutory duties, many other authorities take part in preventing the phenomenon. This publication presents the grey economy prevention carried out by the enforcement authorities in section 4.
1. THE GREY ECONOMY – NEGLECT OF STATUTORY OBLIGATIONS

The impact of the grey economy stretches to different parts of society. Ordinary citizens often encounter the grey economy in the form of unreported payment of wages or failure to report income. However, the grey economy is a much broader concept characterised by the neglect of various statutory obligations.

The Act on the Grey Economy Information Unit that took effect at the beginning of 2011 defines the grey economy as follows:

The grey economy means such activities of an organisation in which the organisation fails to meet the statutory obligations arising from its operations so that the payment of taxes, statutory pension, accident or unemployment insurance contributions or the fees charged by the Finnish Customs can be avoided or unjustified refunds received.

According to the definition, the grey economy involves the neglect of taxes and other statutory payments. The definition also covers the neglect of obligations that affect the payment of statutory pension, accident or unemployment insurance contributions or fees charged by the Finnish Customs. Such duties include registration, reporting and payment obligations. They can also affect applications for the refund of unjustified taxes or fees.

As a result of the grey economy, taxes and fees remain uncollected, competition between companies is unfair, employees can be treated illegally, and the tax morale and legal system can generally become weaker.

The majority of neglect concerns taxes and other statutory obligations.

Most cases of neglect corresponding to the definition are, in terms of both number and monetary value, related to obligations monitored by the Tax Administration. Among other things, the Tax Administration handles tax control, collection of taxes and fees, recovery and legal supervision of taxpayers.

Approximately 3 000–4 000 tax audits are performed each year, with 700–800 of these relating to the grey economy. Based on grey economy audits, some EUR 60–70 million in neglected statutory taxes and fees are ordered to be paid each year. In the audits, grey economy is revealed by things such as missing sales, receipts with incorrect content or receipt trade.

The grey economy in the Tax Administration's 2014 customer questionnaire

The Tax Administration carried out a customer questionnaire for its individual and company customers in

The questionnaire for companies was sent to entrepreneurs and management personnel who are responsible for tax matters at companies. According to the responses, nearly one-fifth of corporate respondents (18%) know a company that sells goods or services in a grey manner. The same number of company representatives said they believed that grey purchasing or sales of goods or services is common or quite common among Finnish companies.

Nearly three out of four (71%) corporate respondents reported that the reason for purchasing grey work or services to be the fact that is is common in some sectors. This result suggests industry-specific differences. Other reasons for grey economy activities were considered to be lower costs (66%), a difficult competition situation (40%), and the low likelihood of being caught (33%).

A clear majority of company respondents (83%) reported that it is difficult to accept that the company buys and sells grey goods or services. Nearly half of the respondents (42%) agreed more or less and nearly one-third (27%) agreed completely that the grey economy distorts healthy competition.

The grey economy involves the neglect of taxes and other statutory payments.

1 The margin of error in the study performed by TNS Gallup is 3.0–5.5%.
Info box:

Transportation companies accept annual reports by the licensing authority

Each year, the licensing authority will examine the prerequisites for a transportation permit to determine whether the holders of the transport permit still fulfil these conditions. The obligation is related to combating the grey economy.

At the end of 2013, the Grey Economy Information Unit examined the tax debts of transport companies. Approximately 1 000 companies had tax debts of more than EUR 12 000, and the transport licensing authority gave these companies until the end of July to pay their tax debts. In July, about 200 operating licences were cancelled due to unpaid tax debts.

All companies were charged an inspection fee of EUR 90 in order to cover the investigation costs to the authorities. Finnish Transport and Logistics – SKAL2 asked transport entrepreneurs for their views concerning the control mechanism and sanction that leads to the termination of business activities.

Based on the questionnaire, transport sector entrepreneurs unanimously support the prevention of grey economy. Over 90% of respondents considered the annual reports to be a good idea. Approximately 85% of respondents felt that the procedure will revitalise the transport industry and nearly just as many believed that losing licences was an acceptable sanction for neglecting obligations. The costs to companies were accepted by less than half of respondents. Nearly half of the respondents considered the cancellation of 200 operating licences to be insignificant in terms of preventing the grey economy.3

Grey economy research in the European Union

During the past 20 years, the European Commission has attempted to find a practical method for measuring undeclared work that could produce comparable results from all member states. Extensive surveys conducted by the Commission have identified research performed in member states using more than 200 different methods.

The process of finding a common method has been complicated by different views of what should be studied and differences of opinion concerning the usefulness of various methods. With regard to feasibility, opinions are divided between direct and indirect methods.

In 2006, the Commission commissioned a report on the suitability of direct methods, mainly interview studies, for measuring undeclared work. The report concluded that direct questionnaire studies provide the best picture of the structure and reasons for undeclared work. Based on its recommendations, the Eurobarometer interview survey was carried out in all member states. However, the results concerning the extent of the grey economy, particularly for Southern European countries, were somewhat difficult to believe.

In 2009, the Commission commissioned a report on the feasibility of indirect methods, simultaneously assessing research performed with such methods in all member countries and two candidate countries.

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2 SKAL represents companies who offer road haulage services, as well as enterprises providing logistical services. Some 6,000 transport and logistics companies are members of SKAL.

When performing suitability assessments, methods based on, for example, the amount of cash, electricity consumption and so-called use of hidden variables were excluded from the wide range of indirect methods. The most appropriate method for comprehensively examining undeclared work in the EU area was considered to be a method based on labour input, which involved comparing labour input and the use of officially reported labour. The study implemented with a method based on labour input covering all member states that was proposed in the report has not as yet been performed.

The Commission's interest in the grey economy has primarily focused on the share of undeclared work rather than the grey economy as a whole, as has been understood in, for example, Finland and Sweden. The approach in the latter countries is fiscal, meaning that research is aimed at finding the total amount of information concealed from the Tax Administration.

The central result of the reports commissioned by the European Commission over the past 20 years is that a single feasible and reliable method for measuring the grey economy has not been found. Research on the amount of grey economy in both Sweden and Finland are based on dividing the target area into parts and on the use of several different methods to supplement each other. Although the entire truth about the amount of grey economy cannot be determined, the selected approach appears to produce results that seem logical in international comparison.

