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# Free Movement of Persons: The Mirage of Social Security Schemes

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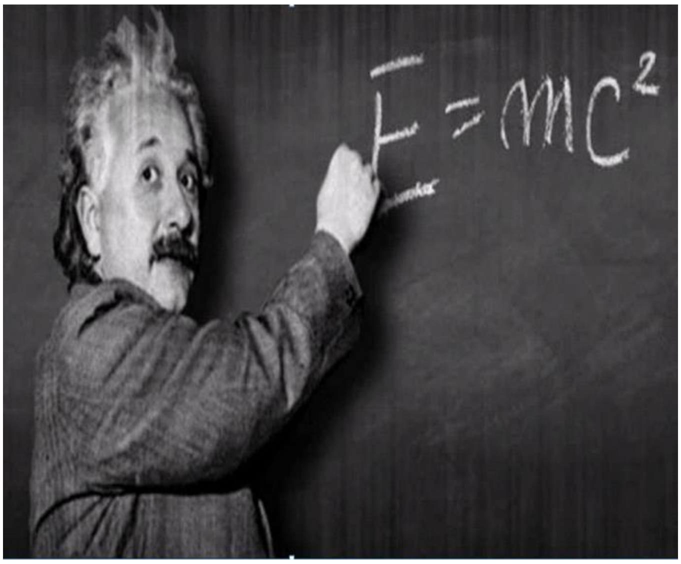


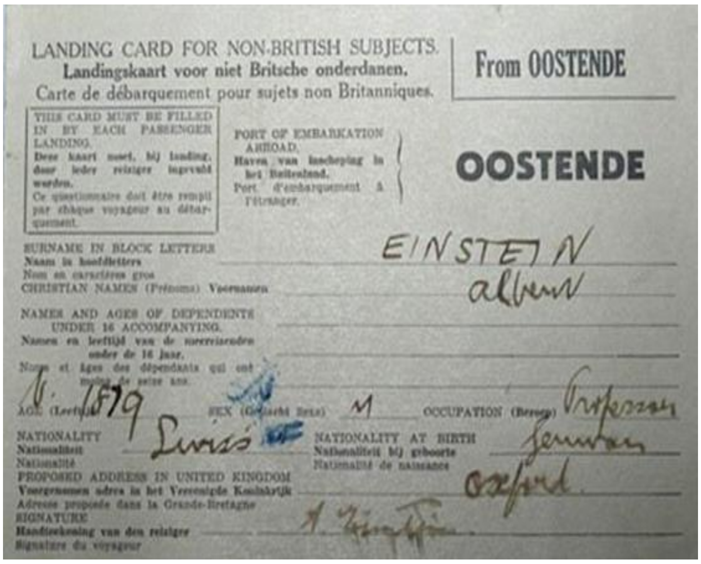
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CHRISTIAN NAMES (Prénoms) Voornamen: albert
NAMES AND AGES OF DEPENDENTS UNDER 16 ACCOMPANYING. Namen en leeftijd van de vergezellende onder de 16 jaar. Noms et âges des dépendants qui ont moins de seize ans.
AGE (Leeftijd): 1879
SEX (Geslacht): M
OCCUPATION (Beroep): Professor
NATIONALITY / Nationaliteit / Nationalité: Swiss
NATIONALITY AT BIRTH / Nationaliteit bij geboorte / Nationalité de naissance: German
PROPOSED ADDRESS IN UNITED KINGDOM / Voorgenomen adres in het Vereenigde Koninkrijk / Adresse proposée dans la Grande-Bretagne: Oxford
SIGNATURE / Handteekening van den reiziger / Signature du voyageur

A. Einstein was in fact a migrant. Born in Germany, he lived in Monaco and later in Italy with his family that left Germany due to economic difficulties. He was educated and worked in Switzerland, obtaining the Swiss citizenship. After a short stay in the UK, Einstein became an US citizen.

Pictures sources: History Industrial Revolution (L), Mercury Press Agency Ltd. (R)

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**Roxana Nedelescu**

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**Abstract**

The purpose of this paper is to address the issue of social security benefits that jobseekers, nationals of other Member State, residing in another Member States are in title to, as well as the economic implications of free movement of persons and labour market access. Consequently, it aims to disentangle between labour mobility welfare effects and "benefit tourism" looking in particular at the United Kingdom social security system and analysing the policy framework currently in place that governs the free movement of people across the European Union Member States.

**Keywords**: Free Movement of Persons, Labour Mobility Welfare Effects, Social Security, Benefit Tourism

**JEL Codes: H31, H55, H77, I31, J01, J15, J78, K37**

## I. Introduction

The European Union is one of the main destinations for people seeking a better livelihood. Contrary to recent mass-media debates and despite increasing global migration flows, intra-EU migration is low. Annual cross border mobility within the EU accounts in fact only for 0.35% of total EU population (OECD Economic Survey of the European Union, 2012). As a reference point, annual mobility across states in the United States is 2.4% of the total population. Less than 3% EU citizens reside in a different EU country, which is one tenth than the United States (Barslund, Busse and Schwarzwalder, 2015). Not only is labour mobility in the European Union low, but it may be decreasing in the future if one accounts for the expected future income convergence between Eastern and Western EU countries.

Nevertheless, immigration from Eastern Europe has attracted much attention from media and governments, with the accession to the EU of ten countries in 2004 followed by two more, Romania and Bulgaria (EU2) in 2007 and removal of labour market restrictions in 2014. The EU-15 are presumed to be the countries most preferred by the migrant citizens of the more recent Member States. Several concerns were raised about the economic effects of foreign workers on host country economies, such as whether immigrants have a negative effect on the welfare of native population, depressing wages and increasing unemployment. Certainly, the economic effects of immigration depend on the host country economy and labour market capacity of absorption, substitutability as well as complementarity of native and foreign workers, but moreover on the skills of migrating population as well as the size of immigration flows.

Recent debates especially in the United Kingdom have focused on “benefit tourism” i.e. foreign citizens using their right to move freely in the EU with the intention of exploiting more generous social security systems. In November 2014, the British Prime Minister gave a speech advocating for EU treaty reforms that would restrict EU workers access to in-work as well as child benefits and impose tighter restrictions on new Member States and EU jobseekers and would ban those abusing free movement right.

This paper addresses several questions: What are the main driving factors of migration? What are the economic implications and the welfare effects of influx of foreign workers? What are the EU rules on free movement of persons and social security rights of mobile citizens? Furthermore, it assesses from an economic perspective the recent judgment of the Court of Justice of the European Union (ECJ) in the case Dano v Jobcenter Leipzig. In this case the Social Court of Leipzig asked the Court of Justice to interpret EU law that regulates the free movement of persons and social security coordination. The Court ruled that the host Member State (i.e. Germany), may deny “social security benefits for jobseekers who are in need of assistance" coming from a different Member State (i.e. Romania) in the absence of a genuine link with the host Member State if the concerned citizen immigrated only to seek employment or benefit from social assistance. Furthermore, this paper takes into consideration the Court reasoning and applies it to the "benefit tourism" debate concerning Romanian and Bulgarian workers in the United Kingdom. It analyses the British social security system, employment rate as well as social assistance requests from Romanian and Bulgarian nationals.

