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PATTERNS OF INFORMAL TRADE IN PETROPAVL, KAZAKHSTAN

ҚАЗАҚСТАННЫҢ ПЕТРОПАВЛ ҚАЛАСЫНДАҒЫ БЕЙРЕСМИ САУДАГЕРЛІК
ӘРЕКЕТТЕР

НЕФОРМАЛЬНАЯ ТОРГОВАЯ ДЕЯТЕЛЬНОСТЬ
В ГОРОДЕ ПЕТРОПАВЛОВСК, КАЗАХСТАН

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by

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A Thesis Submitted to the School of Humanities and Social Sciences of Nazarbayev University
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List of Abbreviations

RoK	Republic of Kazakhstan
ILO	International Labor Organization
USD	US Dollars
USSR	Union of Soviet Socialist Republics
SME	Small and Medium-sized Enterprises
GDP	Gross Domestic Product
WTO	World Trade Organization
KZT	Kazakhstani Tenge
MCI	Monthly Calculated Index
VAT	Value-added Tax
LLP	Limited Liability Partnership

Abstract

Several factors constrain or enable informal trade, ranging from the living conditions of the population, for whom it is often the most viable form of livelihood, to the national institutional framework, to the typology of goods being traded. The characteristics and extent of informal trade are explored in light of the observation of these activities in the northern region of Kazakhstan. The analysis, based on fieldwork and interviews with key stakeholders such as traders, tax inspectors, and local authorities focuses on the practices and interacting institutions of informal trade. The findings show that traders employ two methods to bypass state regulations: personal networks based on trust (*blat*), or pecuniary exchange with or without personal connections. The thesis explores what determines traders' choice of one method or the other in any given situation. Labor market rigidity, weak institutions, the tax system and excessive financial regulations are identified as major drivers of the development of informal trade activities. Thus, the findings suggest that informal trade is a response to changes in market conditions and regulatory regimes, especially under the adverse social, economic, and even political outcomes of the current economic recession.

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Chapter 1 Introduction: Puzzling Informality

After the collapse of the USSR, the newly independent countries began a transition away from a centrally planned economy to a new reality based on the market economy. In Kazakhstan, like elsewhere, this period brought significant difficulties and uncertainties to the planned economy that led to the continued growth of the informal economy. Radical market reforms, the change of socio-economic development model and formation of the free market economy could not help prevent this type of economic activity. In turn, this illustrates that reforms conducted after independence created a new institutional environment that was inadequate to the functioning of business in a formal economy.

The informal economy in Central Asia has deep roots, but prospered particularly during the Soviet era, when the planned economy could not manage the demand for goods and services efficiently (Ledeneva 1998). A centrally planned economy is generally associated with communist and socialist governments such as the former Soviet Union and China. It is an economic model in which governments tightly control the supply and demand of goods and services. Advocates of a centrally planned economy argue that this is a much more efficient way to make sure a country's resources are put to their best and highest use. Yet, critics of centrally planned economy point out that ultimately, governments are unable to control market forces such as supply and demand. As a result, inefficiencies affecting both production and the allocation of goods result in the shortage of commodities and other consumer goods because of ineffective production as well as the allocation of goods. For example, Gorbachev implied that strict regulations and total planning promoted the informal economy: "A serious fault of the political

system was the Stalinization of social life. State regulations extended practically to all activities in society. Total planning and centralized control of all aspects of life literally limited the initiative of people, organizations and collectivities, giving rise among other things to a “parallel” economy that took advantage of the inability of state organs to satisfy people needs” (Gorbachev 1993, 11; translation from Spanish by Lomnitz and Sheinbaum 2004).

Thus, the enduring nature of the informal economy in Kazakhstan can be explained in light of its historical, cultural, and political heritage. Today, informal trade and its practices are a noteworthy aspect of studying because it constitutes the largest part of the informal economy in Kazakhstan. The estimated figure of informal trade makes up 22.9 percent of the informal economy of Kazakhstan, while, for example, agriculture accounted for 15.6 percent, transport for 14.1 percent, and real estate for 12 percent in 2014 (Kazpravda 2014). Recent initiatives of the Majilis (the Parliament of Kazakhstan) illustrate further the prominence of the informal economy. In November 2016, precisely out of concern with the informal sector, the Senate adopted a law designed to bring the informal economy in the open through tax reforms.¹

Research puzzle

Informal social relationships within the formal economy were studied by Lomnitz (1988) a long time ago. She claims that state power considered informal economic practices within the framework of state regulations as inevitable, and sometimes even useful. According to her, such informal activities are not chaotic but rather support a steady system of exchange based on trust and loyalty among its participants, which works in parallel to the formal rules of the state. This

¹ Law of the Republic of Kazakhstan on Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on Taxation and Customs Administration No. 26-VI of November 30, 2016 (The Department of State Revenues, 2016).

study also focuses on the informal trade activities that are based on informal institutions such as trust, loyalty, and lobbying in contrast to the formal institutions.

This study is mainly interested in the puzzle of how do traders circumvent state regulations? In other words, this thesis analyzes the informal trade practices of traders in the bazaar who are supposedly monitored by formal institutions. Scholars usually focus on bazaars in Almaty or Astana, or the larger bazaars of Kyrgyzstan that are supplied with goods from China. The informal trade networks in northern Kazakhstan have not been discovered until now. I investigate the largest bazaar of the Northern Kazakhstan, Altyn Arman (formerly Kolkhozni rynek), which is mostly supplied from the Russian Federation. More specifically, by observing informal practices in this bazaar, this study uncovers the dynamics through which informal trade adapts to formal regulations.

Moreover, Altyn Arman is a useful research site to focus on for two reasons. First, it is the largest market in Petropavl, North Kazakhstan region. Most traders import their goods from Russia and sometimes Kyrgyzstan for distribution to local shops. This underscores the fact that Altyn Arman is the main hub for bargaining and trading processes in the North Kazakhstan region. Second, officially, payments in the bazaar are made in cash only, which opens a myriad of opportunities for informal practices.

To clarify, this study does not examine patronage politics, property rights, or power dynamics (Spector 2009), historical development and gender dynamics of informal economy (Werner 2004), size of the informal economy, poverty, and child labor (ILO 2013a) like other studies do. Moreover, it does not focus on illicit, or criminal economic activities of the underground economy either (the distinction between informal and criminal economy is elaborated in section 2.1). Rather I focus on the daily life of the traders who openly trade in the

bazaar, yet circumvent certain state regulations, thereby engaging in informal economic activities. Thus, the study can shed light on the drivers of microeconomic processes such as decisions and performance of individuals, or single businesses in contrast to aggregate expenditure and consumption of a nation, unemployment, inflation, and GDP issues in the overall economy. The findings of this study are relevant to the conditions found in other bazaars in Kazakhstan and post-Soviet countries.

The thesis is structured as follows: the next section reviews the key concepts describing the informal economy. In the first place, I define what informal economy is, the importance of interpersonal networks, pecuniary exchange, and the role of bazaars. Section three introduces the hypotheses guiding the study. Section four presents the methodology emphasizing aspects like sampling, research ethics, data collection and analysis. Sections five and six, contain the main findings of the study.

Chapter 2 Key Concepts in Analyzing Informality

Addressing this puzzle first requires answering questions like: what is the informal economy in the first place? What is the role of personal connections within informal trade activities? And what is the place of bazaars in the informal economy? Clarifying these aspects is instrumental to understanding the range of informal trade activities in the bazaar economy.

First, I discuss the concept of informality and its social, economic, and political role in the economy. This is important because, often there is confusion between the informal and the illegal or criminal economy. I then use these insights to come to a definition of *informal trade*.

Second, I consider the concept of personal networks, which forms the basis for the occurrence of the majority of informal economic activities taking place in bazaars.

Third, I review accounts of the informal trade mechanisms commonly observed in bazaars around the world, with a particular focus on post-Soviet countries.

2.1 Defining the informal economy

For many years, researchers have struggled to find a consensus definition of the informal economy. Studies on the Soviet and post-Soviet informal markets highlight an interrelation between informal and illicit activities (Chen 2005; Sik and Wallace 1999; Bernabe 2002). Studies on the informal economy in Latin America and Africa illustrate that informal activities can turn illegal and harmful (Dell'Anno 2008; United Nations Economic Commission for Africa 2010). However, while both types of activities are illegal in the strict sense of the word, a distinction must be established between the informal economy and outright criminal activities. Karrar (2013) argues that “[informal work] encompasses work that is basically licit but takes place outside the regulatory apparatus ... In other words, this is work that could have been done in the formal economy, unlike the criminal activities” (pp.461-462). For instance, while selling

popcorn on the street is not illegal, if the salesman does not have the proper license, then he/she is evading certain legal requirements (e.g. tax, safety, and health regulations) (Meagher 2013; Bacchetta et al. 2009). This means that informal activities are not necessarily criminal. However, the problem is that people usually generalize the idea of the informal economy by including outright criminal activities. Even though informal trade is beyond legal constraints, the sector produces and exchanges totally legal commodities and services. It, therefore, should not be confused with the criminal trade generating illegal goods and services (e.g. narcotics production or distribution, prostitution, money laundering, etc.). Instead, the informal trade is viewed as a niche market that generates goods and services with lower prices for people. Yet traders do not follow the formalities established by the legal framework (Garcia-Bolivar 2006; Meagher 2013; Karrar 2013).

Some researchers state that the informal economy tends to prosper in countries with an unfair distribution of income. In other words, the informal economy is more likely to occur in less developed countries (Garcia-Bolivar, 2006; Hart, 1973; ILO, 2013a). At an official level, different countries use different definitions of informality. For instance, the governments of Brazil and India refer to the informal economy as including only enterprises with fewer than five employees (Rani 2008). In Indonesia, the informal economy is considered as only covering unpaid and self-employed family workers (Sugiyarto et al. 2006).

Others argue that informality should refer to behavior, which is unpredictable, unsteady, irregular, or invisible, as opposed to the predictable, conventional, regular, and normal behaviors found in the formal sector (Becker 2004; ILO 2013b; Gerxhani 2004; Garcia-Bolivar 2006). Thus, something can be recognized as informal when it is outside the established formal patterns. For example, Bacchetta et al. (2009) define the informal labor as “all remunerative work – both

self-employment and wage employment – that is not registered, regulated or protected by existing legal or regulatory frameworks and non-remunerative work undertaken in an income-producing enterprise” (p.53). Furthermore, researchers claim that the informal labor is about social security benefits and formal labor regulations that are not covered in the informality (Bacchetta et al. 2009; Chen 2010).