Info box:

Grey economy research in Sweden and Finland

In Sweden, the Svartjobb study has examined the overall framework of the grey economy by comparing the expenses and reported income of households. The content of this framework has been verified and specified by means of a method based on tax audit results and supplementary interview surveys and studies to determine the income level of entrepreneurs. The specification was further continued in the Stattefel study that followed the Svartjobb study.

The Suomen Kansainvälistyvä harmaa talous (Finland’s internationalising grey economy) study evaluates the overall framework of the grey economy on the basis of tax audit results and on a calculation of the difference between theoretical and accrued value-added tax. The structure and manifestations of the grey economy have been defined in reports on different sectors and income types, which have sought solutions for assessing the grey economy related to, among others, rental income, international trade and international investment activities.

Cross-administrative working group on the tax gap is a good example of cooperation between different authorities

The Parliament of Finland’s Audit Committee addressed the tax gap issue in a memorandum contained in the Report on State Annual Accounts 2011. In its memorandum, the Audit Committee stated that more information about the factors affecting the tax gap must be obtained in the future in order to make it possible to allocate the resources and actions used to reduce the tax gap in the proper manner and as effectively as possible.

Based on the Audit Committee’s proposal, Parliament approved the following opinion on 26 September 2013: 'The Parliament of Finland requires that the Government report annually on the estimated tax gap and amount of, changes in and factors essentially affecting outstanding taxes, and on the impact of meas-

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4 Skatteverket: Svartköp och Svartjobb i Sverige, Del 1, Undersökningsresultat, Rapport 2006:4
5 Hirvonen, Markku, Lith, Pekka, Walden, Risto: Suomen kansainvälistyvä harmaa talous Finland’s internationalising grey economy), Eduskunnan tarkastusvaliokunnan tilaaman harmaata taloutta käsittelevän tutkimuksen loppuraportti, Final report of a study of the grey economy commissioned by the Parliament of Finland’s Audit Committee, Helsinki 2010
ures used to reduce the tax gap and outstanding taxes in the Report on State Annual Accounts. The first report shall be included in the 2013 Report on State Annual Accounts in conjunction with factors affecting the state of the country’s economy and tax revenue."

The goal-setting document for the Ministry of Finance and the Tax Administration for 2013 states that "In cooperation with external bodies, the Tax Administration will initiate a report on developing methods for assessing the size of the tax gap and its partial factors."

On 8 February 2013, the Tax Administration appointed a working group with the task of defining the tax gap and dividing it into sub-factors, to create methods for measuring the tax gap, to develop methods for identifying factors affecting the tax gap, to create a method for assessing the impact of measures taken to reduce the tax gap, and to perform the first tax gap assessments. Representatives from Finnish Customs, the Government Institute for Economic Research, the Ministry of Finance, and Statistics Finland were also invited to join the group. The working group submitted its final report in March 2014.

According to the report, the size of the tax gap as measured by the Tax Administration’s assessment method for the first calculated portion, VAT in 2010, was EUR 1.4 billion, which is about 7% of the computational VAT receivables. According to Finnish Customs, the customs clearance tax gap in 2012 totalled approximately EUR 140 million (duty and VAT), the tax gap for excise tax approximately EUR 162-233 million, and the tax gap for taxation of cars approximately EUR 15.5 million. The next phase will involve producing information about the tax gap related to salaries and a time series to evaluate the VAT gap.

A tax gap refers to the difference between expected tax revenue according to the law and actual tax revenue. The grey economy only causes some of the tax gap.

http://www.vero.fi/download/Loppuraportti_Verovajeen_arviointimenetelmien_kehittaminen/%7B7880270F-569B-44AF-9DEA-5D9FAF393172%7D/9492
The grey economy in the media

The Grey Economy Information Unit monitored publicity related to the grey economy in online media during 1 January 2014–30 June 2014. During the analysis period, the monitored media published 748 articles that mentioned the grey economy. The number during the previous six-month period was 782.

During the monitoring period, 748 articles containing at least a mention of the grey economy appeared. Some 20% of the articles associated grey economy with themes dealing with construction work or the construction industry in general. Half of these addressed changes in the notification procedure for contract and access permit information in the construction industry. Other topics included the tax number, results of the Tax Administration’s Raksa project, construction quality, the administrative burden on construction entrepreneurs, and the nuclear power plant project.

2. RESEARCHED AND MEASURED

The Grey Economy Information Unit produces and shares information about the underground economy and on how to combat it. Among other things, the unit compiles reports on grey economy phenomena and the measures used to prevent them. When producing its reports, the unit makes extensive use of information about organisations and people associated with them that is available in registers maintained by different authorities. The Information Unit also utilises public information available from, for example, Statistics Finland or the Finnish Trade Register.

One of the key questions in these reports involves assessing the size of the grey economy. The reports also strive to find indicators that can be used to better evaluate the amount and development of the grey economy.

This section describes some of the themes and measurement methods that are addressed in studies conducted by the Information Unit. The measurement methods used are characterised by the fact that they alone cannot demonstrate the prevalence or amount of grey economy in the material being examined. However, in combination they provide a picture of whether the risk of grey economy in the object of research – for example, a specific entrepreneur group – is greater than for other companies.

The following examples address the importance of indebtedness, key company figures, fulfilling obligations, and the other corporate connections of company personnel with regard to the grey economy. The significance of corporate relations in terms in fulfilling obligations and with regard to the grey economy has been highlighted in several reports.

Fulfilling tax obligations

The reflection of tax debt and the changes in it on general changes in society can provide the authorities with more information about the grey economy. Tax debt is associated with the grey economy when a taxpayer intends to avoid social obligations and tax payment for a reason other than a reduced ability to pay taxes. On the basis of tax audits and taxation by assessment, the grey economy accounts for at least part of tax debt with regard to debited taxes. Paid taxes
in relation to the amount of tax debt tells something about the payment morale of taxpayers. A general deterioration in payment morale is related to an increased risk of grey economy.

The hidden nature of the grey economy makes it difficult to accurately assess the role it plays in tax debt. The grey economy is often a matter of so-called hidden tax debt, which the authorities are not aware of and which is subsequently not visible in the amount of outstanding taxes. However, this hidden part of the tax debt increases society’s tax gap, which comprises the tax debt known to the Tax Administration and hidden tax debt.