The main findings of the paper highlight that labour mobility affects welfare, both receiving and sending countries being better off in terms of employment and wage levels. Certainly high-skilled migrants are more beneficial for the host country economy than lower-skilled or inactive mobile citizens. Nevertheless, empirical studies show that low-skilled mobile workers positively influence the host country labour market by inducing the native labour force to further specialize. Concerning the UK, the main reason of EU2 citizens to emigrate is work related and only a small percentage actually request social assistance. Therefore the benefit tourism debate is grossly exaggerated.

However immigration policy is a complex issue. Leaving aside cultural differences, from an economic point of view, it may be the case that on the short-run tax contributions offset out payments of social benefits, but further analysis is needed in order to understand the long-run implications and if these effects cancel each other out. Nevertheless, restrictive immigration policy may also have a negative effect on the home country welfare, reducing the number of high skilled workers from abroad. This is because mobile workers may choose to migrate to countries with lower labour market restrictions. Given that much of the UK debate concerns inactive persons or low-skilled labour force, the UK risks to induce in fact a crowding-out effect: because of the negative image of immigration only low-skill immigrants without any other opportunities may decide to go to the UK, crowding out high-skilled labour force.

The paper is structured as follows: Section II analyses the welfare effects of free movement of persons, while Section III discusses the economics of labour movement. Section IV presents the EU rules on the free movement of persons and Section V the EU rules on social security rights. Section VI presents the Dano case and Section VII examines the situation of social benefits in the United Kingdom. Finally, Section VIII provides the conclusions of the analysis.

## II. Welfare Effects of Free Movement of Persons

Public perception concerning immigration is exaggerated. Certainly, cultural differences may play a major role, as aversion or fear of foreigners may create expectations. But focusing on economic aspects, further analysis needs to be conducted in order to disentangle the various welfare effects of free movement of persons, distinguishing between economically active and inactive persons and investigating the trade-offs between the two. There are different drivers as well as impacts of intra-EU mobility. Several factors may determine the decision to migrate.

Let $M = f(W_{H,F}, E, L, D, S)$ be the function that defines the decision to migrate:

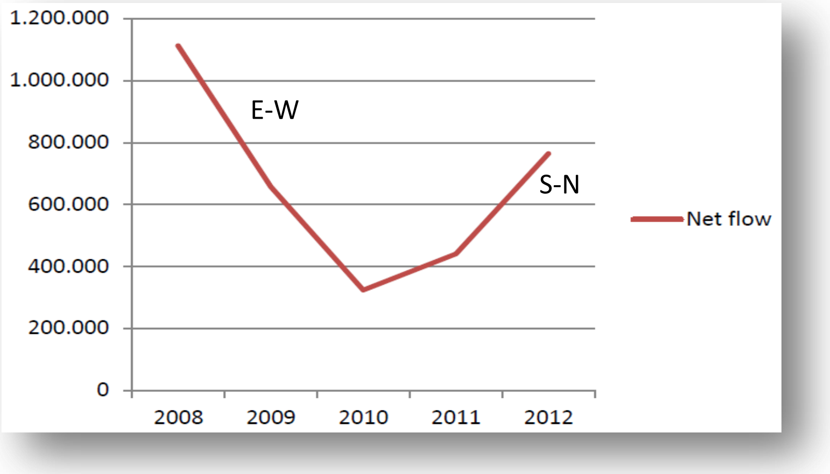
*Microeconomic and Macroeconomic factors:*
Let: H-host country, F-foreign country
$W_{H,F}$ = difference in wages between country H and F
E = economic conditions (e.g. welfare system in the country of destination, business cycle)
L= individual labour market status, i.e. economically active/inactive
*Other factors:*
D= demographic factors (e.g. number of family members, education, age)
S= socio-cultural factors (e.g. language, proximity, religion, culture)

The economic literature on intra-EU mobility finds as the most significant factors to migrate wage differentials, economic conditions and overall gains from migrating. Essentially, individuals compare socio-economic benefits with costs of relocating, which may be denoted by $C=f(P, T, O, I)$, where:
P= psychological cost from leaving the country
T= transition cost, transport and housing
O=opportunity cost from future wage and career development in the home country
I= immigration policy, i.e. time and procedures needed to apply for residence, time needed to apply for citizenship or right to vote, etc.; the more restrictive the immigration policy, the higher the cost of migrating and therefore the lower the incentive to migrate.

Migration is higher when expectations of higher labour returns, income and employment perspectives are higher. Ultimately, if benefits from migrating are larger than the costs, migration will occur.

Cyclical changes of economic growth also impacts migration trends. The economic and financial crisis has had a strong impact on patterns of intra-EU migration flow. The migration patterns initially from East to West, have shifted from South to North (EC, 2013) as shown in Figure 1. In terms of volume, migration from East to West remains higher, however significant migration flows were registered from Southern countries deeply affected by the crisis such as Italy, Spain and Greece, to countries such as Germany and the United Kingdom.

Figure 1. Migration Flow




Source: EPC Issue Paper, 2013

Immigration policy is a difficult topic, as labour mobility affects economic welfare in the host country. Since country H welfare depends on the labour market status (i.e. economically active/inactive) and quality (i.e. high-skilled/low-skilled) of migrants as well as of native workers, different labour market status of foreign workers as well as skills, may impact differently on the host country economy.

Formally:

Let $W_H=f(L^{h,l}_{H,F}, I^{h,l}_{H,F})$, where:

$L^{h,l}_{H}$, number of native labour force that may be high-skilled, h, or low-skilled, l

$L^{h,l}_{F}$, number of foreign labour force in the host country that may be high-skilled, h, or low-skilled, l

$I^{h,l}_{H}$, number of inactive native labour force in the host country that may be high-skilled, h, or low-skilled, l

$I^{h,l}_{F}$, number of inactive foreign labour force that may be high-skilled, h, or low-skilled, l

$=> L^{h,l}_{F}+I^{h,l}_{F}= N_F$, the total number of foreign immigrants in the host country

Assuming:

$\partial W_H / \partial I^{h,l}_{H,F}<0$, inactive citizens lower the host country welfare as most likely they will rely on the social security system of the host country;

$\partial W_H / \partial L^{h}_{H,F} > \partial W_H / \partial L^{l}_{H,F} > 0$, therefore active citizens increases the welfare in the host country. The more skilled the labour force, the higher the welfare effects.

High skilled migrant workers have high labour productivity and may be beneficial to the host country economy and native labour force by impeding firms to delocalize in search for human capital, while some low skilled migrant workers may occupy positions otherwise not supplied by the native labour force. Furthermore, recent empirical evidence (Foged and Peri, 2015) shows that low skilled migrant workers may also positively impact host-country labour market by incentivising native low skilled workers to specialize and therefore obtain a higher wage rate.

Once in the host country, the migrant will have to choose between labour market participation (active) versus leisure (inactive) and in the former case, on the amount of labour supplied in the receiver country. Taking in consideration the wage level in the receiving country labour market and the amount of non-labour income such as social security or other welfare payments, foreign citizens will maximize their utility subject to an income budget constraint.