All enterprises, employees, and practices, which operate outside the formal regulations of the state, by that very fact, take place in the informal economy. The organizational forms used to manage the informal economy are considered informal institutions. Hence, informal markets are related to the organizational forms where formal regulations are closely related to informal arrangements. Clearly, the lines between informal and formal economy are blurred (Garcia-Bolivar 2006; Becker 2004; VanderBerg 2014; ILO 2013a), and indeed it is very difficult to separate the formal from the informal. The informal economy consists of largely legal activities and practices but with violations of some non-criminal laws such as the tax code, safety, health regulations, etc. In fact, the informal economy involves non-participation in at least three major areas regulated by the state: taxation, welfare and other social programs, and regulation (VanderBerg 2014). It is noteworthy to highlight that there is also a concept of paid informal economy, which is considered as a subcategory of the informal economy. This concept is seen as “monetized exchange that is unregistered by or hidden from the state for tax, social security and/or labor law purposes but which is legal in all other respects” (Williams 2011, 25). Some scholars define the informal economy as a part of the economy, activities of which are not included in the GDP (Garcia-Bolivar 2006; Meagher 2013).

In general, the informal economy includes the production of non-prohibited goods and services with no state control; informal institutions that are obedient to informal rules of

behavior; special interactions between economic subjects based on personal relations, contacts, and mutual trust. In this thesis, informality is both a sociological and empirical area of research. To put it differently, this study examines a category of human behavior. At the same time, it considers real economic actors, their conduct, and its connection to the community as a whole.

In light of these contributions, informal trade, can be defined as:

a sector of the economy, consisting of a set of informal activities without criminal nature, regulated by their own informal institutions, with the purpose of avoiding the costs imposed by state regulations, and thereby eschewing official calculations of economic performance.

2.2 Trust-Based Interpersonal Networks

The structure of community consists of social networks that in turn are based on trust (Simmel 1964). In this sense, trust is a concept that is defined culturally and investigated through ethnographic study. In other words, there is no common meaning in regard to the trust but rather various meanings in different societies (Lomnitz 1977; Rose-Akerman 2001). People who are engaged in social closeness do share and expect the same duties and rights, interests and values. They are confident in one another because one believes that the other is willing to make an exchange. “Trust then, is a relational response, not a result of blind loyalty that permits people to take risks in dealing with each other” (Rose-Akerman 2001, 543). Gambett (1988) believes that “trust is a particular level of subjective probability with which an agent assesses that another agent or groups of agents will perform a particular action [...]. When we say that we trust someone or that someone is trustworthy, we implicitly mean that the probability that he will perform an action that is beneficial, or at least not detrimental to us, is high enough for us to consider engaging in some form of cooperation with him” (Gambetta 1988, 207). Basically,

“trust is the basic, subtle, ineffable criterion that sets out the distinctions and boundaries between the “close friend”, the “friend”, and the “acquaintance” (Lomnitz and Sheinbaum 2004, p.6).

Individuals depend not only on formal institutions but also on informal personal connections such as friendship, family, neighborhood, and so on. Indeed, such institutions are regarded as the alternative way out of inadequate formal institutions. Interpersonal trust generates social networks that are an element of complicated communities nowadays. It is argued that informal networks play a significant role in developing states where the market cannot satisfy the needs of societies (Lomnitz 1977; Gonzalez de la Rocha 2001). When the possibilities of an individual are constrained, it is vital for him/her to be able to employ the assistance of social groups. In such social groups, one usually perceives strong trust to rely on it in the future when help is needed.

Blat

In the post-soviet space, the concept of trust often takes a specific meaning, which is encapsulated in the term “blat”. The origins of this word date back to the times of Catherine the Great in the Russian Empire. In 1762, she provided the charter that was officially called “Blatt” (from German “blatt” - sheet) for immigrants from Germany. This blatt included privileges such as an exemption from corporal punishment, hard labor, military service, etc. Local people in the Russian Empire called that document “blat” and a person who had such document “blatnoj” (a person with privileges) (Rg.ru 2016).

At the beginning of the 20th century, this concept passed into the slang of the criminal world and “blatnoi” began to mean members of the thieves living in accordance with the “thieves' law” (*vor v zakone*), and with people more or less involved in the criminal community (Ledeneva 1998). Yet, in the Soviet Union of the 1940s, the expression “Blat is stronger than the

Council of People's Commissars" (*Blat sil'nee Sovnarkoma*, which was the name the Soviet government used between 1917 and 1946) was widely used among masses (Kommersant.ru 2010). It means that acquaintances and bribes could turn out to be stronger than government - especially under a dictatorship.

In the Soviet Union, the word "blat" acquired a different meaning from the criminal world (Ledeneva 1998). Those who experienced the difficulties of those times recall how they managed to do something or achieve something due to kinship ties or acquaintance with the "right" people. Thus, people have come to use the word "blat" to refer to informal relationships, contacts, families, friends, acquaintances, and also purchases on the black market. Under the permanent inefficiencies of the planned economy, the acquisition of goods often depended on acquaintances with the sellers or officials distributing a particular commodity. To denote such useful acquaintances and the process of purchasing goods in this way, people started to use the word "blat".

Successively, informal trade practices helped a lot of people to survive in a post-communist society. When professionals such as doctors, teachers, engineers, etc. lost their jobs they started to trade informally in order to earn something. In such cases, personal relations played a significant role since it was essential to stay in the informal trade, which brings income to the family. This blat exchange continues to exist in today's informal trade practices, where people are ready to circumvent state regulations in order to earn as much as possible.

Thus, in common language, the word "blat" refers to useful connections, acquaintances, kinship through which one can get some benefits bypassing the generally accepted rules and laws, as a rule, to the detriment of the interests of society or the state. "Po blatu" means through a profitable acquaintance, through "necessary" people, including friends and family. Hence, blat is

a form of corruption that constitutes the system of informal negotiations, agreements, contacts, connections, service exchanges, and a black market in order to achieve certain results (Ledeneva 1998). This word is still widely spread across the territory of the former Soviet Union.

Blat is defined by a reciprocal bondage, which creates trust over the long period. It is considered as a non-pecuniary exchange that generates relationships and actually extracts from it. It usually occurs between people who communicate in everyday life within a given society. Indeed, blat feature of exchange is embedded in personal relationships and informal networks based on trust. In sum, reciprocity produces mutual trust in such blat relationships, each side feels responsible for their own and the other side's satisfaction with the favor within their reciprocal relationship. People trust one another because they are interested in beneficial favors. Therefore, the trust-based informal exchange of favors or goods between people who can solve certain problems is called blat (Lomnitz and Sheinbaum 2004).

2.3 Pecuniary Exchange

It is argued that informal channels in the newly independent states, which people use in order to circumvent state regulations, are a custom inherited from the Soviet Union (Ledeneva 1998). These informal channels included both personal connections and pecuniary exchanges. Yet, the use of money was not widespread as the non-pecuniary practices or blat - that were based on reciprocity and friendship during communism. These personal networks helped people to get access to goods and services necessary but limited from formal acquisition (Ledeneva 1998). Indeed, some scholars claim that in Soviet times, useful relations counted more than money (Oka 2015; Chen 2005; Schneider 2005). Such social norms of solving particular problems through informal channels of personal connections were taken for granted. In the late 1990s, it was

preferred to use coveted goods such as cognac and chocolate instead of cash (Patino 2002). The reason is that cash would deteriorate friendly relations implying bribery.

The collapse of the Soviet Union brought a transition from socialist market to capitalism. This significantly changed the way in which personal networks work, so today, personal connections are based on pecuniary relations (Ledeneva 2000; Rigi 2004; Stan 2012), and cash either complements or replaces personal networks. Value-oriented connections have been changed to self-interest or mutual benefits in capitalism (Wanner 2005). Wanner claims that “the social relationships that provided the trust necessary for widespread barter and blat exchange are being supplanted in this new capitalism by connections and networks fueled by cash. Cash payments are now at the core of the economy of favors.” (Wanner 2005, p. 530). To put it differently, unofficial connections are being transformed by the immediate exchange through cash transactions. For example, Oka (2015) found that people in Almaty are willing to employ cash in order to return a favor at once rather than building relationships, thereby escaping lengthy exchanges. This phenomenon illustrates that today one does not necessarily need personal networks but rather money in order to circumvent official regulations. It implies that monetary exchange within the informal activities are more likely to happen today in contrast to Soviet times. Starting at the end of the 1990s people had begun to rely on cash payments instead of favor payments. This change in the informal economic practices affected the behavior of the members of this system, including their mindsets and values.

On the other hand, Oka (2015) argues that Kazakhstani people would prefer to mobilize their personal connections in order to make exchanges of monetary rewards in an effective way with less risk. It means that they prefer to have any kind of personal relations even during the cash payment.

2.4 Formal and Informal Institutions

Scholars who rely on institutional theory differentiate between formal and informal institutions (Williams and Vorley 2014; Webb et al. 2009; Welter and Smallbone 2011). They define formal institutions as state regulations and codified laws, whereas informal institutions as norms, codes, and values of conduct. Of course, the state plays a dominant role in the interaction of formal and informal institutions. One of the main factors impacting the development of the informal trade is state regulations (Kaminski and Mitra 2012; Irnazarov and Vakulchuk 2014; Karrar 2013). For example, Karrar (2013) claims that “[...] government regulations play a particular important role in the rise of informal production because of the costs that they impose on formal business through their various licensing fees, taxes, and restrictions” (pp. 461-462). Researchers found that “a burdensome tax system, rigid labor market, low institutional quality, and excessive regulation in financial and products markets are determinant factors in explaining the size of the informal economy [...]” (Abdih and Medina 2013, p.3). Such factors are crucial for micro-entrepreneurs, including traders to decide whether to employ informal economic activities or not within the formal economy.

The overall impact of the informal economy is mixed. The interaction between formal and informal institutions can be both positive and negative. Kim and Kang (2009) found that during the economic transition in Russia the informal economy supported the development of small firms during the period 1992-1999. Successively, those firms have gradually emerged back into the formal economy. Empirical evidence shows that countries in Latin America sustained their economic development thanks to the procyclicality of the informal economy, with the informal and the formal economies complementing one another (Dell’Anno 2008). It is argued

that even formally registered small enterprises would not survive without the informal trade practices (Bellot 2012; Allen et al. 2017).

The Role of Bazaars

The collapse of the Soviet Union sharpened the phenomenon of informal trade (Kaminski and Mitra 2012; Cieslewska 2013; Karrar 2017; Sasunkevich 2013; Abdih and Medina 2013). The unexpected collapse of the USSR created a vacuum in the economy that was filled by the informal trade just like in other historical phases of turmoil in Central Asia. In other words, the informal trade supplied goods and services that people needed and wanted. In this respect, bazaars became the specific niche where the informal trade practices could flourish.