INDEBTEDNESS AND KEY COMPANY FIGURES

Companies found to be insolvent in enforcement proceedings rarely continue their business

During 2009–2013, the Grey Economy Information Unit studied companies found to be insolvent or otherwise disqualified with regard to their functionality, financial position and reliability and the fulfilment of certain statutory obligations.

The operations of companies found insolvent during enforcement are relatively short-term in nature. Nearly half of the companies in the material have operated for less than three years.

Nearly 60% of the companies were repetitively disqualified during enforcement. The companies’ payments to the Tax Administration required enforcement in more than 80% of the cases. Thus, insolvency and reduced ability to pay for companies which have an impediment for lack of means is quite permanent.

The reports also examined whether companies declared insolvent during enforcement could be removed from the Trade Register at the initiative of the authorities. This would make the use of insolvent companies in business and possibly criminal activity more difficult, which would in turn contribute to reducing the opportunities to operate in the grey economy.

Info box:

The amount of tax debt may predict the incidence of the grey economy. Based on the observations in the reports, even tax debt equal to 5% of turnover poses a significant risk for companies in terms of business continuity.

Ratio between sales margin for licensed premises and salaries in relation to turnover

Sales margin is the share of total sales that the company earns as the difference between the selling and purchase prices of a product. Sales margin is used to finance other business expenses, such as salaries, rent, etc. The sales margin percentage is a reliable comparative figure that is obtained by calculating sales margin as a relative share of turnover.

The variation in the sales margin for companies that fulfil their statutory obligations is relatively small. By comparing the sales margin percentages between companies in the same sector it is possible to get a reliable comparison value that can help detect deviations. For example, an alcohol sales margin percentage that deviates from the average range of variation in the industry can indicate that a company is partially failing to report income. Company-specific audits of the amount of alcohol sales recorded in bookkeeping can be compared to alcohol purchasing information available as comparative data, which in turn reveals possible non-registered sales.

In 2013, the Grey Economy Information Unit examined companies operating in the alcohol service industry and observed that some 32% of the companies in the data had a low sales margin percentage for alcohol or beer. A company for which the sales margin percentages for alcohol, beer or both were less than 50% was classified as having a low margin.
The average sales margin for alcohol service activities in 2013 was 67%. A company with a sales margin percentage of 50% or less deviates significantly from the general average in terms of pricing. The difference in turnover is noticeable, for example, when examining companies with alcohol purchases of EUR 100,000 per year. A company that operates with a 50% sales margin can have an operating income that is EUR 25,000 negative while the operating income for a company with a "normal" sales margin percentage can be EUR 87,000 positive with the same purchase amounts.

Growth in the number of licence holders with a low margin represents a significant risk in terms of preventing the grey economy. The number of licence holders with a low margin has increased by about 10% each year. This development has accelerated noticeably during and since 2009. The increased number is considered to forecast an increase in possible non-registered sales in the business.

Growth in the number of licence holders whose salaries are low in comparison to turnover (less than 20% of turnover) is also increasing. According to Statistics Finland's financial statement statistics, pay usually accounts for 30–40% of turnover in the sector. The reports also observed that low pay and a low sales margin are often linked to each other.

The amount of pay in relation to turnover can be examined in the same way as the sales margin percentage between companies operating in the same sector. Abuses can occur in a company that deviates strongly from the industry average. Particularly in labour-intensive sectors, low pay and the amount of work compensation in relation to turnover may be a sign of undeclared wages. When wages are not entered in bookkeeping, the employees' statutory contributions also remain unpaid, which means that pension and other employment-related benefits do not accrue.

**THE IMPORTANCE OF CORPORATE RELATIONS WHEN DEALING WITH COMPANIES’ OBLIGATIONS**

The Information Unit’s reports generally also examine the mutual networking, or "clustering" of companies and responsible persons in each target group. According to the general definition, a corporate cluster means a group or concentration of companies under the authority of one owner or sphere of interest. Authority in the companies is either directly based on ownership or on decision-making power that is comparable to actual ownership. In addition to Finnish Trade Register information, trade register data from neighbouring countries, such as Estonia, is often used to determine the extent of clustering.

The distribution of business among several different companies is completely legal business planning. However, a high level of clustering has still proven to be a risk factor in terms of the grey economy and creates problems for the control authorities. According to the final report of a working group that considered the development of tax control, the grey economy is detected in 30.84% of tax audits that target corporate clusters. The average share of grey economy in all audits was lower - 20.41%. In cases involving the practise of grey economy, corporate clusters are generally used as tools for committing and concealing financial crime.

**Info box:**

Cluster tax debt means the combined tax debt of a person’s cluster companies. The most natural object of monitoring is the cluster tax debt of a target person in companies where he or she holds a position of authority.

When measuring cluster tax debt, the past of the target person is often examined, which means his or her connections to companies that no longer exist. A history that contains several companies with tax debt that are no longer operational due to, for example, bankruptcy, can indicate the deliberate use of companies with a short life cycle.

The following section presents some recent reports that provided signs of the role that corporate connections, or clustering, play in the incidence and prevention of the grey economy.
Criminal cases in construction industry tax control

The Grey Economy Information Unit has investigated criminal cases observed in conjunction with the Tax Administration’s tax control project in the construction industry (Raksa project). The report addressed a total of 267 financial crime sentences.

Cluster-type activities play a major role

The clearest observation when examining offences reported in the Raksa project was the fact that the grey economy is conducted in clusters. The majority of people found guilty were sentenced because of activities utilising several companies. The majority of the sentences for damages in the Raksa project criminal cases – approximately 80% – resulted from cluster-type activities. The people sentenced were very often connected to each other on the basis of business tax obligations and their position of authority, and via trade register and ownership links.

The primary type of offence was false invoice trade

The offence in clusters and larger entities is typically the receipt trade and/or falsified invoicing, the benefit of which is used for paying undeclared wages. The sentenced persons were much more likely to use shell companies, receipt trade and have an earlier sentence for financial crime in cluster-type activities. Furthermore, 63% of all bans on business operations in the research data were issued in cluster-type activities.

