Culture, Tourism, Europe and External Relations Committee

Inquiry - Immigration

Written submission from The Federation of Small Businesses (FSB)

Overview

The Federation of Small Businesses (FSB) welcomes the opportunity to respond to the Committee’s immigration inquiry.

FSB is Scotland’s leading business organisation. As experts in business, we offer our members a wide range of vital business services including advice, financial expertise, support and a powerful voice in government. Our mission is to help smaller businesses achieve their ambitions. These micro and small businesses comprise the majority of all enterprises in Scotland (98%), employ around one million people and contribute £68bn to the economy.

Since the outcome of the referendum on the UK’s membership of the European Union (EU), FSB has undertaken extensive engagement with our members across the UK to better understand the potential opportunities and risks of the UK leaving the EU. This work was summarised in four reports, published earlier this year:

1. Access to EU single market and non EU markets
2. Access to skills, labour and ease of ‘doing business within the EU’
3. EU funding and what happens next
4. Regulatory framework following Brexit

These reports were supplemented by additional analysis on the two key Brexit issues facing small firms in Scotland: international trade and access to skills and labour. It is outside the remit of this inquiry to summarise the main findings from each of these research programmes; nonetheless it is worth stating that, as a result of the current UK-EU 27 negotiations, easy access to the single market and the ability to hire EU workers are key concerns for smaller businesses in Scotland.

Indeed, their ability to hire people with the right skills and to do business in the EU is fundamental to small firms’ survival and growth in Scotland. Accordingly, FSB has consistently called for:

- The right to remain for EU citizens who are working in Scotland and the rest of the UK, before the point at which we leave the EU.

• A transition period of at least three years – during which existing immigration and trade arrangements continue – following our departure from the EU and until a new immigration system starts to be phased in through an implementation period.

Summary

The UK’s departure from the EU provides an opportunity to develop a new immigration system. In this response, FSB makes the following points:

1. Current UK immigration policies should better respond to Scotland’s demographic, economic and skills needs. EU migration has helped reverse declining population levels and there is a real risk that Brexit will impact Scotland’s ability to grow its population and its economy. Attracting working age migrants to Scotland is a pre-requisite for future economic prosperity.

2. Future decreases in immigration to Scotland, particularly from the EU, will create additional skills shortages and recruitment difficulties for the economy. This will be especially pronounced in key sectors like tourism, construction and healthcare that are reliant on EU workers.

3. Any new immigration system must consider and be responsive to the needs and capabilities of smaller businesses.

4. A new immigration system would benefit from being flexible enough to accommodate the significant variations in the migration and skills needs of particular nations and regions within the UK. Therefore, FSB would welcome additional analysis on the feasibility of a UK differentiated immigration system for employers. Building in greater flexibility is important but it is equally important to ensure we simplify and reduce compliance costs for small employers and maintain the mobility of EEA/EU workers once in the UK.

Lastly, it is worth pointing out that FSB does not have expertise in the administration of the UK immigration system. Rather, our interest is in the outcomes of UK immigration policies and how they affect small employers following Brexit. We have therefore limited our response to these aspects of the Committee’s inquiry.

Small businesses and EU workers

Prior to considering the proposals outlined by Dr Hepburn, the Brexit work published by FSB on skills and labour provides useful context for the Committee’s deliberations. Broadly, it focused on two areas: first, how small businesses in Scotland would be affected by, and respond to, restrictions to the free movement of people; and second, the role of employers in a new immigration system.

The end of free movement to the UK from EU countries, and the introduction of new immigration arrangements for EU citizens seeking to work in the UK, are key challenges facing Scottish small business owners. Indeed, of the 181,000 EU

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citizens living in Scotland, 63% are in employment (114,247) and many work in small businesses.

According to FSB research, one in four small employers in Scotland (26%) have at least one employee from an EU country, which is five per cent higher than levels for the UK as a whole (21%). The reliance on EU workers also differs by geography and sector – just under half of employers in the Highlands have EU workers (41%) compared to 28% in the Aberdeen city region, while those operating in tourism and leisure are more likely to have EU staff (45%). The benefits smaller businesses have gained from having access to EU labour and skills cannot be overstated. As one FSB member put it:

“The talents of EU nationals have helped our business thrive over the past 25 years and we would be worried if we were to lose our current staff due to the EU referendum result. Looking to the future, firms like ours must be able to continue to source international talent and labour if that’s required.” Alasdair Hughson, Keltic Seafare, Dingwall

Allied to this there is the real possibility that efforts to grow the economy will be undermined by lower numbers of EU migrants settling in Scotland. This is especially problematic given the demographic challenges facing the country – people aged 75 and over are projected to increase by 85% in around two decades – and the fact that “most of our population growth is supported by inward migration.”8 Indeed, since 2000, 50% of the increase in non-UK people living in Scotland has come from EU citizens. This is in stark contrast to the UK which is overall less reliant on inward migration for population growth.