During the transitional period, when many state enterprises were shut down and privatized, unemployment rates started to increase. People began to look for new sources of income, and they found it in bazaars employing informal ways of trading (Kaminski and Mitra 2012; Cieslewska 2013; Karrar 2017; Sasunkevich 2013; Abdih and Medina 2013). For example, the bazaar economy still has related to the economic, political, and social transformations in Kyrgyzstan during the last 25 years (Karrar 2017). The labor market has not stabilized yet, and most Kyrgyz people still rely on bazaar trading as their main source of earning. Employers try to informally hire low-paid employees in order to decrease operating costs with no social and other benefits for workers.

The informality of the Soviet Union still lives in the minds of local people. In other words, traders in post-Soviet countries are more likely to participate in the informal economy rather than people living in the West (Sasunkevich 2013; Oka 2015). Hence, the mentality of people can support the existence of the informal economy even if a government and other formal institutions work properly. “Casual” trade is a daily practice rather than survival strategy for traders in

Belarus, for example (Sasunkevich 2013). It has become a part of social life of local people. People have social ties due to informal reasons such as friendship and family ties as well as formal reasons like professional relations. However, in most of the cases, major reasons for people to start bazaar-trade are income and self-sufficiency issues. In this respect, people engaged in petty trade are forced to do that in order to earn money (Bruns and Miggelbrink 2012; Gonzalez-Gomez and Gualda 2014).

In Central Asian states, informal means based on kinship have a long tradition. However, the free market has changed the nature of strong kin networks (Schatz 2004). Schatz who explored changes in the community of Kazakhs notes that “the partial and uneven monetarization of the economy allowed cash to provide some access to political, economic, and social goods. Suddenly, those with financial resources found it possible to forge relationships through easy payment, a practice that could be used to complement or in some cases replace the exchange of favors or the ties of kinship.” (Schatz, p.154). However, it is wrong to claim that monetary rewards completely replaced personal networks. Personal networks still create conditions for informal means, especially among friends, relatives, colleagues and so on. Therefore, it is important to understand which type prevails under what conditions for the purpose of circumventing state regulations.

Chapter 3 Explaining the Patterns of Informality

The literature reveals that people involved in the informal economy, particularly traders in bazaars, engage in informal economic practices because of different reasons - whether to maximize their earnings, save time, bypass bureaucratic and other regulations.

Consistent with the existing literature reviewed above, it is assumed that two methods are available to traders to bypass regulations: (a) through personal networks based on trust and loyalty. In this respect, trust-based personal networks include kinship or families, close friends, friends of friends, acquaintances, and further relations (informal cultural institutions). Hence, traders can circumvent state regulations “po blatu” (see section 2.2), which is through “right and necessary” people; and (b) through bribes without personal connections. In this case, traders can avoid personal connections and escape building further relationships by offering pecuniary advantage to certain interested parties.

However, this leaves unaddressed the question of what determines which method will be chosen in any given case. To address that gap, the following hypotheses are put forward:

(H1) the closer the degree of blat - that is, the social distance between individuals the smaller the favor.

(H2) the greater the social distance between individuals, the larger the favor required, and the greater the resort to monetary bribes.

The two hypotheses identify the social distance between persons as the key variable to understand how they interact through informal practices. The social distance between people can be observed and examined through different situations depending on problems that traders face in a bazaar. Bazaar is a market where people go daily to buy groceries and basic household items. It is also a place where traders must comply with existing state regulations. This is where

informal economy meets consumers as well as state inspectors. Informal economic activities operate outside of state regulations because sometimes it is very hard and unprofitable to follow all state regulations. In this case, the level of issues and obstacles can determine a method that traders will choose; either personal networks or pecuniary exchange within the social distance.

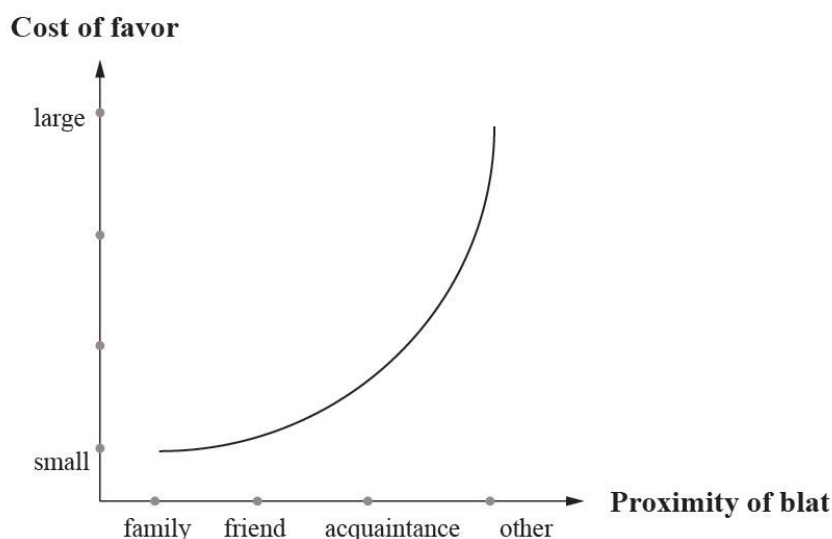
To clarify, state regulations consist of mandatory tax payments, high load of bureaucracy and so on. Personal or social networks are known as a set of human contacts with whom a person can interact with to support a certain set of activities. Such networks are usually mutually beneficial and help traders to avoid the inefficiencies of formal regulations.

Trust is a central and complex concept that plays an important role here. It can be understood differently in various cultures and societies. Yet, it is generally linked to the level of relationships between people who share the same values. For example, one can trust more his/her close friend than his/her acquaintance, while having a relationship with both of them. In fact, it is a central element of cohesion between actors creating a social network. “Social networks based on trust might allow individuals to cope with the imperfections of a given socio-economic system (state or market dominated), but they might also serve to erode the institutional frame of states by facilitating less desirable transactions (corruption)” (Lomnitz and Sheinbaum 2004).

Figure 1 below stylizes how the level of social distance between people engaged will determine the reliance on different types of informal social institutions to maintain their position in the informal economy (the cost of favor) between people within the informal trade activities.²

² This figure is drawn with the sole purpose of visualizing the relationship between the scale of blat and the scale of favor that will be paid. In other words, this exponential curve does not necessarily illustrate the exact relationship between two axes but rather approximately tries to visualize that relationship. Moreover, this favor must not necessarily be represented in money, but also in any tangible as well as intangible goods and services.

Figure 1. The relationship between social distance between individuals and favor in the informal trade practices



In this sense, the social distance between members of society, which implies the level of trust between them, defines the type of favor that will be asked. It is trust-based relationships (*blat*) and money-based interpersonal networks (*vzyatnichestvo*) with or without trust-based relationships that create the base for the informal trade practices in order to circumvent state regulations. It means that people can move from one group to another depending on their interpersonal exchange, and one can become a close friend of another after being his/her acquaintance; or vice versa, people can lose their close relationships and become acquaintances to one another.

Chapter 4 Methodology

This project uses qualitative methods to answer a *how*-type of question. It does so by collecting the real stories of the participants illustrating certain patterns of informal trade practices among

traders in bazaars. The analytical challenge I address is to observe how informal traders bypass state regulations such as tax payment and bureaucratic burden. Thus, the aim of the investigation is not to make causal inferences in response to a *why*-type of question.

Data on informal activities of micro businesses are limited since researchers mostly focus on the macro-level dimension. National statistics mostly present estimates of informal activities by illustrating numbers without elaboration of mechanisms employed in the informal trade. This research, therefore, tries to focus on traders who respond to any changes in the market. Since the study is qualitative it brings a discussion through interpretation, where knowledge comes from people – a part of certain phenomenon.

4.1 Data collection

This study relies on ethnographic case studies, formal and informal interviews, and the analysis of official documents. These methods complement one another in accordance with a triangulation strategy (Merriam and Tisdell 2015). It means that the research involves more than one method of data collection, including semi-structured interviews, observation, and primary sources like official documents. When a researcher talks to participants and asks them questions, he/she is not watching or observing. Hence, it is more likely to miss some important patterns only by talking to participants. In contrast, it is more useful to also question people you observe. Thus, the possibility to capture as much information as possible is increasing. In addition, review of legal documents helped me understand the rules and constraints that traders face and must comply with.

I spent about two-three days per week during the three months of fieldwork in Petropavl. I conducted 18 in-depth semi-structured interviews with people of various professions, ages, gender, and ethnicity. The occupation of the participants in this research is important because it

reveals the details of the phenomenon, in particular, the relationships between economic actors in the informal economy. The semi-structured interviews lasted for around 40-60 minutes based on open-ended questions. Even though the questions were prepared prior to the interview, some were asked spontaneously flowing from the context of the discussion. In this way, semi-structured interviews allowed my respondents to raise issues that I had not considered before the interviews. The responses were recorded through an audio recorder with the permission of the participants. I phrased the questions in a way that made respondents to give as detailed answers as possible instead of saying simple as “yes” or “no” answers (see Annex 1).

However, sometimes I talked to respondents in an informal way without any kind of record. It is very useful to capture all information that can be overviewed later on, especially when the focus of the study is about informality.

Most respondents had no problems discussing and sharing information on the topic. They did not mumble about their informal activities related to bribes and personal connections. I assume that they consider such activities as part of their everyday work. Of course, they realized that it is about corruption no matter whether it is voluntary (bribing) or forced (extortion).

Paragraph-by-paragraph coding was used in respect to interviews in order to illustrate descriptive analysis bringing the idea of what people experience. Since the interviews were audio recorded there was time to analyze the information successively. A transcription software was employed in order to proceed to paragraph-by-paragraph coding. Once all interviews were transcribed I could code each paragraph and identify common, repetitive, or emergent themes. Thus, I came up with particular patterns in the informal trade activities such as resort to social networks, bribery, and ability to negotiate.

Observation was used to observe everyday life of traders. To clarify, I observed how traders sell goods, negotiate with buyers, and interact with other traders. Particularly, this method helped me see when traders provided receipts and when they didn't. In addition, I was able to see how the traders behaved when a consumer asked for a receipt. This method allows a researcher to get real first-hand insights into what traders do and how they perceive a job. Observations were recorded through note-taking method. It is the simplest method of recording but it allowed me to record everything I observed.

Lastly, I studied the existing legal documents to establish the formal institutional framework. Specifically, the documents I reviewed are: the Tax Code and Customs Code of Kazakhstan, the Law on Regulation of Commercial Activities of Kazakhstan, and the Code of Entrepreneurs of Kazakhstan. They are used to understand all the rules and limitations traders face, and which can lead to the informal trade activities. In addition, this helped to construct the interview questionnaire and identify which formal institutions may be replaced by informal ones.