Finnish companies’ connections to Estonia

According to reports, at the beginning of 2012 the Estonian Trade Register contained more than 27,000 companies with one or more responsible person registered with a Finnish identity number. About 11,400 of these companies had a responsible person who lived in Finland. Finnish citizens living in Finland were responsible for the entire management of approximately 2,500 companies.

Of all the Finnish responsible persons in the Estonian Trade Register:

- 16% had tax debt – while an average of 3.8% responsible persons in the Finnish Trade Register had tax debt
- 26% had cluster tax debt through their companies – while an average of 7% of responsible persons in the Finnish Trade Register had cluster tax debt

The number of Finns' corporate connections in the Estonian Trade Register had grown steadily. In 2006, there were about 16,500 Finnish identity numbers and by the beginning of 2012 that number was already more than 25,000. Approximately 19,500 companies had a valid link to Finland. The number of companies increased by about 58% between 2006 and 2012.

The results of the report led to an evaluation that the responsibility relationships that Finnish companies and people have with Estonia and the increase in those numbers would appear to constitute a significant grey economy risk. The company responsible persons in the Estonian Trade Register that had a Finnish identity number were on average more susceptible to problems in terms of handling obligations than people in the Finnish Trade Register.

Bankruptcies and associated persons

A report on tax debt related to taxation of goods examined the probability of bankruptcy stages in two different corporate groups. This section presents an example of causal connection measurement used in the report:

The audit focused on investigating the statistical link between associated persons and the incidence of bankruptcies. The other companies of the associated persons for the target group companies were divided into two groups, A and B, based on whether the associated person’s target group company had experienced stages of bankruptcy (group A) or not (group B).

21% of companies in group A and 2% of companies in group B experienced bankruptcy stages. A statistical link was observed between the bankruptcy risk of companies if the company had a common associated person.

Companies in which persons associated with the target group held the position of associated person in 2009–2013.
The effect of the so-called corporate raider phenomenon was eliminated from the investigation by excluding associated persons who held a position of responsibility in more than 50 companies. In this case, bankruptcy stages in companies further increased the likelihood of a bankruptcy stage in another company, but the link was not nearly as clear; 10% of companies in group A and 2% of companies in group B had experienced bankruptcy stages.

**Tax indebtedness of other companies**
The existence of a statistical link between the tax indebtedness of companies when companies share an associated person was also examined. When the company of an associated person has a tax debt to the Tax Administration, 28% of the other companies have tax debt. When a target group company of an associated person has a tax debt to the Tax Administration, 6% of the other companies have tax debt.

**Info box:**

**Observations of tax debt and connections between companies**

Several reports have observed a clear statistical link between the responsible persons of a company and tax debt in the companies they run. 26–31% of the target group companies of associated persons who had personal tax debt had tax debt. 6–7% of the target group companies of associated persons who did not have personal tax debt had tax debt.

### 3. PREVENTION OF GREY ECONOMY

The grey economy can be viewed in different ways depending on control authority examining the matter. Authorities and other organisations with public service tasks prevent the grey economy in practice by means of, for example, tax, customs or pension audits, and by means of special recovery measures carried out by enforcement. The pre-investigation authorities also prevent the neglect of taxes and other fees under public law in their own work.

Combating the grey economy means preventive measures, disclosure and investigation actions, and measures to recover the financial benefit gained by the person involved in grey economy.

Various authorities have invested more than 2,000 person-years in preventing the grey economy in recent years. Additional resources have been granted during the current prevention programme, and as a result the Tax Administration has increased its investment in grey economy prevention by 128 person-years, the Ministry of the Interior by 92, the Ministry of Justice by 65, Finnish Customs by 21, the Ministry of Social Affairs and Health by 20, and the Ministry for Employment and the Economy by 9 person-years.

**The risk of being caught is increasing**
A person operating in the grey economy often approaches his or her acts in a very rational manner. He or she considers the benefits gained, risk of being caught and consequences of the act. The prevention of grey economy aims at influencing that person’s decision-making by ensuring that the financial benefit of the acts is slight, the risk of being caught is high and the punishment for the acts involves quick and correctly dimensioned administrative or criminal sanctions. The target is to prevent the grey economy in advance. Preventive measures can be legislative changes that strive to change or prevent some grey economy operating methods. Some of these apply to everyone, while others are aimed at a specific group or sector. The following section presents some recent changes.
**Wider use of the tax number under consideration**

The tax number has been used in the construction industry since the middle of 2012. The Register of Tax Numbers contained nearly 800,000 people in September 2014.

Introduction of the tax number has also been considered in the installation or assembly, shipbuilding, transport, repair and maintenance work, cleaning, nursing and care giving work, and in the restaurant and accommodation sectors.

In September 2014, the Ministerial working group on the fight against the shadow economy stated that wider use of tax numbers will only be considered after the national income register is introduced. The Government made a decision to implement the income register in March 2014 in conjunction with the structural policy programme. In this case, employers would report, for example, information about wages paid to their employees to the income register rather than to many different bodies. The reform will probably require several years of preparation.

**Reporting requirement for projects and employees from 2014**

In 2014, a special reporting requirement for employees and construction projects was introduced at construction sites. This procedure involves the main customer submitting information to the Tax Administration on a monthly basis about employees working at the site.

Each customer also reports its subcontracting to the Tax Administration each month. As a result of the changes that took effect in July 2014, the customers is obliged to provide monthly reports containing information about, for example, who the construction services were ordered from, the total size of the contract, how much the company has invoiced the customer for during the current month, and the estimated duration of the work.

The reporting requirement also applies to construction of a single-family house or other construction or renovation work ordered by a private individual if a building permit is required for the work. Among other things, a private individual must provide information about the company performing the work and employees and the wages and other compensation paid to them.

In combination with the tax number reform and the public Register of Tax Numbers, the reporting requirement for employees and projects provide the Tax Administration with the conditions needed to monitor when, for example, a foreign company establishes a permanent establishment, thus making it liable to pay taxes in Finland. The information is also utilised to monitor when employees become liable to pay taxes. The possibility to use undeclared labour or neglect statutory obligations is reduced, which in turn makes it more difficult to gain a competitive edge by unfair means.