Let high/low-skilled mobile citizens utility function be given by:

$U^{h,l}_F = f(G^{h,l}_F, V^{h,l}_F)$, f'>0, f''<0, where:

$G^{h,l}_F$=consumption of goods and services that may be acquired through income

$V^{h,l}_F$=leisure, which may be defined as activities conducted while not working

If active, high/low-skilled workers income function $Y^{h,l}_F = w^{h,l}_F * x^{h,l}_F + A^{h,l}_F$, where:

$Y^{h,l}_F$=individual income

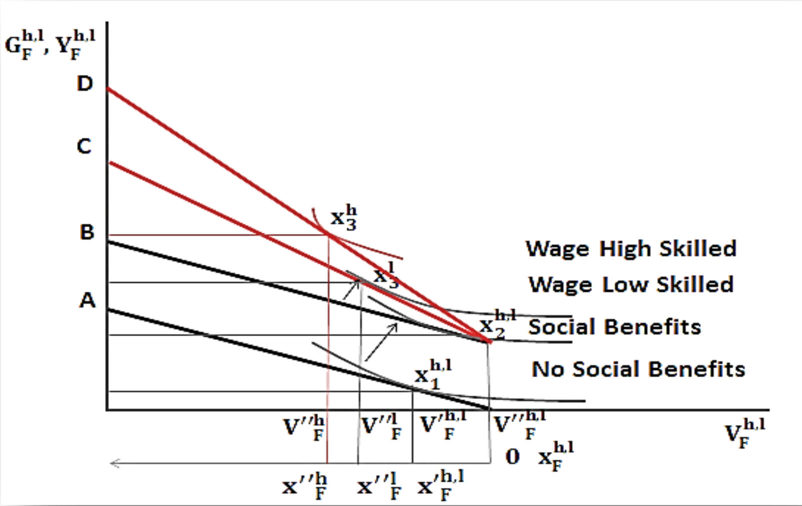
$w^{h,l}_F$=individual wage rate

$x^{h,l}_F$=individual labour supply

$A^{h,l}_F$=non-labour income such social assistance benefits

Individuals are highly heterogeneous in terms of consumption versus leisure preferences which will induce different labour market outcomes. If inactive, 0 hours of working hours are supplied and individual income is $A^{h,l}_F$ if social assistance is received. With strong preference for leisure, individuals receiving social benefits will not participate in the labour market.

Figure 2. Labour Market Participation



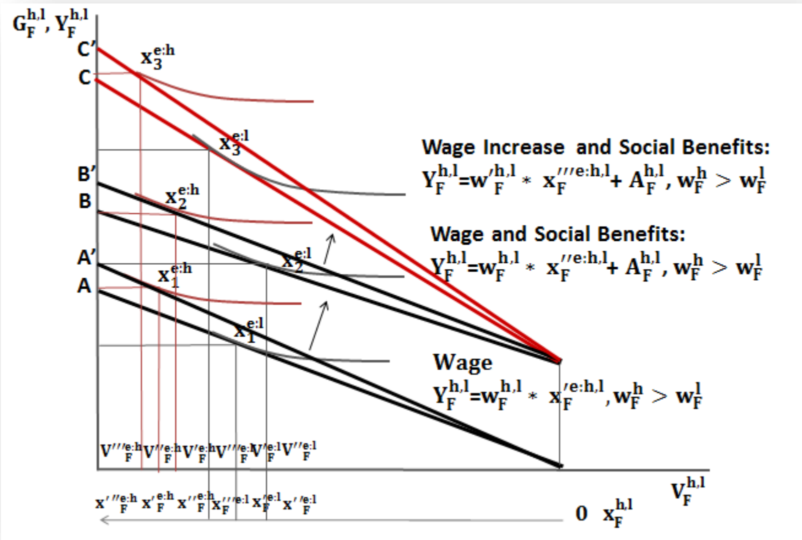

Based on Figure 2, if an individual receives no social assistance and has non-labour income, such as for example support from other members of family, with budget constraint line A, he or she will enter the labour market at point $x_1^{h,l}$ and will decide to supply $x_F'^{h,l}$>0 amount of labour. If non-labour income is received such as social benefits and assuming leisure is a normal good, this will shift the budget line to the right which allows the individual to have more utility in point $x_2^{h,l}$. In this case, given that our mobile worker prefers leisure over consumption, indeed he or she will choose to supply 0 amounts of working hours, as the utility is higher in the second case.

Therefore, the higher the non-labour income in the host country, the more likely the corner solution would be preferred in the case of a mobile worker that favours leisure and indeed, this evidence would support the "benefit tourism" hypothesis, i.e. mobile citizens free-riding on social security systems of the host country. In this case, a possible solution would be to condition the receipt of social assistance based on the period of prior participation in the labour market and social services that control and invite inactive workers to periodic job interviews or job placements.

Since inactive citizens are heterogeneous, for those "trapped" in an unemployment spell, an alternative policy would be to incentivize them to increase their human capital by participating in vocational trainings and therefore be able to obtain an income in their field of activity or in a field that they re-specialize in. This is exemplified by budget line C. Individual utility is higher when he or she gains a wage which is higher with respect to the reservation income when receiving social assistance. As such, the optimal decision is to participate in the labour market at points $x_3^{h,l}$ and supply $x_F^{\prime\prime h} > x_F^{\prime\prime l} > 0$ amount of labour. Overall: $x_F^{\prime\prime h} > x_F^{\prime\prime l} > x_F^{\prime h,l} > 0$. As such, as human capital increases, labour market participation increases especially with higher wages. This may explain why inactive citizens classified as "benefit tourists" are lower skilled.

With non-labour income, in Figure 3, let us assume that the individual budget line is A for low-skilled and A' for high-skilled. As such, the worker will choose to supply the optimal amount of labour, $x_F^{\prime e:h} > x_F^{\prime e:l} > 0$ that maximizes utility. If non-labour income is introduced, the utility will increase but the labour supply will decrease $x_F^{\prime\prime e:h} > x_F^{\prime\prime e:l} > 0$. However if the wage rate increases, the optimal amount of labour will increase at points $x_F^{\prime\prime\prime e:h} > x_F^{\prime\prime\prime e:l} > 0$ since the wage rate of the high skilled is higher than that of the lower skilled.

Figure 3. Optimal Labour Supply




In Figure 3, the higher the skill, the higher the wage and the higher the willingness to increase the amount of labour supplied. Overall:

$$x_F^{\prime\prime\prime e:h} > x_F^{\prime e:h} > x_F^{\prime\prime e:h} > x_F^{\prime\prime\prime e:l} > x_F^{\prime e:l} > x_F^{\prime\prime e:l} > 0$$

However, not always the effect of increasing the wage rate is that obvious. With non-labour income, the worker may consume more leisure and provide less labour supply, i.e. income effect. But as wages increase, the opportunity cost of leisure increases and as such, more time would be devoted to labour, i.e. substitution effect. Therefore the net effect is uncertain, depending on which of the two prevails.