This triangulation strategy was helpful to check the validity of information through different methods of data collection. For instance, it is possible to check information that was given in interviews through an on-site observation, or through documents related to the phenomenon. Furthermore, triangulation strategy is helpful in supporting the internal validity of findings since it is difficult to have an objective "truth". For example, Maxwell (2013) argues that "validity is never something that can be proven or taken for granted. Validity is also relative: It has to be assessed in relationship to the purposes and circumstances of the research, rather than being a context-independent property of methods or conclusions." Nevertheless, I agree that triangulation strategy helps to improve the quality and decrease the bias of the study.

4.2 Sampling

This study targets three groups of respondents for a total of 18 individuals (see Annex 2). The first group (7 respondents) consists of traders working as individual entrepreneurs (*individual'nye predprinimateli*) in the Altyn Arman bazaar in Petropavl. This is the most important category of the study investigating informal trade activities. These people are main economic actors of activities that appear in the informal trade. I found one trader in the bazaar by employing personal relations and used the snowball technique of purposive sampling to have as many participants as possible. Talking to key informants directed me to people who provided further information. Indeed, I interviewed not only owners of certain businesses but also his/her subordinates (e.g. seller, accountant, middleman etc.).

The second group (9 respondents) targeted state officials whose work interrelates with the performance of bazaar traders. People in this group are seen as agents of state power who control and regulate the work of the traders within the framework of appropriate laws. Indeed, these inspectors are those who meet halfway with traders if there is a problem, thereby involving in informal trade practices too.

To be more specific, this target group includes civil servants who work in state agencies and control the work of traders. I talked to three tax inspectors of the Department of State Revenues in Petropavl city. These people are authorized to control and ensure the completeness and timeliness of tax income, customs, and other obligatory payments coming to the state's budget. Hence, they provided information regarding certain state regulations and rules that traders have to comply with. The employees working in the office provided me the information regarding various issues in local trade, including informal practices. In addition, I interviewed one prosecutor working at the prosecutor's office of Petropavl regarding criminal issues in the

informal trade. Prosecutors monitor whether traders comply with the execution of appropriate laws acting on the territory of Kazakhstan. The respondent provided me information regarding problematic issues in regard to traders in the bazaar and city as a whole. I also talked to a fire inspector who inspects whether traders comply with the law in terms of preventing fires in a boutique. He checks buildings, offices, industrial premises, shops, bazaars, and other facilities for their compliance with fire regulations and rules. The officer issues instructions with a list of any identified violations and their specific elimination deadlines. The inspector, on fire security supervision can bring the infringer to administrative responsibility: impose fines or issue a warning letter. Another representative of a target population is an inspector of sanitary and epidemiological service. He records the registration of the inspection, which is signed by an inspector and a trader. Traders get a notification about inspection a month beforehand for the scheduled inspection and a day beforehand for the unscheduled inspection. If any inconsistencies are revealed, a protocol on offenses is drawn up in accordance with the Administrative Code, which is later to be referred to the main state sanitary doctor of the territory where the inspected object is located. If minor violations are found, then the businessman is brought to an administrative fine and within three days, the statement of claim is sent to the court. Furthermore, I talked to three officials from the city's akimat.³ Officials working in the akimat conduct a nation-wide policy of the executive power by monitoring the implementation of strategic plans, regional programs for social and economic development.

The third group consists of two employees working in the National Chamber of Entrepreneurs "Atameken". The respondents provided information regarding problems that traders usually face, how they try to solve certain problems and so on. The mission of the

³ Akimat is a regional body of executive power that has many tasks, including coordination of the activities of law enforcement and other state agencies in the fight against crime and corruption, ensuring the rule of law.

Chamber is to protect the rights and interests of business and to ensure the wide coverage and involvement of all entrepreneurs in the process of forming legislative and other regulatory business rules. When a trader has a particular problem with any type of state regulations, he/she comes to the chamber in order to consult with employees of the Chamber.

The sample size is relatively small since I rely on qualitative research. Sampling in qualitative research is not built to be representative of a wider population as it is in the quantitative research. Rather, it aims to capture diversity around a particular phenomenon. Data collection through observations and conversations is not focused on a statistical sense but on the identification of representative events and people that can be analyzed in depth. In fact, each group of respondents provided necessary information regarding the informal trade activities by bringing various stories and views from different angles of the same phenomenon.

4.3 Research Ethics

Since the investigation is about informality, it is closely related to illegal aspects, notwithstanding the necessary distinctions between the two fields as illustrated. Informal is in fact illegal even if not necessarily criminal, though criminal implications may result from illegal activities involved in informality. Therefore, there might be particular ethical issues during the investigation. I stressed the necessity of informed consent. It illustrates that participation in the study is voluntary and participants have certain rights during the interviews. For example, they were able to withdraw from the research at any time.

In order to reach a participant, I employed a verbal informed consent form. This consent form states that all demographic marks about the participant are anonymous and the information is secure, except for their occupational information. Furthermore, all respondents were assured that their names are replaced by pseudonyms and the data is protected and used only for

academic purposes. All the field notes will be destroyed in one month after the completion of the research project, while audio recordings were already destroyed. Moreover, I told them that the study is not related to the moral judgments due to informal activities. The research is not aimed to discuss the wrongness or rightness of informal activities.

4.4 Data analysis

The collection of evidence is organized around the two hypotheses put forward above. I identified four types of constraints (see Table 1 below) traders face in their everyday activities by relying on the official documents and personal stories of traders and officials. Indeed, these four constraints are interrelated with one another. These constraints are associated with different formal institutions which are replaced by informal institutions. These four categories create a basement for testing the two hypotheses.

Table 1 Constraints and related formal institutions

Constraint	Formal Institution involved
Registration and permits	Bureaucratic agencies (various)
Contracts	Notarial service
Access to credit	Banking system
Tax burden	Department of State Revenue (Tax system)

First, I will look at bureaucratic issues that traders face: from opening new businesses up to everyday job. I will ask them what kind of bureaucratic difficulties they face when they open their businesses, submit reports to administration in the bazaar, pay taxes and pay for rent, issue documents to take loans, issue licenses, etc.

Second, I will look at impact of contracts, agreements between traders and other interest groups, or individuals that are usually conducted through the notarial service. In this sense, an absence of formal contracts between parties will illustrate the importance of personal relations.

For example, I will ask traders whether they create a contract when they borrow money from other people, not banks. I will focus on their alternative ways of formal agreements that can ensure that a trader will repay the borrowed amount within a certain period of time. Certainly, the amount of money and, more importantly, the social distance between individuals will impact the process.

Third, I will look at the credit system, in particular, how traders borrow capital when they need it. I need to ask traders “what are the alternative ways of getting the necessary amount in order to open, maintain, or expand their businesses?” In this case, I will ask them who usually assists them if there is no way to take a loan from the banks. It is important to know the significance of social distance when they borrow money. In other words, as a rule, when an individual takes a loan from the bank, he/she must pay it back with an interest. Informal practices can be different when, for example, your family or close friends will not charge an interest.

Finally, I will look at how traders evade taxes by relying on blat and pecuniary exchange. Tax evasion is an illegal and deliberate avoidance of payment of taxes by individuals or legal entities. The methods of tax evasion in regard to traders depend on the regime of taxation on their businesses.⁴ Generally, the main ways to evade tax payments are closely related to official

⁴ I derived two categories of tax payment regime by relying on legal regulations such as the Tax Code of the RoK as of January 2, 2017, the Code of Entrepreneurs of the RofK as of December 28, 2016, and the Law on Republican Budget of the RofK on 2015-2017 as of November 30, 2015.

All entrepreneurs must register in the tax agency prior to commencing his/her activities. Only after that process he/she can choose the taxation regime within which he/she will work. According to the Code of Entrepreneurship, there are three types of entrepreneurship in Kazakhstan: small, medium, and large. Each type is defined by a number of its employees and the amount of its average annual income. For example, there are subjects of small-sized entrepreneurship that must have no more than 100 employees and no more than 300,000 monthly calculated index (MCI) ($300,000 * 2,121 \text{MCI} = 636,300,000 \text{ KZT}$) of average annual income. Moreover, this small-sized entrepreneurship has subjects (traders) of micro-entrepreneurship that is defined by having no more than 15 employees and no more than 30,000 MCI of average annual income ($30,000 * 2,121 \text{MCI} = 63,630,000 \text{ KZT}$), established by the law on a republican budget. The focus of the thesis lies on the latter category of traders who actually can operate within two types of regimes: patent-based entrepreneurship and individual entrepreneurs with a simplified declaration, according to the Tax Code. Hence, each group has different forms of tax payment during

reports of personal income and profit of organizations. Hence, I need to ask traders whether it is necessary to use personal relations in order to evade taxes, or if they can avoid payment by using other channels. Moreover, I will talk to tax inspectors who are directly involved in the process. I will ask them how much traders usually pay for their taxes since inspectors check declarations that traders fill in. Declaration indicates the amount of income of traders, including the amount of taxes and pension contributions to be paid.

Traders are more likely to use either personal networks or monetary bribes in order to save time and nerves. How much costs they will spend on the informal trade practices will depend on their personal relations (*svyazi*) and impersonal methods (money). For instance, I will investigate whether the relative in the tax department will help them for free, or one will get money or another favor in return.

The next two sections try to test the two hypotheses through the lens of blat and pecuniary exchange. Each of these methods discusses four major constraints mentioned above – permits and registrations, contracts, access to credit, and tax burden. These subsections include personal stories of respondents that give various examples of informal trade activities they experienced. Thus, informal trade activities illustrate certain patterns where personal connections and pecuniary exchange take place.

their activities (see Annex 3). Indeed, the study shows that they use different strategies of circumventing state regulations based on the state restrictions.

Chapter 5 The Importance of *Blat* in Relationships Characterized by Close Social Distance

5.1. Registration and Permits

Traders who ever tried to start and maintain a business continuously face bureaucratic issues such as getting a permit, license, paying taxes, etc. Such burdensome state regulations incentivize the recourse of traders to informal practices.