**Info box:**

The Tax Administration's Raksa project effectively revealed grey economy in the construction sector

When converted into euros, the result of the largest grey economy project in the history of the Tax Administration was more than EUR 200 million. Offences were reported for nearly every 10% of the audited construction companies.

The goal of the Tax Administration's construction sector tax control project was to reduce grey economy in the construction industry and guide companies to operate correctly. The goals were achieved by increasing the number of audits and developing real-time tax control.
The Raksa project was carried out in 2008–2012 and 3,525 tax audit reports were completed during that time. The grey economy was found in nearly every third auditing target. Offences were reported in nearly 10% of the tax audit reports, with 264 of the cases involving aggravated tax fraud. For example, receipts totalling EUR 112 million were found to have incorrect content. More than 90% of the unclear incidents were found in companies with a turnover of less than EUR 6 million.

**EUR 220 million in undeclared payroll**

The tax audit reports prepared during the project showed 4,857 wage earners outside bookkeeping and nearly EUR 220 million in payroll from which withholding tax had not been collected. A total of EUR 92 million in undeclared dividends was found.

According to the Tax Administration, the project has had a positive impact on preventing the grey economy and the risk of being caught has increased. Real-time control measures have proven to be particularly effective. During the project, the Tax Administration made site visits with occupational safety and health inspectors from the Regional State Administrative Agencies, Finnish Centre for Pensions inspectors, and the Police. The most important achievements are permanent, more effective cooperation between authorities and interactive cooperation with stakeholders and large operators in the construction sector.

**Receipt Act took effect at the beginning of 2014**

Legislation on the obligation to give a receipt took effect at the beginning of 2014. Entrepreneurs must offer the customer a receipt for any goods or services purchased. The purpose of the new law is to increase control over the use of cash and enhance prevention of the grey economy.

The law is intended to prevent grey economy in the form of non-registered sales in sectors that use cash. The law applies to business and professional activities referred to in the Business Income Tax Act (360/1968).

An entrepreneur’s obligation to provide a receipt applies to purchases made in cash or with a debit card in all sectors. The law does not require use of a cash register or cash system, and the receipt can also be written by hand.

The obligation to provide a receipt improve the customer’s possibility of detecting sales that are not recorded in a cash register or in bookkeeping. Thus, the customer also has the opportunity to select and make purchases at a company that observes the law. The statutory obligation to provide a receipt also improves the consumer’s position when there is a problem with goods or a service.

**Parliament approved the Tax Debt Register**

The legislation on the Tax Debt Register has been confirmed and the register will be introduced on 1 December 2014.

As of December 2014, the Tax Debt Register will publish information on whether a company, trader or death estate engaged in business has tax debt or reporting deficiencies.

The reform concerns the public register maintained by the Tax Administration, which can provide information about a company’s tax debt situation quickly, reliably and at no cost. The register covers all taxes assessed by the Tax Administration. It will include information about whether a company has unpaid taxes and fees of at least EUR 10,000 that are due for payment and is not subject to payment arrangements made by the Tax Administration or a stay of enforcement by the appeal authority. However, the exact amount of the debt is not provided. Information about whether a company has neglected VAT or the reporting obligation concerning employer contributions is also entered in the Tax Debt Register.
This information is particularly useful when dealing with obligations\(^8\) outlined in the Act on the Contractor’s Obligations and Liability when Work is Contracted Out. Such information can also be used in situations covered by the Act on Public Contracts\(^9\) and in general contract situations between companies. The aim is to eliminate grey economy phenomena and improve the competitive position of companies that handle their obligations well.

**Reverse charge procedure progresses in the scrap industry**

In May 2014, the Government proposed a change in the VAT Act according to which VAT liability would be implemented in the scrap industry. When applying the reverse charge procedure, the buyer rather than the seller would be liable to pay VAT.

The reverse charge procedure in the scrap industry is used in the majority of EU member states. The proposed model also corresponds to the system implemented in Sweden at the beginning of 2013, which according to preliminary assessments has operated as expected without significant problems.

The reverse charge procedure would apply to the exchange of all metal scrap and waste among private traders who are entered in the VAT Register. The system would apply to certain types of metal scrap and waste according to the Combined Nomenclature in the customs legislation.

The proposal is designed to prevent the grey economy. Implementation of the system is aimed at reducing abuse by actors in the scrap industry and improving the competitive situation between companies that operate appropriately and dishonest companies.

Introduction of the reverse charge procedure in the scrap industry would mean an estimated EUR 7–8 million increase in tax revenue each year. The law takes effect on 1 January 2015.

**The amended Act on Commercial Transport on the Road took effect on 1 July 2014**

The purchaser of transport services is currently responsible for ensuring that the transport supplier fulfills certain statutory obligations. The customer must ensure that the transport supplier has a valid operating license and even that the transport price is sufficient to handle employer obligations. According to the amended transport act, a purchaser of transport services is guilty of a transportation order offence if they accept a price that is too low. Based on the law, the price must be such that the transport supplier can handle its statutory obligations as an employer.

Since the beginning of July, the license requirement expanded to also include transport performed as sub-contracting, commercial goods transport by tractor, and commercial towing and removal transportation.

**Info box:**

**Grey economy prevention programme in 2012–2015**\(^{10}\)

The majority of the above-mentioned legislative amendments are included in the ongoing Action Plan to Reduce Economic Crime and the Shadow Economy. According to the Government Programme, prevention of the grey economy is one of the government’s spearhead projects. The prevention programme is a continuation of the five earlier programmes and it contains 22 projects to reduce the grey economy and economic crime. New measures to prevent the grey economy were also outlined in the government spending limits discussion in spring 2013 and government budget discussion in the autumn, and subsequently added to the prevention programme.

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\(^8\) A partial reform of the section concerning construction activities in the Act on the Contractor’s Obligations and Liabilities when Work is Contracted Out entered into force on 1 September 2012 (469/2012 Amendment of the Act on the Contractor’s Obligations and Liability when Work is Contracted Out).

\(^9\) The Act on Public Contracts provision stating that all public sector construction project contracts shall contain a clause concerning compliance with the minimum terms of employment took effect on 1 September 2012 (Act on Public Contracts, section 49).