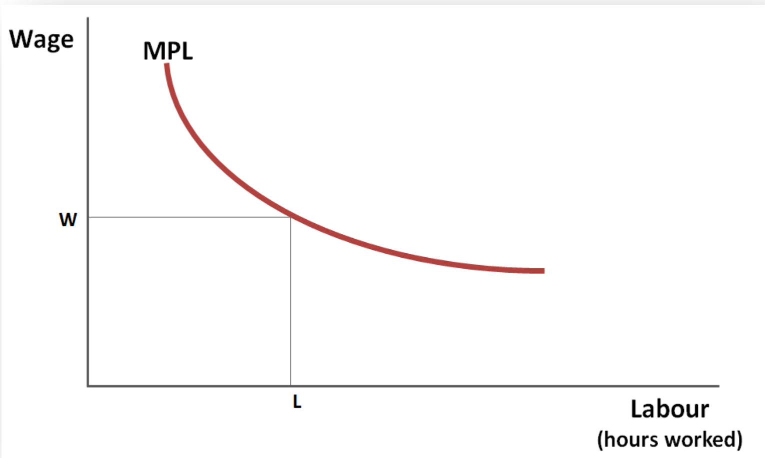
Given that social welfare increases more with high skilled migrants, a discriminatory immigration policy that can perfectly distinguish between inactive/active and high skilled/low skilled would be most beneficial as the host country government would only incentivize high-skilled active workers to enter their economy. However, the government cannot observe the number of hours worked in order to identify the migrants which maximize welfare and regulate its labour market accordingly.

But governments may incentivize either category through taxation. Since the government can observe the gross income before taxation $Y_F^{h,l}=w_F^{h,l}*x_F^{h,l}$, if income is higher than consumption the government may impose a tax, otherwise, a subsidy. However, if the proportion of individuals receiving net subsidies increases tremendously due to increased low-skilled migration flows, the fiscal cost of redistribution could increases. Nevertheless, through taxation and redistribution, the government can maximize social welfare.

**III. Impact of Free Movement of Workers on Labour Markets**

Having discussed the drivers of migration as well as welfare effects of active/ inactive and high/low-skilled migrant labour force, it is important to consider further the impact of migration flows on the labour market. Figure 4 describes the labour market functioning mechanism. In terms of demand for labour, marginal revenue productivity theory states that firms will hire an additional worker as long as the cost of that worker, i.e. his wage, is less than or equal to the value of that worker's extra output, assuming that labour is homogeneous.

Figure 4. Labour Productivity



Formally, let Q = f(K, L) be the production function, where:

Q = output ; K = capital ; L = labour; P=price; W=wage

With fixed capital, in the short run firms can only increase output by increasing labour. In discrete terms, the marginal product of labor can be denoted as: MPL = ΔQ/ΔL

Total revenue (TR) is given by: TR= PxQ

Marginal Revenue (MR) is given by MR=ΔTR/ΔQ

Marginal revenue product: MRPL = MPLxMR=(ΔQ/ΔL)x(ΔTR/ΔQ) = ΔTR/ΔL

In order to maximize profits:

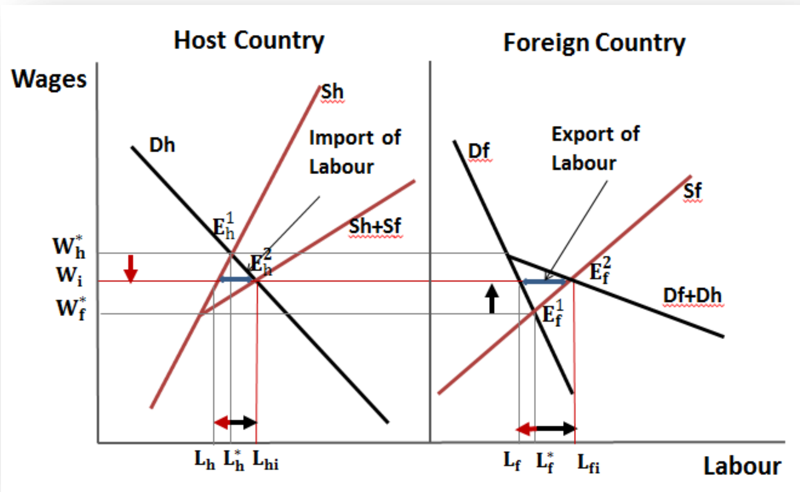
MC= MR <=> W=MRPL , where MC=marginal cost

Since MR=P => W=MPLxP or W/P = MPL

As a rule, the firm should keep on hiring one more worker until the marginal cost of hiring this additional worker equals the marginal benefit.

With integration, labour supply is directly affected through changes in the size of labour force due to migration, while labour demand is indirectly affected through changes in products markets. Assuming homogeneity of labour productivity and that immigrant and natives are perfect substitutes, with mobile labour force, wages across countries may be equalised as shown in Figure 5.

Figure 5. Static Labour Market Integration: Direct Effect on Wages

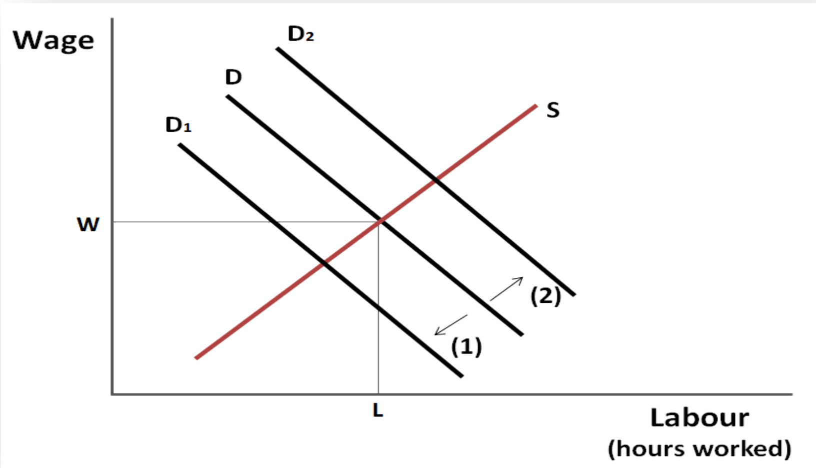



From a static perspective, in the host country (h), the equilibrium wage and labour supplied, $E_h^1(W_h^*, L_h^*)$, is given by the intersection of domestic supply, $S_h$, and demand, $D_h$. The same reasoning applies in the foreign country (f), resulting in the equilibrium wage and labour supply, $E_f^1(W_f^*, L_f^*)$.