As discussed in section 2.2, there is a system of exchange between members of a society based on trust, which is called *blat* in Kazakhstan. For instance, traders working in the bazaar sell their goods on the streets without any formal documents and licenses during the summer. It seems that the informal trade is fully controlled by certain state agencies, yet traders continue to trade informally by relying on *blat*. One trader, named Kuanysh (respondent #5), who sells ice cream, talked about his last-year experience in the informal trading:

“There are certain streets in Petropavl where the sale of goods and services are prohibited by local law. Yet, from time to time during the summer traders of the bazaar go and sell their commodities there. I was one of them last year because I had personal connections (lichnye svyazi) in akimat of the city. A person who works there told me that he will solve problems if they arise. Indeed, he is my relative and did not ask any favor for it. I just knew that I owe him some favor if he asks it in the future. [...] So, the local inspector from akimat came to me on the street and asked me to leave or he will call police in order to penalize me (only police inspector can legally penalize individuals). So, I called my relative to solve the problem. His position was higher than this inspector’s one. They talked to each other by phone and then inspector left [...]”

In this case, Kuanysh could solve a problem by using personal networks only. It means that he neither paid taxes, nor even paid penalties for informal trading on the street. However, he was

lucky to have a person who can tell his subordinate not to create a problem. In other words, his personal connection was strong enough in order to escape the problem. Moreover, his favor in return to the person who helped him was small because it was his relative and he could easily call him.

Another story told by Talgat (respondent #8), a fire inspector, illustrates that traders are more likely to bargain when they have problems with fire security issues. He said that traders usually do not fix those problems in order to receive a further permit from an inspector but rather officially pay fines for noncompliance with the fire regulations. They claim that it is cheaper to pay a certain amount of penalty rather than changing their existing infrastructure in order to comply with formal regulations. In addition, Talgat mentioned that some traders try to use their personal connections in the fire inspection system in order to avoid fines. He claims that there are usually blat relationships among members rather than the usage of bribes. Yet, it is possible that fire inspectors receive their advantages (pecuniary or nonpecuniary) from traders they help too.

5.2. Contracts

Traders and other parties can solve particular problems through blat where trust between traders and other interest groups is the precondition for the creation of informal contracts. Contracts that appear within the informal trade are based on trust and loyalty rather than on the stamp of a notary. It is simply a verbal agreement between people who have their own obligations and functions.

Madiyar (respondent #11), an official from akimat, spoke about blat issues when he was monitoring courtyards in the city. He says that traders who work in the bazaar come to courtyards and sell their goods or services without any formal permits:

“Last year when I was raiding courtyards in the city [...] I caught a trader who set trampolines in the yards and sold the service as an attraction. I do not remember now but I think he took 300 KZT for the entrance [...] Well, I showed my service ID (ksiva) and asked him to stop his commerce and leave as a first warning. Next day, I went there to check whether he is continuing his commerce or not. He was there! [...] When I tried to call a police in order to fine him he began to call someone. It turned out that he had a relative in akimat and that relative accurately asked me to leave him alone [...] There were few cases like that.”

Eventually, a relative of that trader and Madiyar verbally agreed that in future this person will owe a favor to Madiyar if the latter asks him about something. This informal contract is usually called “I helped you today and you will help me tomorrow” among members of the community. In this situation, it seems that a trader had an informal contract with his relative, which caused another informal contract between his relative and Madiyar. Certainly, that person who helped a trader was expecting such contracts because it is impossible to sell goods and services without being controlled by the state. Moreover, such contracts are based only on trust and “honor bright” (*chestnoe slovo*) rather than on notarized signatures.

Andrei (respondent #4) argues that such activities usually occur between traders and officials during the summer season. Traders in the bazaar start to open seasonal businesses such as selling of ice cream, popcorn, barbecue (*shashlyk*) and so on. Accordingly, officials also begin to come and check frequently. According to Andrei, it is not because they care about the discipline in the bazaar but rather about informal earnings from traders. He says that,

“A friend of mine worked here too. Last summer he decided to make aqua grim for children and adults in the bazaar [...] A couple weeks later he realized that most people

asked him about drinks [...] He decided to sell various drinks except for alcohol. The latter decision was not formal since he needed a separate document (permit) for that. The next day an inspector from akimat asked him to provide a permit, which he did not have [...] My friend was lucky to have good relationship with an administrator who helped him to negotiate with that official. Ultimately, he paid 10 percent of his daily profit to that official.”

The story implies that Andrei’s friend was still in profit otherwise he would stop his business at all. The important part here is that he did use personal connections among relatives or friends. Thus, he was able to establish the informal contract between him and a civil servant. Moreover, he found a representative of the state power that can help him tomorrow.

5.3. Access to Credit

Traders face difficulties when they want to borrow money through the banking system. For instance, in order to take a loan in a bank, a trader must show a certain share of the monthly pension contribution. This amount of pension payment depends on the amount of the monthly salary of a trader. The thing is that by employing informal economic practices traders often decrease the amount of salary on paper in order to pay less in taxes and pension contributions. Thus, he/she faces difficulties in banks when asking for loans. However, traders can again rely on personal connections to solve this problem and find the money needed. Furthermore, in order to expand the business a trader relies on the informal contracts or unwritten agreements based on trust and reputation.

When a bank refuses to provide traders money, they use informal practices to reach their objectives. For example, Kuanysh (respondent #5) said that he usually borrows money from the

same wholesaler who supplies him with goods. He said that his supplier knows him very well since they have worked together for three years now:

“I remember I did not have money to purchase commodities from him and asked him to lend me commodities up to one million KZT (account payable without formal papers). He agreed and did not even ask me to make formal agreements or something like that. He just trusted me.”

Moreover, that wholesaler never asked for interest fees for that debt. It illustrates that Kuanysh could substitute his difficulties in the banking system with his personal connections, which provided him even better conditions than formal procedure. More importantly, it shows that the close social distance between Kuanysh and his wholesaler generated the smaller favor for Kuanysh to return. He said that it is known by default that he owes him a favor even though he did ask Kuanysh about it.

Saule (respondent #7), a trader from Altyn Arman, provided another story about loans and banks. She says that it is her family and relatives who help her when it is necessary for her business. Saule claims that without personal relations she would have closed her trade activities a long time ago:

“Believe me, if you want to start a business, you are better to have good personal connections with bureaucratic agencies as well as with your relatives (family, friend, etc.). It is not a secret that most of us face difficulties when something bad happens to the state economy. For example, you know that most Kazakhstani people lost a lot of money during the devaluation of our Tenge. So did I. Well, I can tell you that I lost millions of KZT and wanted to cease my business [...] However, I am happy to have my family and

relatives who provided me a certain amount of money to continue my business. Some of them did not even ask me for return [...] it was like a charity for me.”

This example shows that personal networks, in particular very close relations, do help traders stay in business when they have no other choice but stop the business. Certainly, banks are not ready to help such traders and if they do, it would have very high interest rates in return. The case of Saule also illustrates the importance of informal institutions such as trust and loyalty of her relatives that caused them to give a hand when the state cannot.

5.4. Tax Burden

Mandatory pension contributions

According to the stories of traders, it is not difficult to evade taxes or to minimize them as much as possible without having personal networks. For example, pension contributions in the amount of 10 percent are paid out from the monthly salary established by the trader. Moreover, there is 8 percent of income tax each month that needs to be paid to the government. This means that 18 percent of the monthly income is paid out to the government. In this case, a business owner must pay for each employee including himself/herself. Some employees want to pay the real amount of pension contribution in order to collect as much money as possible. It implies that the owner loses his/her money during the payment of real share of monthly salary to the pension fund. In this respect, traders who have employees usually set their informal conditions of labor, claiming that the amount of money going to the pension fund and national fund will be the minimum. It means that since the minimum wage in Kazakhstan equals to 24,459 KZT, the owner will put 2,445.9 KZT (10 percent of the amount) into the pension fund and 1,956.72 KZT (8 percent of the amount) will be paid to the national fund.

According to the traders I interviewed, it is usually about 5,000 KZT for pension and 4,000 KZT for income tax per month, illustrating the official amount of salary as 50 thousand KZT per month when it is higher indeed. For example, a cashier named Marzhan (respondent #1) told me that her real salary is 70,000 KZT but her pension contribution is 2,445.9 KZT and tax income is 1,956.72 KZT per month which is below the mandatory monthly contributions. Otherwise, she could not find a job because almost every business owner employs such practices. On the other hand, she claims that it is useful for her since her monthly salary is higher in this way: $70,000 - 2,445 - 1,956 = 65,599$ KZT; otherwise it would be $70,000 - 7,000$ (mandatory pension contribution) $- 5,600$ (income tax) $= 57,400$ KZT. Hence, Marzhan saves 8,200 KZT per month, which is a good amount of money for her. It is absolutely beneficial for the owner, and useful for an employee in the short term only. Indeed, this scheme is very useful for patent holders who work for themselves without any employees. They usually set the minimum amount of the salary for themselves. In fact, some owners contribute a higher amount of money in order to be able to get loans in the banks when necessary. According to the rules of the banking system, the capability of payment of loans is calculated based on the monthly payment in pension fund since it indicates the amount of salary one receives. In other words, the higher a salary, the more chances to get a big loan. Therefore, sometimes traders (owners of the business) try to pay a higher amount of money to the pension fund (see section 5.2 below). Moreover, according to the Law on pension of the Republic of Kazakhstan, an individual can pick any consecutive three years since 1995 as the foundation of their pension, which will be paid monthly when a person retires. For example, the owner of the business Sergei (respondent #2) claimed that he put 50,000 KZT per month in the period 2013-2016 in order to get a higher pension when he retires. However, sometimes employees complain about this way of

circumventing state regulations because they face difficulties when they want to take a loan in the banks. The cashier Marzhan said that it usually relates to the question of taking mortgage:

“With a pension contribution of 2,445 KZT per month no banks will provide a mortgage.”

Certainly, the salary is provided in cash to employees. Thus, formally the amount of salary of workers can be known only through pension payments. It means that tax inspectors cannot have evidence to claim that the owner of the business pays less or more than he/she should pay. Formally, employees get minimum wages, they do not complain about it, and representatives of state agencies cannot disturb the owner. However, not all informal trade activities occur without personal networks in the bazaar.

In this respect, one trader named Olga (respondent #3) told me an interesting story regarding informal activities. She explains how she gets additional informal income from people she knows:

“I think it is not a secret that some people come to individual entrepreneurs and ask them for a favor. In particular, a sister of my husband asked me to put pension contributions into her pension fund because officially she did not have a job but she had three years until her retirement. So every six months she gave me 50 thousand KZT and I put them into her pension fund as one of my employees. Basically, she was registered as my subordinate (cashier).”

Olga claims that she did it for free because it was her relative. She mentioned that it is fine for her and it would be inappropriate to ask her relative a favor (money) in this situation. It illustrates that such closest degree of blat kinship does not demand the return of a favor. Yet, it does not mean that all family members would act in similar way. Moreover, it implies that more distant individuals such as friends, acquaintance, or friend’s friend are more likely to pay off

higher favor than those within family. For example, Olga said that it is negotiable and depends on the level of relationships between two parties. According to her, some traders take 40 to 60 thousand KZT per year.

