# Social security and free movement in the EU

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**INT-AR Paper 2 – Social security and free movement in the EU**
**European coordination – Legal loopholes – Welfare tourism?**
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## Introduction

Since the establishment of the European Economic Community (EEC), the free movement of citizens of the Member States has been a key theme in the European cooperation. The removal of barriers for the free movement of citizens belonged to the basic principles of the 1957 Rome Treaty. This Treaty forms the basis for the EEC and contains several provisions that guarantee the free movement (Treaty of Rome, 1957, Articles 48-51). The Treaty gives European citizens the right to go to another EEC member state to seek employment and to work in all EEC member states. This INT-AR paper deals with the social security that is applicable in case of free movement of workers. The first sections treat the general principles of the social security in case of cross-border work. The following sections look after loopholes and question marks in the legislation and the link with free service provision. The final section assesses the notion of welfare tourism.

## The coordination of social security

Although the actual arrangement and application of the social security system does not belong to the competence of the European Institutions, the coordination of national social security schemes became one of the first and crucial regulated fields of cooperation between Member States. In order to prevent that EU-citizens who work and reside temporarily in another Member State lose their social security rights the Member States considered it necessary to govern the coordination of their social security systems. These arrangements and the fine-tuning of the different national systems in cross-border situations know a long history. Since 1958, the Council has concluded regulations for the social security coordination of mobile and migrant workers. The coordination was (and is) based on the principle that persons moving within the EU are subject to the social security scheme of only one EU member state. The regulations have to guarantee the equal treatment and to counteract discrimination.
In the course of the years, this legislation has been revised, based on jurisprudence and practical experience. The European Council modified the corresponding Regulation number 3, concluded in 1958, 14 times. The subsequent and completely revised Regulation 1408/71 was likewise modified 39 times. These modifications had to do with adaptations to changes in national legislations and with improvements based on case law stemming from proceedings of the Court of Justice of the European Union. The readjustment of the coordination rules in 2004 took the form of an overall modernisation exercise, leading to Regulation 883/2004 (also called the Basic regulation), with the additional aim to simplify the procedures. At the same time, the legislator wanted to get rid of several exemptions. The necessary implementing Regulation 987/2009 was concluded in spring 2009. The modified rules came into effect from 1 May 2010. The basic principle – only one legislation applies – stayed upright. The last revision dealt with several important question marks. The coordination mechanism had to be made resistant to practices that attempt to circumvent the mandatory contribution of social security payments, for instance by using foreign letterbox companies. Crucial issues were how to get a grip on cross-border recruitment and the free movement of workers that pursue activities in multiple countries, like in the international transport and the inland waterways, but also in the construction or infrastructure sectors. After the conclusion, the procedures and working methods to be followed in case of cross-border work have figured several times on the agenda of the Administrative Committee for the coordination of the social security systems. This Committee, with representatives from all Member States, has the tasks to monitor all questions and problems of administrative and interpretative nature and to facilitate the uniform application of EU-legislation (based on Title IV of Regulation 883/2004).

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**The main principles of the current rules**

Regulation 1408/71, concluded in 1971, and the complete revision with the Council Regulations concluded in 2004 and 2009 guarantee workers who are EU-citizens the right to social security benefits, irrespective of the place of work or residence. Workers who decide to settle down in another EU country have, in principle, the right to be treated as if they were citizens of that country. The objective was and is a reciprocal coordination, not the harmonisation of the social security systems in the Member States, in order to regulate cross-border situations. The general rule for the social security in the case of labour migration is the application of the country where the work is performed principle (the *Lex loci laboris*). Workers have to be insured and will build up and acquire social security rights in the country where the work is pursued. The 2004/2009 revision enhanced the right of equal treatment. Whilst this principle was originally applied only for persons who at the same time had decided to work and live in another country, the condition to reside there is no longer an absolute must. A second modification broadens the scope. Next to workers, self-employed, civil servants, students and pensioners, with their family and relatives, non-active persons are inserted in the application of the coordination rules. The scope of application no longer contains an exhaustive enumeration. A third change is the simplification of several rules with regard to unemployment: an unemployed who decides to move to another Member State in order to find a job, retains during a certain period the right of unemployment benefit payments in the country of origin.

**The functioning of these rules**

In addition to the coordination rules for the social security, the terms as formulated in Directive 2004/38/EC with regard to the residence rights of EU citizens that want to live in another Member State apply. EU citizens have the right to live on the territory of a Member State for a maximum period of three months without further conditions or formalities to fulfil, except the obligatory possession of a valid identity card or passport. EU citizens who want to stay for a longer period in another Member State either must be employed or self-employed in the host country or dispose of sufficient resources for themselves and their family members to ensure that they do not lay claims on the social assistance system of the host country during the stay. During the first three months of residence, the host country is not obliged to confer entitlement to social assistance. As long as EU citizens and their family members not become an unreasonable burden on the social assistance system of the host country, they cannot be expelled. If they are an employee or self-employed, expulsion is under no circumstances legitimate. Every EU citizen residing lawfully for a continuous period of five years in the territory of the host country, acquire a permanent residence in that country. Until the expiry of this period, expulsion is possible if a person does not comply with the applicable requirements.