Looking at the direct effect of labour mobility, if workers from the foreign country decide to enter the labour market of the host country, the labour supply increases in the host country. Assuming demand for labour is unchanged in the host country, the new equilibrium point is given by $E_h^2(W_i^*, L_{hi}^*)$. As such, the outward shift of the labour supply curve lowers the equilibrium wage $W_h^*$, to $D_h$ , reducing the employment for residents from $L_h^*$ to $L_h$ as they may not be willing to supply labour for a reduced wage, but total employment increases from $L_h^*$ to $L_{hi}$ in the host country.
In the home country, the demand for labour supply increases as a result of workers leaving to go to the host country. Now the equilibrium is given by $E_f^2(W_i, L_{fi})$. In the home country, as a result of the export of labour, the domestic labour supply decreases from $L_f^*$ to $L_f$ but the total labour supply as well as wage increases from $L_f^*$ to $L_{fi}$ , and respectively from $W_f^*$ to $W_i$.

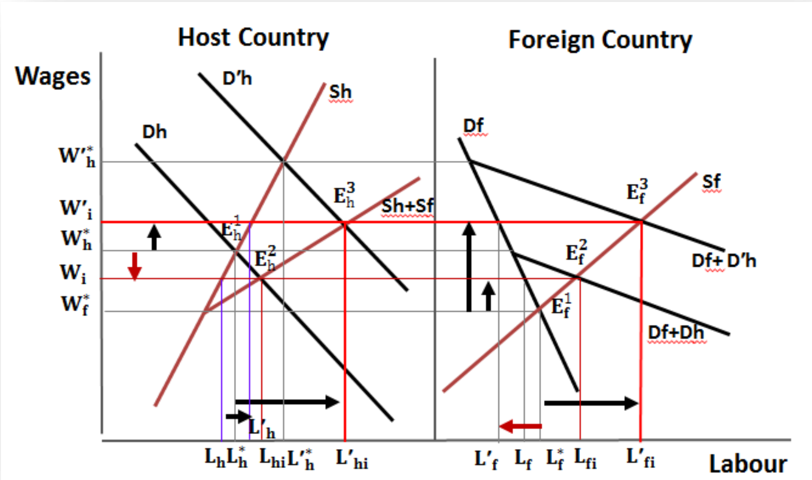
There are also indirect effects through product markets. Figure 6 illustrates that contraction of domestic industry, due to imports, reduces domestic output and, consequently, demand for labour (1), while expansion of domestic industry, dues to exports increases output and as such, the demand for labour (2).

Figure 6. Labour Market Integration: Indirect Effect on Wages




Therefore, from a dynamic perspective, immigrant flows stimulate market change due to the output increase. The increase in labour supply induces a decrease in labour costs, i.e. wages. In the subsequent periods, the low labour cost can generate an increase of demand for products since more customers will be present in the market and following that, of labour. As shown in Figure 7, the decrease in the wage rate on the original demand curve $D_h$, on the longer-term, will induce an upward shift of labour demand, from $D_h$ to $D'_h$ in the host country and from $D_f + D_h$ to $D_f + D'_h$ in the foreign country. With respect to both the equilibrium point without immigration and equilibrium point with integration, the total quantity of labour increases in both countries to $L'_{hi}$, $L'_{fi}$ and the wage rate rises to $W'_{i.}$

Figure 7. Dynamic Labour Market Integration: Direct Effect on Wages




Therefore from Figure 7 one may conclude that with increased labour force, both countries are better off in terms of higher employment and wages, provided that sufficient labour flows occur in the host country that induces market change, i.e. an output increase and consecutively an increased demand for labour.

## IV. EU Rules on Free Movement of Persons

So far, from a purely economic point of view, we have determined that labour movement is in fact beneficial for both the host and the foreign economies. Now we turn our attention to the legal framework and European legislation that governs the free movement of persons, in order to understand under which conditions EU citizens are entitled to move freely across borders.

Free movement of persons and the right to reside in a different Member State, other than one's own, is stipulated by the Art. 21(1) of the Maastricht Treaty (1992, formally the Treaty on European Union). These rights are not unconditional. Currently, Directive 2004/38/EC regulates the free movement of persons across the European Union. It defines the rights and obligations of European citizens, differentiating across residence rights, by duration of stay: for stays of less than three months, citizens have the right to reside in a different Member State only if they have a valid identity document or passport; for stays of more than three months, the right of residence is granted under certain conditions, i.e. sufficient economic resources as well as sickness insurance need to be guaranteed such that the EU citizen and his family do not represent a burden for the host country social services and they may need to register with the local authorities; for stays of more than 5 years, the right of permanent residence may be acquired, with equal rights to host Member State nationals. The right to enter and reside may be restricted only due to public policy, public security or public health grounds, but not due to economic arguments.

In practice, EU law provisions concerning free movement of EU citizens have been implemented gradually. To start with, the Schengen Agreement (1985) and the Schengen Implementing Convention (1990) abolished internal borders and harmonized external border control procedures, among other achievements. However, not all[1] EU Member States adhere to the convention as yet. The 2004/38 Directive has already been transposed into national law and implemented by all Member States. However, limitations concerning the free movement of persons have been maintained by several Member States concerning citizens of new Member States for a period of seven years following the date of accession. Therefore, restrictions on free movement of workers applied up to 1 January 2014 de facto in most[2] EU Member States.

From an economic point of view, labour market entry barriers were in place since employers would need to request work permits from the national authorities in order to hire a Romanian and Bulgarian citizens (EU2). With the lifting of entry barriers, the benefit tourism "hysteria" started. In the United Kingdom, politicians and certain sections of the media feared invasion: rules to access benefits were tightened in order to ensure that migrants could not claim out-of-work benefits for three months after their arrival and one would qualify for support only after six months of residence, assuming there existed a genuine chance of employment. Statistics confirmed part of the story: in 2014 the number of Romanian and Bulgarian (EU2) immigrants in the UK increased with respect to the previous year, but the main reason for immigration was work-related: between April 2013 and June 2014, 167 282 EU2 citizens were employed in the UK. This number was significantly higher that the corresponding number of 126 082, for the previous period in 2013 (ONS). Still, the debate did not concern the increase in tax paying immigrants, but the increase of benefit tourists. Given that the latter are the main concern we wish to address, one may enquire what are the benefits that new immigrants can access under EU law.

[1] Schengen members: EU Member States except Ireland, United Kingdom, Denmark, Bulgaria, Romania, Cyprus and Croatia plus Norway, Iceland, Switzerland and Lichtenstein.

[2] Except Italy. In 2009, Greece, Spain, Hungary, Portugal and Denmark also lifted labour market restrictions for Romanians and Bulgarians. In 2011, Spain re-introduced labour market restrictions due to the economic and financial crisis.

## V. EU Rules on Social Security Rights

Article 2 of the Treaty of Rome (1957) sets out as an objective the establishment of a common market in order to support economic development and high employment rates, raising social protection as well as the standard of living in the Member States. Art. 3(1)(c) EEC clearly indicates that the Community aimed at “the abolition, as between Member States, of obstacles to freedom of movement for[…]persons”. It initially targeted economically active individuals and focused on creating a European labour market. But in order to support the development of the European labour market and incentivise intra-EU labour mobility, EU law ensures that national security systems do not act as a barrier and a disincentive for workers to move across Member States.