In contrast, there is a story where a trader obtains pecuniary advantage for the informal economic activity. Zhanibek (respondent #6), a trader from the bazaar briefly mentioned that he received 30 thousand KZT for such a favor:

“By the way, I forgot to mention that once I helped my friend’s acquaintance to get the formal monthly pension contribution. He paid me 30 thousand KZT for my favor since my friend asked me about it. In fact, I could request about 50K KZT for such a favor. Thus, I employed him as “a driver who transport my goods” for a year. To be honest, I did not even ask if he needs more years to “be employed” and pay pension contributions. It is not my business.”

It is clear that Zhanibek earned informal money through his business. In this case, it is not Zhanibek who needed help but someone else. It seems that mandatory pension contributions do not require traders to have personal networks in order to evade taxes and other costs. Moreover, traders are able to earn additional money here.

Cash registers

Officially, a cash register (machine) is mandatory for businesses working with cash. In the case of working without cash, a cash register is not necessary. However, not all traders use cash registers in the bazaar. The reason is that some of them were patent holders who can be free from using cash registers. Instead, they pay 2 percent of estimated income beforehand.

For example, Andrei said that he paid for the patent one month prior to the start of his business. In other words, he buys the patent every month because he does not know whether he will continue his business or not. Indeed, it illustrates that owners of the patent can significantly decrease their estimated monthly income and pay much less tax for their activities.

On the other hand, a trader working with a simplified declaration must pay three percent from his/her revenues, not profit. In this respect, they rely on records in the register machine in order to calculate trader's revenues. What happens, in reality, is that traders sell goods and services in exchange for cash only and often do not provide receipts for consumers. The observation showed that traders are not willing to give receipts, or even ask their customers about it unless the latter ask traders to provide receipts. Thus, they avoid recording in cash registers that later will be checked and taxed by the tax inspectors. Indeed, most traders I have interviewed said that it is usually "one to twenty" rule. To put it differently, traders will provide receipts once in twenty transactions even though customers do not ask receipts. Hence, traders want to show that they do have revenues in order to show "something" when they will meet tax inspector. Otherwise, it would be too evident that they evade taxes.

The tax department cares only about revenues of traders, not their profit. In the case of holders of patents, they believe in their estimations and accept two percent of tax from those estimations established by traders. In the case of traders with *uproshenka*, tax inspectors can rely on their records of cash registers. Certainly, the state does not receive the amount that they would receive if those traders paid fairly. In order to avoid creating a record of transactions, cash is the most common medium of exchange within the informal trade. Therefore, the informal trade seems to survive in industries like bazaars where traders accept only cash.

The trader Sergei (respondent #2) mentioned that, of course, it is easier to report to tax inspector if the latter knows you well. He says that if a trader has some personal networks in the tax department, then a trader will not be asked “unwanted” questions about his/her trade activities:

“Our businesses are small and revenues are not that high. It is rarely seen that a trader would bribe a tax inspector. Tax inspectors usually do not investigate our real earnings. Yet, it is always better to have good relationships with them because sometimes they are ordered from the central office to fine a certain amount of traders.”

According to Sergei, tax inspectors ask him to make discounts for them when those are in his boutique as a return of favor. Basically, a trader can avoid extra audit and bureaucratic issues by having close relationships with a tax inspector. In this respect, a favor in return of providing a discount for the inspector is relatively small. On the other hand, those who do not have personal connections in the Department of tax revenues are not engaged in the informal practices at all. It is rare to offer a bribe for tax inspectors during the submission of tax reports if one does not have personal connections.

To understand the situation around the relations between tax inspectors and traders in the bazaar, I talked to Gabit (respondent #15), a tax inspector in Petropavl. He provided me an interesting story about their formal inspections of shops and boutiques in the bazaar and other stores:

“Cash registers are very important for us during our audits. For example, we can check the daily revenue of any boutique at any time. The scheme is the following: I enter the store and check their cash registers. I refer to the recordings of that cash register and the amount of cash in the machine. If the amount of cash is more than it is in the records then

it means that a trader did skip a certain number of records in order to evade taxes. For example, once I checked a trader, in particular it was a cashier (not owner), and realized that she had about 100 thousand KZT in cash while it was about 70 thousand KZT in the records of the machine. The result was a penalty for an owner of the store.”

The story of Gabit illustrates that it was a formal audit conducted by him, where informal negotiations did not take place. It seems that an owner of that store did not have an opportunity to solve that problem informally. In such cases the informal networks are significant for traders to be able to find a consensus without any formal penalties for a trader. Yet, according to traders, sometimes it depends on a tax inspector's attitude and position – not all of them are ready to be engaged in the informal activities. Some respondents say that they are either afraid of being caught in bribing and other informal favors, or they hold a position of a “right” (*pravilnyj*) civil servant.

Chapter 6 The Role of Pecuniary Exchange in Relationships Characterized by Remote Social Distance

6.1. Registration and permits

It is not usually the case to resolve issues in such situations described in Section 5.1. For instance, I found such a pattern that traders are forced to employ remote relationships in order to solve the problems. Bureaucratic burden creates a ground for informal trade activities, in particular when one opens a business. When I interviewed Zhanat (respondent #9), an inspector of sanitary and epidemiology station, he talked about long bureaucratic procedures that traders face. For example, an entrepreneur needs to meet about 20-30 requirements in order to open a barbershop in the bazaar. According to the "Sanitary and Epidemiological Regulations for Communal Facilities" approved by the Resolution of the Government of the Republic of Kazakhstan No. 94 as of January 17, 2012, traders who want to open barbershops, beauty salons, or spa centers must meet certain requirements. To understand the scale of bureaucracy there is the following package of documents and permits needed to open a small barbershop (4-5 employees): personal medical status of employees, the register of disinfection means, the register of bactericidal plant registration and control, journal of the control of work of sterilizers, the register of works on cleaning and disinfection of ventilation and air conditioning systems, and program of production control. Moreover, it is necessary to find companies (that can perform various types of work) and make few formal agreements with them on: the export of solid waste, the disinfestation and deratization, the utilization of hair and nails, washing working clothes, the disposal of fluorescent lamps, medical examinations of employees and the control of sterilizing equipment. In this respect, licenses for rendering hairdressing services, manicure, pedicure and cosmetic services are not required. After meeting such requirements, a potential entrepreneur can obtain a permit from the state sanitary epidemiological station, fire department, and akimat to

open his/her business. According to Zhanat, traders do not want to wait for too long to start their businesses. He mentioned that sometimes it takes up to 4-5 months or more to prepare all documents and find necessary companies.

As a result, the potential entrepreneur loses his/her desire to do business, or he/she starts to employ informal trade practices. In other words, it is possible to circumvent state regulations even in more difficult situations, by having social networks or/and a certain amount of money. For example, Zhanibek (respondent #6), trader in the bazaar, told that,

“Sometimes it is hard to have networks in every issue. People that I know change their jobs or retire. Hence, we need to find a common language (naiti obwij yazyk) with a new person who is regulating certain things related to our jobs.”

Thus, there are occasions when traders must take a risk and offer a certain amount of money in order to solve his/her problem. Zhanat mentioned one entrepreneur who wanted to open a barbershop in the Altyn Arman bazaar:

“He was a friend of my former colleague who asked me to help him with bureaucratic procedures in order to obtain a permit as soon as possible. I consulted and advised him in preparation of documents regarding sanitary and epidemiological regulations. As a result, I saved him about three weeks, to be honest. [...] I think he is still working there.”

When I asked Zhanat whether he received anything in exchange for his favor, he said that a trader bought him horsemeat for the winter, which is called “sogym” in Kazakh. Thus, they exchanged the favors between one another and were satisfied by the results. In other words, it seems that a trader spent a significant amount of money for sogym since its cost is about 300 thousand KZT today. Hence, it illustrates that people have a larger favor in return in such remote

social distance. It is more likely that a trader would not spend a lot of money if Zhanat were his brother.

Even though the price for certain services is much higher in the informal sector, people are ready to pay because it pays off the higher costs in the long term. In other words, traders do agree to pay a certain share to officials to avoid legal restrictions, since the informal earnings pay off those costs. If reciprocal relationships replaces the formal institutions in order to achieve certain outcomes, today the usage of money has become the central way to solve problems quickly and easily. The reason behind it is to avoid any personal debts in front of those who helped. Such monetized exchange is comfortable for traders.

6.2. Contracts

Kairat (respondent #10), an official from akimat, told me an interesting story. He said that, of course, informal trade practices happen in the city but you need very good relations (*horoshie svyazi*) in order to solve them. For instance, he caught one trader on the street selling fried corns, without any license to sell it:

“[...] So, that trader violated administrative regulation which prohibits any commercial on that street and, moreover, he did not have a special license (permission) from local sanitary-epidemiological station controlling sanitary of food. Hence, I could fine him by two articles of the Codes. I mean not me, but police [...] He started to call his friends or someone but it did not help him because that person who he relied upon did not have enough authority to prevent my intentions [...]”.

Thus, in order to not turn up in such situations, traders try to widen their circle of friends and acquaintances who can really help them in future. Such people are usually those who control

certain services within state regulations like people working in akimat, department of tax revenues, police department, and fire department. Hence, it is important for them to find new persons in their circle since there is no guarantee that those who can claim to help can help them in reality. The traders of Altyn Arman bazaar claim that they are ready to exchange favors as long as it is helpful for their businesses. According to the stories of traders, reciprocity networks initially begin with kinship and later on expand to dozens or hundreds of people.

The continuation of the story demonstrates other interesting aspects of the informal trade practices in the region. Kairat continued:

“[...] Therefore, he offered me a deal (contract) between him and me. He said that he will pay me a certain amount of money every day from his daily profit if I close my eyes and leave him alone. I was afraid to engage in such informal processes but, eventually, I agreed. However, now I faced a problem since police inspectors could come and catch that trader. Since the trader gives me an interest (dolya/procenty) I need to provide him an opportunity to sell the products. So, I talked to the Head of the police department of that region and offered him free partying (gulyanka) once a week. Thus, I solved the problem.”

Overall, we can notice three other patterns here. First, the trader, who could not solve his problem through the personal networks, could actually negotiate with the official by creating an unwritten contract between them. It demonstrates that traders can solve the problem without any personal connections. Second, the official was engaged in bribery by taking share from the trader and not “touching” him in exchange for a favor. It illustrates that the absence of personal relationships can actually be replaced by informal agreement (contract) between two parties. Third, this official could also find a compromise in the situation by providing a favor for the

person who could penalize the trader too. In other words, it is an extension of the informal trade practices, or so-called contract, which encompasses other related members of the formal system. However, the most interesting fact is that all these people did not know each other beforehand but could informally solve the problem by relying only on trust to each other. Indeed, the official from akimat mentioned that he was initially afraid to be engaged in the process but he agreed because he trusted both parties. Probably, there is a mutual solidarity, which is significant for the preservation of such networks. This example illustrates that the distant relationship between the three of them required the larger favor for each of them.