Small businesses and free movement of people

At this stage little is known about the short, medium and long-term impact Brexit will have on small businesses. What we do know is that Scotland could face immediate skills and labour problems if, according to KPMG, 77,829 EU citizens act on their plans to leave the country.9 How employers react to a labour market where EU labour and skills are increasingly scarce is therefore an important consideration in the development of a new immigration system.

As outlined in the graph below, FSB research found that small employers would consider a diverse set of strategies to continue meeting their labour and skills needs following Brexit and cope with increased competition for staff.

Roughly, it is possible to identify two groups. On the one hand, there are employers who would adapt their recruitment practices by hiring UK citizens with equivalent skill levels or continuing to employ EU citizens and incurring any additional costs. On the other hand, there are those employers who would consider making significant changes, such as reducing operations, closing their businesses or moving operations abroad. This was articulated by a business owner interviewed during the research who said that:

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8 Ibid.
“If I didn’t have access to my non-UK workforce I would close down. I would not operate without my European staff. It wouldn’t be possible. I would have real reservations about my ability to get the skills I need from UK workers alone. Not just reservations – I know it wouldn’t happen. There are plenty of other businesses in my sector who wouldn’t do very well at all if all the European workers went home. They would probably collapse.” FSB member, Construction

Figure One: Options business owners with EU employees would consider if there were more barriers to recruitment

Source: FSB Scotland Brexit Skills Survey

<table>
<thead>
<tr>
<th>Option</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recruit UK citizens with the same skills</td>
<td>59%</td>
</tr>
<tr>
<td>Continue to employ EU citizens and accept any additional costs</td>
<td>44%</td>
</tr>
<tr>
<td>Reduce your business operations</td>
<td>37%</td>
</tr>
<tr>
<td>Sponsor non-UK non-EU citizens to work in your business</td>
<td>27%</td>
</tr>
<tr>
<td>Close the business</td>
<td>19%</td>
</tr>
<tr>
<td>Invest in training existing workforce to fill skills gaps</td>
<td>16%</td>
</tr>
<tr>
<td>Consider moving operations abroad</td>
<td>12%</td>
</tr>
<tr>
<td>Invest in machinery to automate processes that were...</td>
<td>11%</td>
</tr>
<tr>
<td>Increase wages or benefits to attract similar quality domestic...</td>
<td>7%</td>
</tr>
</tbody>
</table>

A post-Brexit immigration system

Given that 26% of Scottish employers have at least one employee from the EU and the majority recruit EU workers from Scottish and UK labour markets (85%), the future treatment of EU citizens is an important issue for the small business community. This point is worth expanding upon because 95% of small employers have never made use of the UK’s points-based immigration system – mainly because their business’ labour and skills needs were being met through UK and EU labour markets.10

“Sectors like mine would never have expanded in the last ten years without EU workers. They have been central to business growth.” FSB member, Aberdeen

Needless to say, there will be challenges for smaller employers navigating the current complex and largely unknown immigration system, while the Home Office is introducing and administering a completely new system.

FSB research published earlier in the year found that 56% of UK employers of EU citizens were concerned about being expected to enforce new immigration rules in a post-Brexit environment. This is unsurprising given the UK Government, via the Immigration Acts of 2014 and 2016, has placed additional enforcement duties on employers to “reduce the demand for skilled migrant labour”.11 Further, the

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introduction of an Immigration Skills Charge has increased the cost of skilled workers from outside the European Economic Area to:

“… cut down on the number of businesses taking on migrant workers and incentivise training British staff to fill those jobs”.

Unsurprisingly these policies have led many small businesses, which employ people for their suitability, skills and attitude, to feel penalised for hiring foreign workers to sustain and grow their businesses. The UK’s departure from the EU, therefore, provides an opportunity to develop a new approach to immigration. The extent to which this system enables Scotland to better respond to the county’s demographic and skills challenges is an important consideration.