As such, Regulation (EC) No. 883/2004[3] of the European Parliament and of the Council (2004)-Art. 4, Art. 70, defines the coordination of social security systems between Member States concerning the application of social security schemes to employed, self-employed individuals as well as to members of their families, moving across EU Member States. To put it simply, in order to ensure access to benefits for workers when moving within Europe, the country where the work place is located has to provide insurance, or in the case of inactive individuals, the insurance is provided by the country of residence.

Cash benefits may be transferred from one country to the other, and periods of insurance obtained in another EU country may be considered when applying for benefits. In fact, Art 7 of Regulation (EC) No 883/2004 states that “cash benefits payable under the legislation of one or more Member States or under this Regulation shall not be subject to any reduction, amendment, suspension, withdrawal or confiscation on account of the fact that the beneficiary or the members of his family reside in a Member State other than that in which the institution responsible for providing benefits is situated”. Country-specific conditions apply solely to country specific non-contributory cash benefits granted to individuals in certain need, but not based on contributions or means tested.

Therefore, one could truly free-ride on national social systems by benefitting from non-contributory benefits. However, as we will see below, EU law allows Member States to restrict access to non-contributory benefits.

[3] Amended by Regulation (EC) No 988/2009 of the European Parliament and of the Council of 16 September 2009 (OJ 2009 L 284, p. 43), and Directive 2004/38/EC of the European Parliament and of the Council of 29 April 2004, amending Regulation (EEC) No 1612/68 and repealing Directives 64/221/EEC, 68/360/EEC, 72/194/EEC, 73/148/EEC, 75/34/EEC, 75/35/EEC, 90/364/EEC, 90/365/EEC and 93/96/EEC (OJ 2004 L 158, p. 77, and corrigenda OJ 2004 L 229, p. 35, OJ 2005 L 30, p. 27 and OJ 2005 L 197, p. 34).

## VI. The Dano Case

The single market has been created by removing barriers to the movement of economically active citizens. Economic literature has generally found evidence that active workers are beneficial for both sending and receiving countries. Indeed we saw in previous sections that social welfare increases together with the increase in human capital and labour skills. But one cannot discriminate across labour market status and allow only active citizens to move freely across borders.

We turn now to assess the implications of free movement of economically inactive citizens, especially since social benefit access by non-nationals has generated ardent debates at both national and EU level despite the fact that little evidence has been found to support the claim that EU citizens migrate to exploit benefits. Instead, the evidence points to the direction of moving for work or family reasons. Regardless, social security/financial support are the prerogative of individual Member States. Social security rights[4] do not depend on residence, but they may depend on the source of financing for the payment of these benefits (i.e. contributions made by employees and employers vs. non-contributory benefits) or on the minimum employment period[5] (i.e. sickness cash benefits, maternity and paternity benefits, old-age benefits and unemployment benefits).

In specific cases, such as in the case of Dano v Jobcenter Leipzig recently judged by the European Court of Justice, residence may be taken into account in order to assess the economic and social status of the person concerned. Furthermore, benefits that meet specific conditions as for example special non-contributory cash benefits that Ms. Dano requested, are not subject to Art. 7 of Regulation No. 883/2004. These benefits guarantee a minimum subsistence income and take into account the economic and social situation of the Member State concerned and in this case, are to be provided exclusively in the state of residence.

Ms. Dano resided in Germany since July 2011 and received child benefit from the German authorities as well as maintenance payments. She applied for "basic provision" aid (i.e. subsistence benefit, social allowance for her son, and support for accommodation and heating costs). Her application was denied. After she appealed in 2012, it was again refused by the Social Court, Leipzig. Evidence showed that Ms. Dano did not seek to integrate into the labour market, but only to benefit from the German social assistance scheme. Therefore, in order to avoid excessive social benefits

[4] Benefits referred to are: sickness benefits; maternity and equivalent paternity benefits; invalidity benefits; old-age benefits; survivors' benefits; benefits in respect of accidents at work and occupational diseases; death grants; unemployment benefits; pre-retirement benefits; family benefits.
[5] Requirements vary across Member States.

requests that would burden national assistance systems, unequal treatment concerning granting social assistance benefits between national of the host Member State and other EU citizens is permitted.

However, in order to promote more integration and cross-border movement of persons, social exclusion is a crucial issue that needs still to be addressed. Art. 18 of The Treaty on the Functioning of the European Union (TFEU) prohibit any discrimination on the basis of nationality, while the Charter of Fundamental Rights of the European Union (2000) Art. 1, 20, 51, state that human dignity must be respected and ban any type of discrimination. Given that EU nationals may reside for a period of more than three months in another Member State only if they have sufficient economic resources such that the EU citizen and his family does not represent a burden for the host country social services and in the absence of proven educational training and professional experience or effort to look for employment, ECJ ruled that EU law did not prevent the host Member State from denying non-contributory benefits to nationals of other Member States. As such, EU law protects the social security systems of individual Member States from being abused by non-nationals that do not seek to integrate in the labour market.

## VII. The Impact of Immigration: The Case of the United Kingdom

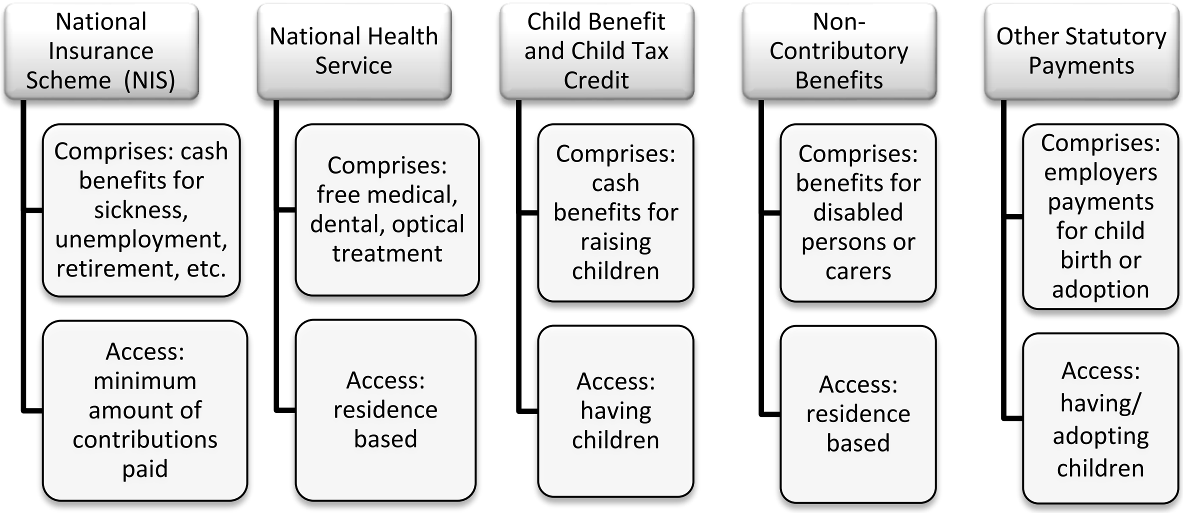
As of 1st January 2014 labour market restrictions have been lifted for Romanian and Bulgarian citizens in countries where they were still enforced, among which, the United Kingdom. Policy makers should have rightfully been concerned about cheaper labour entering the British market from the EU2 countries, given the possibility that influx of foreigners would depress wages for native workers. British politicians and media grew instead very concerned with so-called benefit tourists, i.e. EU2 citizens moving to the UK with the sole purpose of taking advantage of social assistance. In this context, several questions arise: does the British social security system allows for easy access to such benefits and if so, is this the main reason of EU2 citizens to migrate to the UK? Furthermore, given the increased migration to the UK, what is the balance between EU2 tax payers and EU2 citizens requesting social assistance? In the following sub-sections we will answer these questions.