**Important case law**

The Court of Justice of the European Union has clarified the right of access to (parts of) the social security. In a few cases, the central question was whether economically inactive EU citizens residing in another Member State are entitled to claim rights to social benefits, which apply to the citizens of that country. The coordination regulations seem to suggest these rights, although Directive 2004/38/EC does not impose this obligation. In November 2013, the Court ruled in the so-called *Dano*-case. A woman of Romanian origin, a long-time resident in Germany, had never worked in Germany and was not a job seeker. Her appeal on social assistance for job seekers was dismissed. The case was brought before the European Court. The Court confirmed, according to the EU-legislation regulating the free movement (Directive 2004/38), that the host country is not obliged to grant social assistance during the first three months of residence. Is that period exceeded (but still less than 5 years), providing one's own subsistence becomes a condition for the right of residence. If someone does not meet these requirements, no entitlement to social benefits exists. There is in general only entitlement for benefits for which contributions are paid (e.g. unemployment benefits). The ruling is important in light of the discussion on social security and welfare tourism.

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**Some legal loopholes**

An exception, formulated in the coordination of social security Regulations, to the country of employment principle applies to posted workers who work temporarily in another country on behalf of their employer in the frame of the freedom to provide services. A person who is posted for a period shorter than 24 months remains subject to the social security system of the country where he/she is usually employed. The administrative work and costs necessary to integrate workers who work for a short time in another country in completely different social security systems do not outweigh the benefits. Besides, it is hard to derive rights in such short periods. However, the relationship between posting and social security has appeared susceptible to various ways of problematic use.

The Basic Regulation 883/2004 defines the maximum period of posting at 24 months.[i] After these 24 months, in principle the rules of the country where the work is performed apply, unless an agreement is reached within the meaning of Article 16 paragraph 1 of the Regulation.[ii] This period of 24 months is not mentioned explicitly in the Posting of Workers Directive 1996/71/EC. Earlier research revealed two important problems.

- Posting of workers in the frame of cross-border service provision is used as an instrument for transnational recruitment whereby workers are recruited from countries with low social security costs. This occurs in the construction and agriculture, and meanwhile in other sectors with strong competition on labour costs.
- Secondly, the creation can be detected of fictitious foreign companies that recruit workers who then are posted into several countries. Examples can be found in international road transport and inland waterway transport.

**Cross-border provision of services**

The deficient control on compliance with the social security payments and with existing employment conditions, combined with low risks of detection create plenty of space for unscrupulous companies that circumvent through various misleading ways the rules and regulations. Falsification of the so-called A-1 forms (a standardized statement that proves the social security registration of any country), the use of the posting formula to foreign workers who have been living in the country of employment and job mediation by fake agencies or letterbox structures are practices that have come to light in controls. A report drafted by the labour inspectorate and the most engaged social partners in 9 countries revealed the complicated control on the legality of the posting. The fact that the country where the work is pursued has only limited powers when it comes to checking the legitimacy of posted work and the employment relationship between the posted workers and the posting company in the country of origin impedes effective control. Limited power resources and poor functioning sanctions, partly because of a lack of international cooperation in gathering information and dealing with fraud, hamper the effective exercise of checks on lawfulness. Besides, a host country has few competences to control to what extent a company is legitimate; cooperation of the host country is crucial.[iii]

**Free establishment and the use of letterbox companies – a case**

In recent years several transport companies (in the Benelux countries) received the offer to transfer the workforce to intermediate companies (located in, for instance Cyprus) and to hire the staff through these intermediate service suppliers. The 'companies' publish glossy websites in various languages and from different addresses in Europe. With reference to the changes in the coordination of social security as a result of Regulations 883/2004 and 987/2009 (applicable since May 2010), the intermediates offer to act as employers for the workforce. The original employer of the truck drivers would become the 'client' and only receive an invoice for supplying services, whilst the truck drivers would continue to work for the original employer. Truckers who work for this client (their former employer) earn the minimum wage (taxed for income in the home country) and all other wage components and bonuses (for overtime and irregular work, for instance) are paid undeclared (neither in the home country of the worker, nor in the country of establishment of the letterbox).