Alibek (respondent #14), a tax inspector, mentioned how he was engaged in the informal trade practices by having a certain share from the monthly income of a trader in Altyn Arman. Alibek argues that they had an informal contract between them - he does not record any violations in the store regarding tax evasion and gets a certain amount of cash in return. Such agreements are useful for both parties except for the national fund that loses money. Alibek claims that it is a widely expanded practice in the small districts (*raion*) rather than in Petropavl itself (*oblast'*). In other words, traders and officials are more likely to have informal contracts, including the pecuniary exchange.

6.3. Access to Credit

Retailers cannot always count on the good will of wholesalers to set up their business. In such situations, traders have an alternative “formal” way of obtaining the money they need.

Almaz (respondent #17), a representative of the National Chamber of Entrepreneurs “Atameken”, provided the interesting facts about this process. Basically, traders go to the banks asking for a certain amount of money but get denied. However, workers of banks give them tips on how to get a loan. They ask traders to provide informal records of their monthly revenues and

expenditures as an evidence of their profit. Traders, in turn, write additional revenues (*narisovat' dohody*) in their records in order to increase a chance of getting a loan in the bank. Bank workers, of course, know that traders show artificially increased income. Almaz argues that bank workers do that due to a necessity to get bonuses and a salary as a whole. He said that there are cases when workers of banks lose their jobs because they cannot provide their customers a certain amount of loans. The reason for that is that bankers are also responsible for spending accrued fund. Furthermore, it is not necessarily important for traders to have personal connections with bank workers. Almaz claims that many small-sized traders employ this way of borrowing money through middlemen. These middlemen connect traders who look for funding and bank workers who seek necessary customers. In this sense, traders usually pay the middleman and nothing to a bank worker. It means that the bank worker is more likely to get his interest from that middleman. The amount of favor depends on the relationship between a trader and a middleman, and between a middleman and a bank worker.

Saule (respondent #7), a trader, says that she once relied on her cousin's friend as a middleman who has very good personal networks in the city:

“He helped me to find a bank worker who could provide me a loan by relying only on my records, which appeared to be artificial since we had to increase our income. It was two years ago and, of course, my cousin asked me to pay off for his service but it was cheap. I do not even know what they gave to that bank worker. I am very thankful my cousin's help because it allowed me to stay in business during the economic crisis. [...] I sell meat and I still often provide my cousin and his friend a good discount when they or their wives come to the bazaar.”

In the case of Saule, she decreased her favor in return due to her kinship ties. She must provide something in return because it was not necessarily her cousin who helped but his friend. Her cousin was a middleman between Saule and that friend, who in turn was a middleman between Saule and a bank worker. It is more likely that her cousin asked his friend to decrease the amount of favor as much as possible since they are family. Overall, it illustrates how one's family ties can impact (diminish) the amount of favor in return even though it is not a family who helps but further relations of that family.

6.4. Tax Burden

One-day firms

“One-day” firms (*odnodnevki*) initially began to appear in the 1990s. However, during that time they served for only one or two fraudulent operations and existed for a short period of time - one to two months. That is the reason they are called “one-day” firms. Due to such a short “lifespan”, fake firms do not provide reports to the controlling state agencies.

“One-day” firms still exist and are active on average for about a year, or until they are caught by law enforcement agencies, provide formal reports to the state agencies and, as a rule, have real founders. These firms are counterparts that operate only “on paper”. However, they serve exactly the same purpose of siphoning public moneys, cashing out and “optimization of taxes” (Spravochnik ekonomista 2008). It is an ordinary legal process of opening business (limited liability partnership (LLP) or individual entrepreneurship) but with a purpose of abuse. As a rule, the only result of their work is the reduction of taxes for their legal partners or the plunder of state funds.

A typical benefit of using a one-day company is that the taxpayer reduces taxable profits and also receives the right to a tax deduction for value-added tax (VAT) by simulating the usage

of services of one-day firms (usually intangible: consulting, marketing, etc.). In fact, no services are provided, and the money transferred to the one-day company is cashed out and returned to the organizer of the fraud. With the use of one-day firms, so-called gray schemes are also used, in which pretended, not imaginary deals are involved. In this case, the customer purchases any goods or services, but the transaction does not correspond to its economic essence. For example, instead of consulting services, publicly available informational materials are sold/purchased from the Internet.

According to the prosecutor's (Sabit (respondent #13)) and the tax inspector's (Gabit (respondent #15)) elaborations, traders use one-day firms, which are often registered in the name of people who have lost their passports and do not even suspect they are formal owners of certain businesses. Today it is often homeless people who agree to such deals since they do not care about liabilities in future but rather about a certain amount of money that they can receive now. Consequently, if tax inspectors can find those people, there is a very low probability that they can collect taxes from them. Moreover, Sabit claimed that today there are no measures taken towards cancellation of tax audits results. At the same time, a collection of tax debts will be difficult due to the existence of misunderstandings (*raznochteniya*) on issues of additional taxes, which in turn raises impossibility of cancellation of taxes on counterparties. Moreover, due to various amounts of damage, it is impossible to take measures of administrative character in regard to the legal entity in accordance with Article 278 of the Code of the Republic of Kazakhstan on Administrative Offenses because sanctions of this norm consider only fines to the tax payments. The prosecutor claims that that situation won't change until radical changes of the norms of existing legislation take place. Under such conditions, a taxpayer who evades tax

payment has a great chance of escaping all types of responsibilities, and recovery of damage will be impossible if he/she has personal connections:

“I remember one case when we caught one trader who used such informal way of tax evasion. The amount of taxes was in millions of KZT, which is a very serious issue. We provided all evidence about his informal trade activities and he must be penalized for that. However, after a couple of weeks I was very upset when I knew that he bribed a judge and police and was free to go. Today that trader is still working in our city and this is unjust. I doubt that he knew that judge prior to this case but I know that this trader has a lot of money. Certainly, he could “buy” this judge by providing him money or something else. Did you see what kind of cars are parked in front of the court? ... It is funny when judges claim that these cars are borrowed from their relatives or it was a gift from someone.”

Ultimately, the period of existence of such firms is short, that is why, by the time the tax inspector starts interest in a certain case, the firm no longer exists and it is impossible to verify its reporting or even collect taxes from it. More importantly, it seems that “one-day” firms are used by traders either who have a lot of budget or personal relations in terms of solving problems afterwards. According to the prosecutor, the trader was very rich and probably spent a substantial amount of bribe on officials to solve this problem. It means that the social distance between them was more distant, which increased the amount of monetary bribes.

On the other hand, as mentioned above, traders usually open one-day firms either by using homeless people who care about instant award, or by asking people who do not care about outcomes. The latter category usually consists of those people who plan to emigrate from Kazakhstan (non-residents).

Another tax inspector, Manat (respondent #18), told me that one trader once created a one-day firm registered in the name of a Kazakhstani citizen who was planning to move to Russia forever. He said that the trader gave that man around one thousand USD as a favor. Thus, it means that traders try to use more distant relations in order to avoid any further relationships and pays off a favor at once. In case of creation of one-day firms, traders are less likely to rely on close relations such as family and friends because it is risky for the latter to be engaged in such informal practices.

Conclusion

Although informal trade practices pre-existed, Kazakhstan is one of the post-communist countries, in which informal trade practices have flourished after the introduction of the market economy. Traders in Petropavl use various informal channels in order to circumvent state regulations. Two major patterns can be highlighted with respect to the informal trade practices in Petropavl city: personal networks and pecuniary exchange. For instance, the trader from the Altyn Arman bazaar, Saule (respondent #7) claimed that,

“Sometimes when I ask my close friends who can help me with certain problems of state regulations, I do not necessarily have to pay them something in return. [...] but when I do not have such connection and refer to friends of my acquaintances I definitely must pay a certain amount of money. I think it is just”.

Traders use these two methods to bypass state regulations either through personal networks basing on trust, or through pecuniary exchange with or without personal connections. The goal of this thesis was to explore what defines which method to be chosen by traders in any given condition. I created a framework that consists of four interrelated constraints and formal institutions that impose those constraints. This structure helped me to distinguish informal solutions, which substitute formal institutions. Traders rely on informal solutions such as kinship and bribing within the bureaucratic burden; trust, reputation, and bribing within the notarial service; bribing, trust, friendship, and usury within the banking system; and kinship, “one-day” firms, fake pension contributions and profits within the tax system. Table 2 summarizes each discussed constraint in the findings.

Table 2 Mechanism of interaction between formal and informal institutions

Constraint	Formal Institution involved	Informal solutions	
		Blat (H1)	Pecuniary (H2)
Registration and permits	Bureaucratic agencies (various)	Kinship	Bribing
Contracts	Notarial service	Trust, reputation	Bribing
Access to credit	Banking system	Trust, friendship, kinship, usury from wholesalers	Bribing
Tax burden	Department of State Revenue (Tax system)	Fake pension contributions, decreased profits, kinship	“One-day” firms

First, traders face various bureaucratic difficulties such as unnecessary and repetitive requirements when they open and maintain their businesses. In order to avoid such formal barriers they employ informal solutions such as blat and bribes, thereby overcoming those barriers. As discussed above, traders employ blat through kinship relations when they need instant informal solutions like escaping penalty for trading without permits. The findings show that a trader can simply call his/her relative in order to solve the problem created by an official from akimat. Since not every trader has personal connections to solve a certain problem, the one without starts to rely on pecuniary exchange. For instance, Zhanibek (respondent #6) claims that it is necessary to find common ground (*naiti obwij yazyk*) by bribing officials. In this case, bribing does not necessarily means money but other popular favors like horse meat for the winter period. This mechanism shows that blat- and pecuniary-based informal solutions can replace the formal institutions when needed. It is argued that acceptance of bribe implies social inferiority similar to accepting tips. Indeed, any material payment in return for a certain favor is considered a graft (*vzyatnichestvo*). In most of the cases, it happens when there is no possibility to rely on

personal connections. It seems that cash payment or bribery is the last resort option if one does not have the necessary personal relations.