### The United Kingdom Social Security System: What the UK Is Allowed to Do[6]

The British social security scheme comprises several services, as listed in Table 1 below. Social security financing is based on contributions[7] made to the National Insurance Scheme, as well as general tax revenue.

[6] Insurance is done automatically once 16 years old.
[7] See Annex Table 1

Table 1. The UK Social Security Scheme




The UK system is a mix between Social Security paid on the basis of individual contributions and Social Assistance which is funded from general taxation. The main concerns when talking about benefit tourism relate in fact to the non-contributory cash benefits. Table 2[8] provides an extensive list of cash benefits and requirements to be met in order to be entitled to receive them.

Table 2. UK Benefits Criteria

| *Cash Benefits* | *Requirements* |
|---|---|
| Sickness - Statutory Sick Pay | Employment contract;<br>Being sick for 4 days consecutively;<br>Have average weekly earnings at least as equal to the lower earnings limit (LEL). |
| Employment and Support Allowance | Class 1 or 2[9] contributions which sums up to min. 26 times LEL paid in one of the last 2 tax years;<br>Class 1 or 2 contributions of at least 50 times LEL paid or credited in each of the 2 past tax years. |
| Statutory Maternity Pay | Minimum 26 consecutive weeks of work for the same employer;<br>Average weekly earnings at least as equal to LEL. |
| Maternity Allowance | Not benefitting from Statutory Maternity Pay;<br>Being employed for at least 26 weeks out of 66 test weeks;<br>Average earnings at least as the maternity allowance threshold |
| Ordinary Statutory Paternity Pay | Worked for 26 weeks for the same employer;<br>Average earnings in the last 8 weeks of at least the LEL |
| Additional Statutory Paternity Pay | Partner returned to work before the end of maternity/ adoption pay period.<br>Worked for 26 weeks for the same employer;<br>Average earnings in the last 8 weeks of at least the LEL |
| Invalidity Benefits: Employment and Support Allowance | Illness or disability sufferings certified by a medical assessment |

[8] See Annex Table 2
[9] See Annex Table 1

| | |
|---|---|
| Old Age Pension and Benefits | Reach State Pensionable age<br>Meet the minimum insurance contributions, for at least 30 tax years |
| Survivor Benefits<br>Bereavement Payment/ Allowance*<br>Widowed Parent Allowance**<br>Additional Pensions* | Partner/Parent death<br>*based on contributions<br>**for individuals that are entitled to child benefit |
| Work accidents Benefits<br>Disablement benefit | Disability due to a work accident or due to industrial disease<br>Being disabled/ill for more than 15 weeks after the date of the accident |
| Unemployment Benefit<br>Jobseeker's Allowance (182 days) | Paid Class 1 contribution on earnings of at least 25 times LEL at least in one of the 2 relevant tax years;<br>Paid Class 1 contribution on earnings of at least 50 times LEL at least in both of the 2 relevant tax years. |
| Income Support | Part-time workers with income& capital are below a certain threshold |
| Income Based Job Seeker Allowance | Unemployed persons with income& capital are below a certain threshold, not entitled to any other benefit |
| Council Tax Benefits | Paid Council Tax and income& capital are below a given threshold |
| Long Term Care<br>Partial Assistance<br>Co-financing | Illness/disability on the long-term |
| Family Benefits<br>Child Benefit<br>Child Tax Credit | Being responsible for one or more children under 16 or up to 20 if in full-time education;<br>Reside in the UK; |
| State Pension Credit | Be at least 65 years old |
| Housing Benefit | In case rent is paid and income and capital are below a given threshold |

One may easily conclude that most benefits are accessed on condition of previous contributions. Therefore benefit tourism concerns: State pension credit, Income-based allowance for job seekers, Income support, Disability living allowance, Family/Child benefit and Housing benefit which are residence based.

However, in order to access these benefits, one has to pass the Habitual Residence Test (HRT), and meet the residence requirements. Starting on 1 January 2014, the HRT consists of a decision based on the proof of right to reside based on nationality, immigration status, family circumstances and their right to reside under UK, EU laws and bilateral treaties and proof of habitual residency, i.e. period of residence in the UK, reason to migrate; how long one plans to stay, finding employment and proof of link to the UK. As such, before claiming benefits, the claimant needs to have been living in UK for three months.

From 1 January 2014, several restrictions have already been implemented:

- EEA nationals' job seekers as well as EEA national workers which became unemployed, after 6 months lose their rights to reside and indirectly the jobseeker allowance if evidence of actively seeking employment is not provided.

- Housing benefit is denied to new jobseekers as it does not fall under social security coordination rules.
- In order to acquire the status of "worker" and implicitly access a wider range of out-of work and in-work benefits, new checks are in place:
    - Tier 1 assessment – a new Minimum Earnings Threshold is in place requiring minimum weekly earnings of £153, for three consecutive months;
    - In case Tier 1 threshold is not met, Tier 2 is applied – it consists of a detailed individual assessment, verifying if the individual's activity is genuine and effective.

Therefore one could easily conclude that, given the additional requirements the UK government introduced, as well as the discretion of Member States acknowledged by the ECJ ruling in the Dano case, the checks needed in order to prevent new immigrants from abusing the welfare system are already in place.

**The United Kingdom EU2 Migration Flows: What Is Actually Happening in the UK**

Regardless of checks and balances in place, one could argue that foreigners abuse the system, applying for benefits more often than natives, representing an extra burden. This section examines the relevant statistics. In 2013 the estimated Romanian citizens resident in the UK was 128 000, while resident population of Bulgarian citizens was 49 000; therefore for the EU2 countries, of 177 000 (0.3%). Latest data available for the period April 2013 - June 2014 show that indeed there has been an increase in emigration to UK of EU2 citizens. Between June 2013 and June 2014, 32 000 Romanian and Bulgarian citizens emigrated to the UK, a statistically significant increase from 18 000 in the previous 12 months (IPS). Out of the 32 000, three quarters of EU2 citizens emigrated for work related reasons, i.e., 24 000. By mid-June 2014, approximately 209 000 EU2 citizens officially resided in the UK. In September 2014, 167 000 Romanian and Bulgarian citizens were registered as employed (LFS), which represents a 33% increase with respect to the same period in 2013. These statistics take into account the number of employed people present in the UK labour market at a certain time and do not take into account the immigration date. Regardless, EU2 immigration rate in the UK has increased over time, along with the employment rate. Overall, between July to September 2014, the employment rate of Romanian and Bulgarian citizens residing in the UK was about 79%, higher than non-EU citizens of 61.6%, and of the British citizens, of 73.6% (LFS). Certainly, the main reason to migrate is work related and not benefit-related.