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The social security payments are based on the minimum wage and the former employer is 'freed' from additional payments (such as mandatory employer contributions in the home country or sectoral charges for pensions or vocational training). The recruitment of workers through these letterbox companies is presented as a 'perfectly legal' method to make substantial savings on the labour costs of drivers. The introduction of a labour contract under a foreign legal frame (even though workers do not live there and never will get to that country) creates this opportunity. In short, the use of foreign intermediaries is lucrative because of the lower social security contributions. The used method to circumvent the mandatory social security contributions refers to the Basic Regulation on the coordination of the social security. It often takes place through the provision of A1 (previously E101) forms in the intermediate's country of registration. This standardised EU-form declares where a person is registered for the social security and in which country contributions are paid. The issuing of the form has some built-in control mechanisms. The competence to figure out in which country the government must provide an A-1 document lies first in the hands of the competent body in the country of residence of the driver. Besides, the coordination rules impose conditions on the genuine character of a company: it must be a company with local operations and output in the country of establishment. In some cases, it turned out that uninsured drivers drove around with foreign A-1 documents, which were issued without the competent body involved. Paychecks made it clear that social security payments were not duly made in the country of establishment, since only the basic wage and not the total wage premium was paid.
In one case, brought up by the Dutch transport union FNV, it took 16 months (and a change of government) to convince the social security authorities to enforce Dutch social security and working conditions. The case was clear from the beginning and transmitted to the Dutch authorities in March 2012, but partly because of the fear that the authorities of the workers' country of residence would be accused of 'creating barriers to the free provision of services', the competent social security institution – Sociale Verzekeringsbank (SVB) – was reluctant to act immediately. The final statement issued by SVB in October 2013 was clear, however: based on Regulations 883/2004 and 987/2009, truck drivers living in the Netherlands and on the payroll of one of the intermediates had to stay in the social security system of their country of residence – the Netherlands. The case had other far-reaching consequences. The SVB stated that the labour relation was still intact with the client (the original employer) 'as the activities were still pursued under the subordination and authority of the client'. The SVB concluded that the intermediate firm could not prove that it was a real undertaking with activities in the country of registered office. In summary, the link between the driver and the intermediate was qualified as artificial and created with the sole aim of circumventing social security obligations in the country of residence.

**Welfare tourism debated**

In 2013, the Dutch Government notified the European Commission that the free movement of EU citizens posed the risk of migration motivated by the search for social security payments. The responsible state secretary spoke of a major problem with EU citizens applying for assistance without having worked in the Netherlands. His evidence came from a fraud case by Bulgarian citizens who had received some local benefits. In total, he claimed a number of 4200 EU citizens seeking payment of social benefits in the Netherlands. The government wanted to put an end to this and asked the European Commission to come up with a solution. The Commission in turn argued that it was a non-issue; the Netherlands scored well below the average in terms of the number of resident Europeans on benefits. A year later, the European Court of Justice judged in a case of a Romanian woman who moved to Germany and applied for social assistance there (C-333/13 - *Dano*). The Court stated that the right to free movement does not automatically imply the right to social assistance: an EU citizen who resides more than three months in another Member State must have sufficient resources in that country to provide for his or her livelihood. According to the Court, EU countries have the right to refuse welfare benefits (special, non-contributory cash benefits) to nationals of other Member States, who have come to their country especially for those benefits.[iv]

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In another case (*Alimanovic*, in September 2015), the Court ruled that equal treatment with regard to the right to social assistance depends on the legality of stay in the country. Remarkable was that the person had worked for 11 months (in Germany) and then had enjoyed a lawful period of six months of unemployment benefits. The German social insurance agencies decided after those six months no longer to provide benefits; the Court approved this policy. The Court referred to Article 7.3.c of the EU Directive 2004/38. This article states that EU citizens who become involuntarily unemployed within the first twelve months of their stay in another country retain their status as legitimate job seeker in the country and are entitled to equal treatment in the social security for a period of at least 6 months. After a period of six months, the host Member State has the right to refuse access to non-contributory forms of social assistance.

**Who is entitled?**

Entitlement to benefits differs depending on the type of benefit. Relevant is the distinction between contributory benefits (such as unemployment benefits and work-related pensions) and social assistance. Non-Dutch EU citizens cannot simply settle in the Netherlands and then apply for social assistance. One condition for the application of the free movement and the right to establish in another EU country is that a person is able to provide the own subsistence and living costs. An EU citizen should, after a stay of three months, either be employed or self-employed, or have sufficient means of subsistence.[v] People who have worked in the Netherlands and have contributed to the social security are consequently insured for their social costs and, if they fulfil all other conditions, have the right to receive, for instance, unemployment benefits. Workers from another EU Member State, who have contributed and have worked at least 26 weeks in a reference of 36 weeks, derive the right to receive unemployment benefits during 3 months. This period is extended if the worker has worked for at least 4 years in a period of 5 years.

**Available data**

Few detailed figures are available on the composition of the group of benefit recipients in the Netherlands. The overall number of benefit recipients rose to 490,000 people (in August 2015, including state pension recipients with additional benefits), after a decline that began since 1998 and brought back the total to 370,000 in mid-2007. Changes in the conditions for receiving benefits make the numbers not fully comparable; however, the figure provides a proxy idea. It is worthwhile, independent of the question how many people are included, to analyse who receives benefits and whether there have been important changes over the years.