Second, bribing, trust and reputation replace the formal institution of notarized contracts when traders try to negotiate both with officials and non-officials. These people can exchange favors (pecuniary and nonpecuniary) by relying only on trust and reputation. The analysis suggests that it is a debt of honor among members of the informal sector that should be returned at any time. Certainly, blat does have unwritten rules that include the ethical principle of exchanges. For example, an individual who breaks such rules by not providing particular favor in return can lose his possibility (status) to employ such blat relationships in future. He becomes an untrustworthy person among members of the informal networks. In other words, in blat relations one should not cheat on others and money does not play a role here. Instead, one should share problems with his/her family or friends in order to show that he can obtain or provide support. Breaking these unwritten rules have relevance to policy concerns such as aspects of tax revenues, criminal law (potential implications in health and labor safety), social welfare implications, abuses from users and public officials (blackmailing, racketeering). When a trader cannot rely on blat relations, he tries to make a deal (contract) with a third party. In this sense, a trader offers an interest (*dolya/procenty*) in the form of money to others in order to solve problems. On the other hand, offering cash is not only an informal way to speed up a certain process but also a way to provide gratitude quickly. In other words, there is no need to invest your time in a long-term friendship building in order to use them in future. Hence, cash helps to pay back the debt at once. Another reason to avoid personal connections is not to be obliged to someone (return obligation) in future. It is better off to use money in order to find mediators and solve a problem by yourself. Traders in bazaars often say “*I do not want to owe something to someone [in future] (ne hochu*

byt' dolzhnym)". However, money cannot always replace interpersonal interaction. For example, in respect to graft and its illegal character, one cannot easily provide pecuniary exchange if there is a lack of trust and personal connections. Moreover, there is a market rate (*taksa*) for a certain service. It means that different factors such as financial status of "a giver" and level of personal relationships play a role here. The richer a trader is the more expensive his request will be priced by people who can help. In this respect, the solvability of the problem does matter too. If a person who wants to help assesses a situation as a difficult one, the price or favor in return will be respectively higher. In fact, the study shows people use different strategies depending on their problems, purposes, and resources acquired within the informal trade practices.

Third, traders use informal solutions such as trust, friendship and kinship, as well as usury from wholesalers and bribing, when they borrow money from the banks or other parties. Contrary to Schatz's (2004) argument, findings of the study suggest that there are still informal trade activities based on personal networks such as family, friends, and acquaintances. In this sense, trust creates solid social networks between economic actors, which eventually generate a community that can manage the problems informally. Trust-based interpersonal relationships are important for informal trade practices to be operated. Such relationships can serve as a support for opening, widening, and maintaining business opportunities. For instance, traders do rely on kinship and friendship when they have problems in the banking system. They borrow money from relatives, usually without any favors in return. Furthermore, traders can also rely on wholesalers who supply them with commodities by borrowing money without any interest rates and returns. The investigation illustrates that traders of Petropavl bazaar activate their personal connections for more effective and secure monetized exchange. Personal connections do not necessarily mean that it is about relatives, friends, and other long-term relationships. In contrast,

it can also be the short-term relationships based on practical goals. It means that such connections are employed during certain necessities only. For example, when a trader does use informal records of his monthly revenues as an evidence of his profits in the banks. In this case, middlemen connect traders and bank workers, of course, where both middlemen and bank workers get their interest in the form of money.

Fourth, tax burden promotes the creation of mechanisms of tax evasion in regard to pension contributions and cash registers employing the blat and one-day firms using pecuniary exchange. In the framework of tax burden, traders have to pay 10 percent of mandatory pension contributions and 8 percent of income tax to the government. In order to save as much profit as possible, traders in particular patent holders and individual entrepreneurs formally establish the minimum amount of salary for employees and themselves. They use such loopholes in the legislation where tax inspectors cannot prove whether it is real amount of taxes or not. Traders simply do not specify certain taxable income in tax declarations or indicate expenses that actually did not have a place, which reduces the tax base. Moreover, there are cases when traders use their businesses to help their relatives collect a certain amount of money for their future pensions without asking for any favor. Yet, some traders earn extra money from people who need pension contributions, while not working there in reality as in the case with Zhanibek (respondent #6). In addition, in order to avoid tax payments, traders rely on transactions with “one-day firms”. These firms allow traders to abuse a current legislation by evading taxes, cashing out, or money laundering. Employment of such affairs involves pecuniary exchange between traders (usually between small and big businesses) in a substantial amount of money.

Indeed, informal activities go along with formal institutions in maintaining the market. In other words, tacit state approval allows the informal trade to operate. Market-oriented reforms

usually are not able to fully provide support to market institutions, but merely increase the costs for traders in dealing with formal regulations. Hence, as practice shows, people tend to provide informal favors in order to solve a certain problem. It is true about those who do not have personal connections to rely on as well as those who do have social networks. To put it differently, all groups of people tend to be engaged in the informal economic activities if state regulations seem costly to them. Unfortunately, although labor activity is bypassing the tax authorities and contrary to the law, for traders in the bazaar it is usually the last opportunity to make a living better.

Moreover, the study shows that officials are ready to be engaged in the informal trade activities in order to earn additional income. The main reason for that is very low income of civil servants who somehow try to find another source of earnings. Hence, it is predictable from the standpoint of civil servants to participate in the informal economic activities. On the other hand, officials do take a part in such activities due to feelings of duty before relative, friend, acquaintance, etc. to help if he/she is actually able to. As study shows, they do not always ask for any favor in return. As for traders, it is more about money – whether they are engaged in personal or impersonal practices. They usually offer a certain share of money both to the officials and relatives who help them. Probably, they mostly focus on pecuniary exchange since business is their only source of income and they try to stay in business no matter the cost.

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ANNEXES

Annex 1

Standard set of questions used for the interviews

1. How do you pay taxes? Was it difficult to register your shop?
2. When do you usually face problems with state officials? Why?
3. What kind of obstacles do you face from state regulations?
4. How often do you get support from state institutions?
5. How would you assess current state regulations in comparison to 1990s?
6. How do you think Soviet past impacted the way business develops today? Why?
7. Which steps are necessary to be successful in trade (material resources, personal networks, other)? Why?
8. To what extent are personal networks important to maintain your business?
9. What kind of goods do you buy and sell? Where do they come from? Why did you choose this kind of goods?
10. What recommendations would you give in order to improve current state regulations?

Annex 2

List of the respondents

Occupation	Interviewee	Pseudonym
Traders	#1	Marzhan
	#2	Sergei
	#3	Olga
	#4	Andrei
	#5	Kuanysh
	#6	Zhanibek
	#7	Saule
Fire Inspector	#8	Talgat
Inspector of Sanitary and epidemiological station	#9	Zhanat
Employees of akimat	#10	Kairat
	#11	Madiyar
	#12	Zhanel
Prosecutor	#13	Sabit
Tax Inspectors	#14	Alibek
	#15	Gabit
	#16	Daniyar
“Atameken” employees	#17	Almaz
	#18	Manat

Annex 3

Two Forms of Tax Payment in Kazakhstan

Patent-based entrepreneurs (traders)

Traders use so-called “patent” right as the simplest way to sell goods and services in Kazakhstan, according to the Tax Code of the RoK (Article 428, point 3 and 4). Patent-based entrepreneurs are traders (individual entrepreneurs) engaged in the personal business that do not use the labor of hired workers and whose income does not exceed 3000 MCI (about 7 million KZT) for a year can apply a special tax regime based on a patent. This form of calculations with the budget is convenient, as a rule, for beginners and having small revs. The most useful thing in this case for traders is that they do not have to have a cash register in order to provide accountability in terms of fiscal receipts.

A patent is a document certifying the right to apply a special tax regime and confirming the fact of paying taxes to the budget. One must register as an individual entrepreneur in local tax committee and obtain a certificate of state registration in order to receive a patent. At the same time, a fee is paid for the registration of an individual entrepreneur in the amount of a two-month MCI, which is 4,242 KZT (2,121 KZT x 2). Further, a statement with an indication of the type of activity and a certificate of state registration, as well as a license, should be submitted to the tax committee at the place where the activity is carried out if the activity is allowed to be licensed. At the request of the entrepreneur, a patent may be issued for one month or for several months, but not more than for a year. For licensed activities, a patent is issued for a period not exceeding the period of validity of the license.

The amount of taxes on the patent is set at two percent of the estimated income claimed by the taxpayer. In this sense, the income is taken as gross with the inclusion of all costs. The entrepreneur independently calculates taxes without any calculations by applying a single rate (2 percent) to the expected income (revenue), without deduction of costs. The amount received is the cost of the patent. For example, if a monthly income without deductions amounted to 100,000 KZT, then the patent will cost 2,000 KZT (100 thousand KZT x 2%). In addition, 10 percent of the monthly salary should be paid towards pension collection.

Indeed, the mechanism for determining tax liabilities is not difficult for an entrepreneur. The cost of a patent is entered to the budget in the form of individual income taxes and social taxes in equal shares. In addition, “patenters” (except for sellers of excisable products) are exempt from the use of cash registers with fiscal memory.

In addition, the deduction of mandatory pension contributions to the accumulative pension fund should be mentioned. Traders with the patent must pay at least 10% of the minimum wage (MW is 24,459 KZT in Kazakhstan) (Uchet.kz 2016). It is very important procedure since without a document confirming the payment of mandatory contributions to the pension fund no patent can be issued for a trader.

The Tax Code provides standards that allow the cost of the patent to be recalculated depending on the actual income received. If the actual income exceeds the declared amount, the taxpayer must within 5 working days declare the amount of the excess and pay taxes from it. If the actual income is lower than the declared income, he can apply to the tax authority for a chronological investigation to determine the actual income and revise the declared income. In the case of the termination of entrepreneurial activity before the expiration of the patent, the amount of taxes paid is not subject to return and recalculation.

The patent form cannot be used in certain types of activities: the production of excisable goods; storage and wholesale of excisable goods; realization of certain types of petroleum products - gasoline, diesel fuel and fuel oil; organization and holding of lotteries (except of state (national)), subsoil use, collecting and receiving glassware, collecting (storing), storing, processing and selling scrap and waste of non-ferrous and ferrous metals, consulting services, accounting or audit activities, financial, insurance activity and intermediary activity of an insurance broker and insurance agent.

Individual entrepreneurs (traders) with a simplified declaration

Accounting and financial reports are made in a simplified manner (*uproshenka*) for traders in this category. Indeed, *uproshenka* is the most popular form of submission of tax returns. The reason is that it is easy but with no such constraints as with traders using patents. Traders with *uproshenka* can hire up to 25 employees and can have more or less sufficient turnovers. However, not every type of activities can employ this simplified form of declaration. However, I investigated those traders who are able to use this form of tax returns. Moreover, traders working in this category can earn up to 1,400 of a minimum wage (equaling to more than 34 million KZT in 2017). The tax amount is 3 percent of the revenues and pension contributions (10 percent of the monthly salary).