Options for differentiating the UK immigration system

Recognising the varying demographic and employment challenges across the UK, FSB has highlighted the benefits of an immigration system which is able to adapt to the different needs of the UK’s nations and regions. In Scotland, access to skilled staff and labour has been a consistent barrier to growth for small firms even with the larger pool of labour currently at their disposal.

During our research with FSB members we were particularly struck by the recruitment challenges facing many smaller businesses, especially those in labour-intensive sectors operating in sparsely-populated rural areas. As outlined above, many businesses have adapted to this by recruiting migrant workers already in the local area.

Taking these concerns into consideration alongside Scotland’s need to adapt to an ageing population, it is our view that any future decreases in (controlled) immigration to Scotland would create additional skills shortages and recruitment difficulties in specific sectors. As a result, we believe there is merit in the idea that the Scottish Government should have a stronger role in any new immigration system.

It is within this context that we welcome Dr Hepburn’s extensive research into immigration models in Europe, Canada and Australia and the options for a differentiated UK system. As an overarching principle, FSB believes any moves to differentiate immigration policies in Scotland would have to meet the needs and capabilities of small businesses, as these employers would have a key role to play in any new system. These businesses comprise 98% of all firms in Scotland, employ a million people and have created around one in three new jobs.

Thus, however important it may be to introduce a flexible immigration system, it is equally important to ensure we simplify and reduce compliance costs for small employers – many of whom do not have a dedicated HR function to meet their regulatory requirements. Moreover, given the employer’s perspective was not part of

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15 See: http://www.fsb.org.uk/standing-up-for-you/national-offices/scotland/news/2017/08/16/top-three-tips-for-understanding-jobs-figures
Dr Hepburn’s remit, FSB would welcome additional analysis on whether differentiated systems in multi-level states leads to further costs and complications for employers.

Dr Hepburn’s comprehensive research suggests that differential immigration systems can enable multi-level states to better meet their labour market needs through integrated and bespoke regional economic and migration strategies. The report further sets out a range of measures which could create greater alignment between the economic needs of Scotland and its immigrant settlement patterns.

The range of proposals categorised by Dr Hepburn as “soft and mid-range levers” appear sensible, practical and relatively easy to implement. These specific proposals – which would increase the Scottish Government’s role in immigration – to improve migrant economic integration, increase international outreach activities, and ensure Scotland better contributes to UK decision-making on immigration, could allow better consideration of Scottish needs. As a result, we believe there is merit in:

1. Introducing Scottish Government representation on the Migration Advisory Committee (MAC) to advise on labour shortages and skills gaps in Scotland. Indeed, there is precedent for such a move with the appointment of a Scottish representative on the Ofcom board.

2. Revising and expanding the Scottish Shortage Occupation List given the diverging needs of the Scottish and UK economy – and in particular the potential labour and skills gaps that emerge following Brexit. Although the MAC has found it difficult to obtain relevant labour market information, other countries such as Canada, Spain and Switzerland operate effective immigration systems which consider sub-state labour market needs for equivalent Shortage Occupation Lists. Further, we would highlight the extensive data set gathered by Skills Development Scotland and the creation of a new Scottish Government analytical unit as routes to improve data collection.

3. Charging existing Scottish Government international offices in the USA, Canada and Brussels to promote Scotland as a world-leading location to start a business, with a view to expanding the number of offices abroad in Poland, Germany, Spain and Italy (countries that comprise the largest groups of EU citizens in Scotland). Given that people born in European Economic Area (EEA) countries and non-EEA countries are more likely to start a business in Scotland, action is required to pre-empt any potential reduction in start-up rates as a consequence of Brexit.

19 See: https://www.skillsdevelopmentscotland.co.uk/what-we-do/partnerships/regional-skills-assessments/
On balance, we believe that the importance of labour and skills challenges facing Scottish smaller businesses requires an immigration system which is able to differentiate need in different parts of the UK, perhaps by giving the Scottish Government a stronger role in immigration processes. Some of the measures set out in the Committee's report demonstrate how this could be achieved; nonetheless, further work is required to assess if differentiation leads to greater costs and complexity for employers, particularly given the majority of small employers have never used the UK's points-based immigration system.