The Dutch statistical office CBS records EU-citizens in the category *western allochthones*. A large part of this category origins (according to the CBS-definitions) from a German or Indonesian background. The size of citizens coming from Central and East European countries (CEE MOE) has increased in the last 10 years (to 177,000 per 1 January 2015). There were 108,000 citizens with a Polish background. The total of residents coming from Bulgaria and Romania in 2013 was around 4% of all EU-residents (or 0.23% of the total population). The share of *western benefit receivers* in the overall figure of benefit receivers was stable; in absolute size the overall total increased in recent years to 54,500 persons (in August 2015, a decrease started from spring 2015). In total, 4,160 citizens from CEE-countries that belong to the labour force (15-65 year old) received (by the end of December 2013) social protection benefits. The use of social protection by CEE-migrants is slightly higher than the use by the autochthones (2.8% compared to 2.3% per 1-1-2014). However, the share of unemployment benefits of CEE-residents was substantially lower (in August 2014) with 2.4%, compared to 6.9% for Dutch workers. The percentage of non-Dutch unemployed is increasing.[vi]

The 75,000 temporary workers from CEE-countries, calculated in the so-called *Migrantenmonitor*, in general have no entrance to the social protection or unemployment benefits. If these workers are included in the calculations of the benefit use, the share of CEE-workers having benefits falls sharply.[vii]

The total of *non-western benefit receivers* increased steadily to 241,000 persons (in August 2015). However, figures on the background of this category are less reliable.

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**To resume**

The statistical office CBS has published data on benefit fraud that reveal a serious decrease of fraud in the period 2002-2008. The available data provide no evidence for the existence of large-scale welfare tourism related to social protection benefits. Most migration and mobility related research in Europe confirms that migrants are not interested in the country with the best social benefits. The general rule is that the presence of jobs is the most predictive parameter for an increase of labour migration and mobility. Research and literature provide a certain pattern for the impact of this type of labour migration on the welfare state, and particularly on the social security. Labour migrants in the lowest segment of the labour market perform very often work for which it is difficult to find sufficient labour supply in the receiving country. Partly, there is the effect of substitution, whereby other vulnerable groups are pushed out of the labour market. There are only few incentives for employers, in case of enough supply of cheap labour, to invest in these more vulnerable workers. Besides, the import of cheap labour can have a downward effect on the wages of the lowest pay scales. The use of labour migrants can conserve certain types of low-paid jobs (and the related production of goods and services) that normally would have disappeared. This all seems not very rational, as it could block innovation, but, for instance, it still keeps the Dutch agro- and horticulture profitable. In other sectors that are inland or site specific, like domestic work and caretaking, the influx of migrants guarantees the necessary and growing services that are closely related with the future of the welfare state.

The Dutch labour market is not very generous with regard to the offer of stable jobs. Many migrant workers work in precarious and flexible jobs with short time contracts, as such they belong to the invisible and unrepresented part of the labour market. The cross-border recruitment of workers has facilitated the expansion of flexible labour relations. Labour is becoming more and more a commodity, with work performed under a contract for the provision of services, by a person who is no longer considered a stakeholder. Thus, the impact of cross-border mobility of workers on the flexibilisation of the (Dutch) labour market is continuously expanding. If the result is less contributions to the social security schemes, in the end the impact on the financial sustainability of the welfare state will increase.

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[i] Article 12.1 Regulation 883/2004: A person who pursues an activity as an employed person in a Member State on behalf of an employer which normally carries out its activitie s there and who is posted by that employer to another Member State to perform wo rk on that employer's behalf shall continue to be subject to the legislation of the first Member State, provided that the anticipate d duration of such work does not exceed twenty-four months and that he is not sent to replace another person.

[ii] Article 16.1 Two or more Member States, the competent authorities of these Member States or the bodies designated by these authorities may by common agreement provide for exceptions to Articles 11 to 15 in the interest of certain persons or categories of persons.

[iii] http://www.eurodetachement-travail.eu/datas/files/EUR/synthesegenerale_2013EN.pdf

[iv] http://curia.europa.eu/juris/document/document.jsf?docid=159442&mode=lst&pageIndex=1&dir=&occ=first&part=1&text=&doclang=EN&cid=705697

[v] http://www.europarl.europa.eu/atyourservice/en/displayFtu.html?ftuId=FTU_5.10.4.html

[vi] UWV Kennisverslag 2015-1, april 2015, Kenniscentrum UWV, www.uwv.nl/kennis

[vii] Ontleend aan http://www.cbs.nl/nl-NL/menu/home/default.htm (bezocht op 12-1-2014).

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