\(^{10}\) http://www.vm.fi/vm/fi/04_julkaisut_ja_asiakirjat/03_muut_asiakirjat/20120119Tehost/name.jsp
The "Ne bis in idem" law, protection against self-incrimination and plea bargaining will change tax audits and criminal processes

The "Ne bis in idem" law, or Act on Tax Surcharges and Customs Duty Surcharges Imposed by a Separate Decision (781/2013) has been in effect for nearly one year.

**Info box:**

Ne bis in idem is a Latin legal principle that means "not twice in the same thing". The Convention on Human Rights, protocol 7, article 4 defines the principle of ne bis in idem as follows: No one shall be liable to be tried or punished again in criminal proceedings under the jurisdiction of the same State for an offence for which he has already been finally acquitted or convicted in accordance with the law and penal procedure of that State.

The law is intended to reconcile a tax penalty assessed as an administrative sanction and punishment imposed as a criminal sanction so that a natural person, domestic death estate or corporation is not investigated and punished twice for the same act. On the other hand, the law makes it possible to realise criminal liability in cases in which a tax penalty is insufficient with regard to the severity of the act.

Since 1 December 2013, the Tax Administration has been able to make a taxation decision for a natural person, death estate or corporation without imposing a tax penalty if an offence has been reported for the same act. According to the new law, a tax penalty can be imposed later if the criminal procedure does not progress to court proceedings for one reason or another. The purpose of the procedure to encourage the authority to decide as early as possible whether to process the consequences of taxation-related abuse administratively as a tax penalty matter or on criminal grounds as a prosecution matter.

**Self-incrimination**

Self-incrimination has also become a part of the fair trial process in Finland, at the latest as a result of legal cases KKO 2009:80 and KKO 2010:41. Protection against self-incrimination has also been discussed in legal literature using different terminology. In its present form, it is based on the International Covenant on Civil and Political Rights, article 14, section 3, item g, according to which, in the determination of any criminal charge against him, no one can be compelled to testify against himself or to confess guilt.

In the Government proposal to Parliament concerning the reform of Chapter 17 of the Code of Judicial Procedure and the related legislation concerning evidence in a general court of law (Government Proposal 46/2014), utilisation of evidence obtained by violating protection against self-incrimination and by means of torture will be prohibited. This ban would also apply in other official proceedings and in pre-trial investigation or criminal trial with regard to a statement or material evidence obtained from a person by threat of coercive measures or otherwise against his or her will. Such a statement or piece of evidence could not be utilised in a criminal case if the methods had an pertinent and temporal connection. The proposal also includes a ban on utilisation of evidence obtained in some other illegal manner if pressing reasons exist with consideration to the nature of the case, method of obtaining evidence, importance of the evidence in terms of solving the case, and other conditions.

**Plea bargaining**

So-called plea bargaining will be implemented at the beginning of 2015. In a new procedure called plea bargaining, person accused of a crime can receive a lighter sentence after confessing.

Plea bargaining can be used in crimes in which the most severe punishment is a maximum of six years imprisonment. However, plea bargaining will not be applied to crimes against life or health or sexual crimes that violate the right to sexual autonomy or which target children.

The intention of making plea bargaining possible is to increase the effectiveness of and accelerate the processing of extensive and complicated financial crimes. The procedure is intended for cases in which it can be assessed as being of most benefit in terms of sensible allocation of official resources and prompt handling of a criminal matter.
CASE ANTON –A SIGNIFICANT PRECEDENT

Finland's largest receipt trade case took a new direction in Supreme Court

The investigation and legal processing of a major receipt trade matter in the construction sector has lasted a total of 10 years. The Supreme Court decided to return the case to the Court of Appeals in June 2014. In its preliminary ruling (KKO 2014:46), the Supreme Court stated that the procedure referred to in the charges can constitute tax fraud for the purposes of evading payment of withholding tax, employer social security contributions and VAT in company activities for all parties to the procedure. With regard to judicial procedure, the preliminary ruling also had value in that, according to the Supreme Court, the Court of Appeals should not have investigated the evasion of withholding tax for those people who had not appealed or counter-appealed the decision.

According to the charges, persons doing construction work (authorised to sign for the company) had signed construction contracts in the name of a limited company and agreed on invoicing of their work through the company. After payment to the company account, the funds were withdrawn and mostly deposited to the people who performed the work. Some of the funds were divided among the people responsible for the company operations (office staff) and people who assisted in mediating the contracts (mediators).

The case was a question of whether the people participating in the procedure described were guilty of tax fraud in taxation involving the failure to deduct withholding tax and make employer social security contributions for wages paid by the company and neglecting to report payments received by the company in value-added taxation as company sales.

In terms of criminality, the Supreme Court considered – in contrast to the Court of Appeals – that the procedure referred to in the charges as the right to use a name can constitute tax fraud performed in office company activities for all parties.

In its ruling, the Supreme Court presented the following arguments:

Taxation assessment of construction activities practised in the name of office companies

Construction activities by people authorised to use the name has taken place in the name of office companies according to a contract between those people and the office staff. The Supreme Court has stated that construction activities were arranged to appear as if they were completed performed in the name of the office companies, thus providing the grounds to consider the activities to be company operations when legally assessing the construction activities. Furthermore, the contracts concerning the construction work and the payments made on the basis of those contracts resulted in business transactions in the bookkeeping of the office companies. The funds paid for construction work performed in the name of the office companies were in the possession of the companies and were part of the companies' assets and ownership. Similarly, the activities of those authorised to sign were not arranged in a manner that appeared independent and were not conducted in the name of or by them with regard to external bodies.

The activities described as use of the name were intentionally arranged so that work that appeared to be performed by the office companies was actually performed by those entitled to sign for the company. The Supreme Court considered that, based on the procedure described, the role of the office companies could be considered equal to functioning as an employer.

Based on the grounds presented above, the Supreme Court considers that construction work performed in the name of office companies owned by those authorised to sign constituted office company business that is liable for VAT. Payments, mainly in the form of wages, for construction work performed in the name of office companies should have been subject to withholding tax and employer social security contributions.