Table 3 presents available data concerning the number of individuals receiving UK social security benefits and tax credits, distinguishing between Romanian and Bulgarian claimants.

Table 3. Number of benefit claimants, by Country (House of Commons, 2014)

| *Working age benefit claimants, February 2014* | |
|---|---|
| Country | Number |
| Total | 5 309 580 (100%) |
| United Kingdom | 4 914 160 (92.6%) |
| EU | 130 990 (2.5%) |
| Of whom | 2 480 (0.05%), Romanians<br>Less than 2 430, Bulgarians |
| Other non-UK | 264 430 (5%) |
| *Child Tax Credit (CTC) and/or Working Tax Credit (WTC), received starting with March 2014* | |
| Total | 4 644 200 (100%) |
| United Kingdom | 3 905 500 (84.1%) |
| EU | 317 800 (6.8%) |
| Other non UK | 421 100 (9.1%) |
| *Child Benefit, December 2013* | |
| EEA countries or Switzerland | 34 268 children |
| Of whom | 392 children (1.14%) Romanian |
| | 245 children (0.7%) Bulgarian |

From the table above, it is obvious that Romanian and Bulgarian nationals have a very high rate of employment in the UK and a very low rate of social assistance claims. Weighing labour mobility costs and benefits, one may conclude that more tax revenue is received from EU2 residents in the UK, than benefits paid to them. The net fiscal impact of EU2 immigrants is positive for the UK. Overall, EU immigrants residing in the UK have made a net fiscal contribution of GBP 25 billion since 2001. For every 1 pound they receive in benefits, they pay 1.34 pounds. Moreover, EU citizens are 45% less likely than UK natives to receive benefits.

Certainly more data is needed to disentangle further across benefit requests per type and nationality. Nevertheless, one can clearly see that the overall effects of labour force migration is beneficial to the UK economy overall and EU2 migrants have a very high employment rate, not abusing the national social system. Furthermore, if the latter were true, going back to the Dano case, as the ECJ ruled, social assistance may be denied if specific conditions are not met and the claimant represents a burden for the host country social security system.

Therefore Mr. Cameron's proposed reforms concerning EU migrants access to welfare such as restricting EU migrants' access to in-work benefits, restrictions on jobseekers' rights to stay in UK after six months and a ban on child benefit claims for non-resident children, would have to be defensible. Otherwise, the ECJ could conclude that indirect discrimination would be in place for restricting child benefits (Open Europe, 2015), for example. Nevertheless, reforms would not require necessarily treaty changes, but rather EU or domestic legislation changes.

## VIII. Conclusion: Tackling European Migration

As of 1st January 2014, labour market and welfare systems restrictions imposed during the previous seven years on Romanian and Bulgarian citizens were lifted in the nine EU countries where they were still enforced. This liberalisation created uneasy public debates in the richer Member States, fearing massive immigration and free-riding behaviour on the national welfare systems, the so called "benefit tourism".

This paper has shown that while indeed there has been an increase in migration from Romania and Bulgaria towards the United Kingdom, the feared massive invasion has never materialised. Furthermore, the main reason for migration is work related. The employment rates of Romanian and Bulgarian workers are even higher than those of native labour force, while benefits claimed are enormously lower than those of native or non-EU migrants, corresponding to under 0.1% for working age benefits and under 2% for child benefit. These findings support previous research evidence by Dustmann, Frattini, and Halls (2010) showing that "migrants from EU 10 countries made a positive net contribution on average to public finances in the UK, i.e. that they paid more to the public sector in taxes than they received in the form of welfare grants and public spending." Conducting a more in depth analysis, Dustmann and Frattini (2013) find that from 1995 to 2012, EEA immigrants "have made an overall positive fiscal contribution to the UK", while "the net fiscal balance of non-EEA immigrants is negative, as it is for natives".

Furthermore, with EU social system coordination, the benefits under discussion have been shown to concern only non-contributory benefits, based on residence, which fall exclusively within the competence of national authorities. But since the UK has introduced already new rules on claiming benefits and the ECJ ruled that non-contributory benefits may be refused if certain economic and labour market requirements are not met, the "benefit tourism" debate may be closed.

But with one issue closed, another arises. Since the host Member State may not expel other Member State citizens based solely on economic grounds, by refusing the right to access non-contributory social benefits to a certain category of citizens, what the host Member State would in fact do is to create poverty. This is the real issue that has to be tackled in the future. Further coordination is needed covering non-contributory benefits in the form of either bilateral agreements between sending and receiving countries but even more importantly, a common EU approach is needed. A step further in the European integration process would be to progressively construct a true European labour market, with EU-wide social security agreements. Rather than transfer social benefits rights, a central institution is needed to protect the rights of mobile workers as well as regulate and administer the requests for social assistance.

Leaving aside the “benefit tourism” debate, the real discussion should be focused instead on the welfare effects of mobile workers in both the host and home country. In this paper it is shown that even if from a static perspective mobile workers may depress native salaries and employment levels, from a dynamic perspective both countries are better off with migration, wage and employment levels increasing. Furthermore, high-skilled mobile workers increase native welfare by being willing to supply more labour instead of leisure and by doing so, having a higher income and therefore contributing more to the host country budget. These findings corroborate the conclusions of extensive literature that there is little evidence of a negative effect of immigration on the host economy. On the contrary, with ageing labour force and decreasing wage differentials, little immigration has been found to reduce the native population welfare, while more immigration, to increase it.

More research is needed in order to apprehend thoroughly the effects of immigration. In order to comprehensively understand trends in the labour market as well as welfare effects, national and European Union authorities should consider the development of relevant instruments and tools such as better time series data in order to quantify immigration effects that could contribute to the assessment and introduction of efficient policy proposals. Bottom-line, immigration is a sensitive topic: on the one hand, cultural differences may create fear, causing negative attitudes towards migrants that are over exploited by the media, while on the other, governments may use it as a strategic argument for their own benefit.

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## Annex 1

### Table 1. NIS Contributions

| *Category* | *Condition* | | *NIS Contribution Type*[10] |
|---|---|---|---|
| Employee | Earnings Limit<Earnings<Primary threshold | i. | Pay to protect benefit rights |
| | Earnings>Primary threshold | ii. | Primary Class 1 (% deducted from weekly earnings) |
| | Earnings>Secondary threshold | iii. | Secondary Class 1 (paid by employers) |
| Employer | Employees benefits | iv. | Class 1 A, 1 B |
| Self-employed | Earnings>Small Earnings Exception | v. | Class 2 (flat rate) |
| | Earnings>Income Tax Personal Allowance | vi. | Class 4 (not counted for benefits) |
| Voluntary contributions | Individuals not accountable for: i., v., or contributions are not sufficient for benefits eligibility | vii. | Class 3 (count for retirement and bereavement, flat rate) |

[10] The exact rates for the 2013-2014 and 2014-2015 tax year are available here: https://www.gov.uk/national-insurance/national-insurance-contributions-how-much-you-pay