Liability for evading taxes

Construction activities conducted in the name of the office companies had been the business of these companies in its entirety. The office staff had actual decision-making power in the companies. The office staff had decided to accept construction work carried out by the people authorised to sign for performance in the name of the office companies. The procedure was implemented with the purpose of avoid-
ing taxes related to construction work. Based on these and other grounds, the Supreme Court considered that the office staff are also criminally liable for tax evasion for construction work performed by the people authorised to sign with regard to all tax types included in the charges.

The people authorised to sign agreed with the office staff on performing construction work in the name of the office companies, arranging invoicing by the office companies, and distributing the benefit of evading taxes. As a result, the people authorised to sign had actual decision-making power concerning their own activities in the office companies and thus the Supreme Court also considered them to have criminal liability for all tax types included in the charges.

The mediators brought the office staff and people authorised to sign together and arranged their communication. According to the Supreme Court, imputation of tax fraud as an actor requires evaluation of how significantly the proper mediator can be considered to have contributed to the joint activities of the office staff and people authorised to sign that were aimed at evading taxes.

Processing of the matter with regard to approximately 50 defendants continues in the Helsinki Court of Appeals. The Court of Appeals must assess the facts and circumstances of the matter on the basis of the criminal evaluation of the Supreme Court (KKO 2014:46).

4. ENFORCEMENT AND PREVENTING THE GREY ECONOMY

The Enforcement Agency comprises the National Administrative Office for Enforcement and the 22 local enforcement agencies operating under it. In combination with the court system, enforcement forms the legal protection system for society and belongs to the administrative sector of the Ministry of Justice. The basic task of enforcement involves enforcing neglected obligations. The majority of enforced obligations involve payments. These obligations are mainly civil demands for payment confirmed by a court sentence or public claims for payment or taxes that are directly enforceable.

A total of EUR 2.7 billion were transferred to enforcement for collection in 2013, and the collection result was some EUR 1 billion. In 2013, taxes and public claims for payment accounted for 62% of the matters transferred to enforcement. At the end of 2013, the number of debtors with enforcement cases pending was approximately 240,000 (including natural persons and legal persons).

THE ROLE OF ENFORCEMENT IN PREVENTING THE GREY ECONOMY

Enforcement is actively involved in combating the grey economy and enforcement activities have many impacts related to preventing the grey economy. The grey economy is intended to maximise financial benefit by neglecting statutory payments related to the activities that are levied by society. Financial or other crime is often related to such activities. For example, by effectively collecting neglected taxes, enforcement can in individual cases prevent actors in the grey economy from achieving financial benefit, collect the neglected tax for the state, and successful recovery also has a preventive effect on the grey economy.

The effectiveness of enforcement is directly related to its preventive effect on the grey economy. A potential grey economy actor will not resort to abuse when he or she is aware that it will not produce financial benefit.

Enforcement has other concrete effects on combating the grey economy, such as preventing unhealthy competition in business. Effective recovery implemented by enforcement ensures that entrepreneurs who handle their payment obligations properly do not have to compete with actors who neglect their obligations. The grey economy leads to an unhealthy competition situation in the market, because a grey economy actor can price its products or services at a lower level than an entrepreneur who handles all his or her obligations. Effective recovery prevents the continuation of an unhealthy business by making it possible to keep capital within the scope of business, and thus using enforcement measures to prevent continuation of the activities.

The role of enforcement in combating the grey economy often appears to be related to grey economy that has already been revealed. Based on tax audits, the Tax Administration has ordered debiting that is
transferred to enforcement or compensation for injured parties (often the Tax Administration) are sought in Police criminal cases and subsequently transferred to enforcement for payment, first as a preventive measure and finally in the form of a binding judgement. However, this is only part of the truth. In an enforcement procedure, the debtor’s financial position is examined carefully and, if necessary, the investigations can also extent to third parties and the debtor’s inner circle. Information access rights are very broad for enforcement. The possibilities of observing and identifying potential grey economy actors are good in these investigations. Cooperation between the authorities ensures that the necessary official actions target the right objects.

ENFORCEMENT MEASURES TO IMPROVE THE EFFECTIVENESS OF GREY ECONOMY PREVENTION

Enforcement combats the grey economy by means of special recovery, corporate recovery, and in the normal enforcement process. The following section highlights the special features of each recovery method with regard to preventing the grey economy.

Special recovery

Enforcement involves the processing of huge amounts of data and the recovery process must progress in a prompt manner. In special recovery, the functions focus on debtors for which investigation the asset position and implementing measures requires a lot of work. Debtors transferred to special recovery have usually attempted to avoid paying their debts and put their property out of the reach of enforcement through various types of abuse. These debtors often have links to financial crime and the grey economy. Due to the time required, it is not practical to deal with such debtors in the normal enforcement process.

The fact that the grey economy was given an important role in Jyrki Katainen’s Government Programme also made it possible for enforcement to increase its efforts to combat the grey economy. Grey economy actors are often the target of measures by several authorities and the increased cooperation between the authorities and elimination of barriers to information exchange between different authorities outlined in the Government Programme were seen as an important elements in preventing the grey economy. Cooperation between the authorities has traditionally played an important role in special recovery by enforcement.

Earlier, only the Helsinki and Lapland enforcement agencies had special recovery departments. Some enforcement agencies also had assistant enforcement officers to handle special recovery. Special recovery was expanded to the national level in 2011 as part of the enforcement measures to improve the effectiveness of grey economy prevention. Nation-wide special recovery currently operates in six special recovery districts, which are Southern Finland, Western Finland, Central Finland, Eastern Finland, Ostrobothnia, and Northern Finland special recovery districts. Special recovery has a staff of seven district enforcement officers and 48 assistant enforcement officers. Eight of these assistant enforcement officers serve under the title of senior advisor.

Since cooperation and information exchange between the authorities are of utmost importance when combating the grey economy, special recovery is able to respond to the needs of cooperation authorities with the required urgency and expertise. Special recovery cooperation with the nearest cooperation authorities (the Police, Tax Administration, Finnish Customs) has been regular and organised. The reform of the Coercive Measures Act that took effect at the beginning of 2014 and the procedure prescribed therein concerning the enforcement of temporary confiscation for security further increases the need for cooperation between the Police, customs and the Finnish Border Guard. New enforcement tasks also include enforcement measures related to freezing of terrorism property and probably, at a later time in conjunction with the reform of the Act on the Enforcement of Certain Obligations of Finland as a Member of the United Nations and of the European Union, future enforcement measures related to freezing of property. Cooperation between the authorities also plays an important roles in these matters.

A typical special recovery debtor

It is difficult to define a typical special recovery debtor, but the matter most commonly involves an entrepreneur debtor, who has as a result of one or more bankruptcies lost his or her property and has become over-indebted. However, the debtor continues the business activities under shell companies. Shell companies are usually close relations in the name of which property that is actually derived from the debtor’s activities and is under his or her authority can be accumulated.
Another significant group of special recovery debtors are financial criminals, who incur debts rapidly after the exposure of abuses due to obligations to pay damages associated with Tax Administration enforcement or crimes. Such actors are prepared for the exposure of abuses and have attempted to arrange their property in advance so that it is possible to avoid paying damages.

Both types can be clearly considered grey economy actors and special recovery debtors are often the target of measures by other authorities, such as the Police, Tax Administration or Customs. However, it is notable that enforcement’s own measures and investigations also lead to actions targeting the debtor with regard to other authorities, for example, in the form of tax audits conducted by the Tax Administration or criminal investigations by the Police. The number of reports made to other authorities continues to rise. In this way, enforcement also participates in revealing the grey economy.

Special recovery debtors
Debtors are mainly transferred to special recovery via two routes. In practice, this means that suspicions about the debtors abuses either arise during normal enforcement processes which are not practical to investigate in normal process due to the amount of work involved, or the need for broader investigation work and enforcement measures involving a large amount of work is detected in conjunction with measures initiated by another authority and enforcement.

A total of 495 new debtors were transferred to special recovery in 2013. Taking into consideration debtors transferred during the previous statistics year, 1,141 debtors were the target of special recovery measures in 2013. The statistics showed that the processing of 498 debtors was completely finished during the year. The need to initiate special recovery measures became apparent for 133 debtors in conjunction with measures initiated by other authorities. Based on observations made by enforcement itself, a total of 362 new debtors were transferred to special recovery in 2013. The total sum of money for the debts and preventive measures transferred to special recovery for processing was EUR 216.3 million.

Productivity of special recovery
The amount of money deposited to special recovery creditors was approximately EUR 39.2 million in 2013. The monetary result of special recovery activities is also transferred to creditors by other means than the deposits of funds directly from special recovery. Investigations and measures initiated by special recovery often serve as an incentive in terms of signing contracts and have a direct impact on payments made to the creditor. During enforcement procedures, creditors and debtors agreed on EUR 1 million in payments, and EUR 1.7 million was otherwise paid directly to creditors during enforcement procedures. Some EUR 15 million in property was assigned from special recovery to some other enforcement body for distraint or seizure. Property with a value of some EUR 19 million was transferred to cooperation authorities, death estates or creditors as the target of seizure or other measures.

Taking into account all of the above-mentioned amounts, the monetary outcome in 2013 was approximately EUR 76.5 million. The comparative figure for 2012 was EUR 36.7 million. The value of property that was the target of distraint or seizure in special recovery was approximately EUR 99 million. This property will only be realised as a monetary result at a later time.

It is difficult to measure the success of special recovery in preventing the grey economy, but the expansion and establishment of activities are visible in the results of special recovery. Successful activities have contributed to strengthening the position of special recovery as part of prevention of grey economy achieved by means of official actions. Effective action by the enforcement authority is at the heart of combating the grey economy. The results obtained by expanding special recovery by enforcement are encouraging, and as a result the participation of enforcement in preventing the grey economy has been more effective.

There is no certainty concerning the continuation of additional funding allocated to combating the grey economy after the current government term. If the additional funding does not continue after 2015, the small staff of special recovery will likely have to be further reduced. Like the entire public sector in general, enforcement is the object of large savings targets. Enforcement is attempting to respond to these savings targets by means of an ongoing structural reform. Among other things, the structural reform will examine enforcement work methods and practical use of the staff in different tasks. At the same time, the position of special recovery in the enforcement procedure will certainly be examined. It is hoped that the organisation that has now been built and has proven very functional could continue in its current form, at least until the enforcement structures are adapted in the reform.
Corporate recovery

Corporate recovery is directly related to the role of enforcement in preventing the grey economy. About 10% of enforcement debtors are legal persons, which means different types of companies. Enforcement has already attempted to improve the conditions for enforcement in recovery that targets companies for several years. Corporate recovery requires special expertise and although it is now handled as part of the normal enforcement process, assigning it specifically to experts in the area is certainly justified in the future.

Different assistant enforcement officers naturally have different types of expertise in relation to corporate recovery and business. Corporate recovery training has been a focus of enforcement, and since 2012 the obligation compliance report produced by the Tax Administration's Grey Economy Information Unit has been an important tool in terms of supporting corporate recovery. This report produces a comprehensive information package to support decision-making in corporate recovery and its content provides good support for enforcement's information needs. Earlier, collecting the same amount of data required inquiries to several different authorities. Today, the assistant enforcement officers usually have access to that information on the same day. At this time, enforcement is the biggest customer of the obligation compliance reports in terms of numbers of reports. The Grey Economy Information Unit has also compiled two phenomenon reports concerning companies that have had to go through the enforcement process. The information obtained from the reports was and can be utilised to renew enforcement methods and corporate recovery.

The normal enforcement process

The above describes special recovery and corporate recovery, which were especially developed in enforcement to improve prevention of the grey economy. However, in terms of the preventive effect that enforcement has on the grey economy and its impact even in individual cases, the enforcement measures performed during normal enforcement processes are most important.

The sums of money collected by enforcement make up the majority of results of normal recovery work, and enforcement is visible to the general public by means of the work done in normal enforcement. Despite the fact that massive numbers of cases and debtors are handled in the normal processes, normal recovery also handles so-called demanding cases in addition to corporate recovery. In borderline cases, the line between demanding recovery performed in the normal recovery process and special recovery may naturally vary quite a bit. However, the amount of work required for a debtor report can be considered to be the differentiating factor. The normal process cannot focus too much on investigating a few demanding cases, and large numbers of debtors must be handled in a prompt and appropriate manner as prescribed in the law.

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