

Summary: Intervention & Options

Department /Agency:
**Border & Immigration
Agency**

Title:
**Impact Assessment of Fees for the Highly Skilled tier of
the Points-Based System**

Stage: Final

Version: 4

Date: 29 January 2007

Related Publications: Highly Skilled Migrants under the Points Based System: Statement of Intent; Response to charging consultation

Available to view or download at:

<http://www.bia.homeoffice.gov.uk>

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What is the problem under consideration? Why is government intervention necessary?

The Government wishes to implement the tier for highly skilled migrants as the first part of the new Points Based System for managed migration, based on that operated in Australia. The Highly Skilled tier (Tier 1) will embrace four sub-categories: General; Entrepreneurs; Investors; and Post Study Work. The Government wishes to set fees for the Highly Skilled tier that meet our charging policy objectives which include recovering the true end-to-end costs of the immigration system from those who benefit most.

What are the policy objectives and the intended effects?

- To rebalance the funding of the immigration system to ensure that those who benefit most from the service make a larger contribution, helping to reduce the burden on taxpayers
- To charge fees that recover the full administrative costs and that help to recover the true end-to-end costs of the immigration system from initial application to enforcement and compliance activities from those who use it
- To develop a fees model that is clear, straightforward and easily understood to our customers

What policy options have been considered? Please justify any preferred option.

1. Do nothing - maintain the existing fees charged for the routes on which the Highly Skilled tier sub-categories are based
2. Charge one fee of £600 for out-of-country and £750 for in-country and extension applications
3. Maintain existing fees as far as possible but align some fees to produce a more consistent fees structure

The preferred option is 3. This will minimise the negative impact on the economy and at the same time meet the stated charging policy objectives.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? Regular review of volumes of applications against projected demand with assumption of fee change to reflect cost charges.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.

Signed by the responsible Minister:

.....Date:

Summary: Analysis & Evidence

Policy Option: 2

Description: Charge one fee of £600 for out-of-country applications and one fee of £750 for in-country applications

COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups' The main affected group is applicants who will have to pay an additional £61.5m in fees over five years. The economy will also lose £21.1m in output from a reduction in the numbers of migrants coming or remaining in the UK to work.
	One-off (Transition)	Yrs	
	£	5	
	Average Annual Cost (excluding one-off)		
	£ 4.2m	Total Cost (PV)	£ 19.7m
Other key non-monetised costs by 'main affected groups'			

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups' The key benefit is the additional revenue to the government of the fee increases £61.5m over five years (the majority of this is transfers).
	One-off	Yrs	
	£	5	
	Average Annual Benefit (excluding one-off)		
	£ 1.4m	Total Benefit (PV)	£ 6.4m
Other key non-monetised benefits by 'main affected groups' Improved fairness as those who benefit from managed migration contribute more to the cost of administrating it.			

Key Assumptions/Sensitivities/Risks

A wage elasticity of labour supply of 0.5 was used to estimate the likely decrease in numbers of applications as a consequence of the proposed fee increases. The range used below is 0 to 1.1.

Price Base Year 2008	Time Period Years 5	Net Benefit Range (NPV) £ (36.9m)-6.4m	NET BENEFIT (NPV Best estimate) £ (13.2m)
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What is the geographic coverage of the policy/option?			Worldwide		
On what date will the policy be implemented?			February 2008		
Which organisation(s) will enforce the policy?			N/A		
What is the total annual cost of enforcement for these organisations?			£ N/A		
Does enforcement comply with Hampton principles?			Yes		
Will implementation go beyond minimum EU requirements?			N/A		
What is the value of the proposed offsetting measure per year?			£ N/A		
What is the value of changes in greenhouse gas emissions?			£ N/A		
Will the proposal have a significant impact on competition?			No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium	Large
Are any of these organisations exempt?		No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)				(Increase - Decrease)
Increase of	£ 0	Decrease of	£ 0	Net Impact £ 0

Key: Annual costs and benefits: Constant Prices (Net) Present Value

Summary: Analysis & Evidence

Policy Option: 3

Description: Maintain existing fees as far as possible but align some fees to produce a more consistent fees structure

COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups' The main affected group is applicants who will have to pay an additional £43.2m in fees over five years. The economy will also lose £13.2m in output from a reduction in the numbers of migrants coming or remaining in the UK to work.
	One-off (Transition)	Yrs	
	£	5	
	Average Annual Cost (excluding one-off)		
	£ 2.6m	Total Cost (PV)	£ 12.3m
Other key non-monetised costs by 'main affected groups'			

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups' The key benefit is the additional revenue to the government of the fee increases £43.2m over five years (the majority of this is transfers).
	One-off	Yrs	
	£	5	
	Average Annual Benefit (excluding one-off)		
	£ 1.1m	Total Benefit (PV)	£ 4.7m
Other key non-monetised benefits by 'main affected groups' Improved fairness as those who benefit from managed migration contribute more to the cost of administrating it.			

Key Assumptions/Sensitivities/Risks

A wage elasticity of labour supply of 0.5 was used to estimate the likely decrease in numbers of applications as a consequence of the proposed fee changes. The range used below is 0 to 1.1.

Price Base Year 2008	Time Period Years 5	Net Benefit Range (NPV) £ (22.3m)-4.7m	NET BENEFIT (NPV Best estimate) £ (7.6m)
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What is the geographic coverage of the policy/option?		Worldwide		
On what date will the policy be implemented?		February 2008		
Which organisation(s) will enforce the policy?		N/A		
What is the total annual cost of enforcement for these organisations?		£ N/A		
Does enforcement comply with Hampton principles?		Yes/No		
Will implementation go beyond minimum EU requirements?		Yes/No		
What is the value of the proposed offsetting measure per year?		£ N/A		
What is the value of changes in greenhouse gas emissions?		£ N/A		
Will the proposal have a significant impact on competition?		Yes/No		
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)		(Increase - Decrease)	
Increase of £	Decrease of £	Net Impact	£

Key:	Annual costs and benefits: Constant Prices	(Net) Present Value
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Evidence Base (for summary sheets)

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

1. BACKGROUND TO THE HIGHLY SKILLED TIER

1.1 In 2006, following an extensive public consultation, we published proposals to modernise and strengthen our immigration system by bringing in an Australian-style points system comprising five tiers:

- Tier 1 Highly skilled individuals to contribute to growth and productivity.
- Tier 2 Skilled workers with a job offer to fill gaps in the UK labour force.
- Tier 3 Low skilled workers to fill specific temporary labour shortages.
- Tier 4 Students.
- Tier 5 Youth mobility and temporary workers: people coming to the UK to satisfy primarily non-economic objectives.

1.2 The Highly Skilled tier is about boosting the UK's economy by attracting and retaining the "brightest and best" as workers or businesspeople. Highly Skilled migrants will be free to seek employment anywhere in the UK, which will widen the pool of highly skilled individuals available to employers, whilst maintaining the flexibility of the UK labour market. Unlike the other tiers, we will not ask applicants in the Highly Skilled tier to have sponsors.

1.3 The Highly Skilled tier will embrace:

General

For migrants who wish to find highly skilled employment in the UK.

Entrepreneurs

For those investing in the UK by setting up or taking over, and being actively involved in the running of, a business.

Investors

For high net worth individuals making a substantial financial investment in the UK.

Post-Study Work

This category aims to retain the most able international graduates who have studied in the UK. It will also enhance the UK's overall offer to international students.

1.4 There will be three ways of applying:

- Entering the UK in a Highly Skilled sub-category (out-of-country)
- Extending a stay in the UK in a Highly Skilled sub-category (extensions)
- Switching while in the UK into a Highly Skilled sub-category (in-country)

1.5 There will be a single application process and single application fee, whether in or outside the UK improving the efficiency of the decision making process. This replaces the current two-stage process that exists for certain routes where applicants have to demonstrate that they meet the relevant criteria prior to applying for entry clearance or leave to remain in the UK.

1.6 This Impact Assessment examines the costs and benefits of the different charging options for the Highly Skilled tier which is to be implemented from the first quarter of 2008. A separate Impact Assessment considering the wider impacts of the policy to introduce the Highly Skilled tier will be published on www.bia.homeoffice.gsi.gov.uk prior to implementation.

For further information on the Highly Skilled tier, please refer to '*Highly Skilled Migrants under the Points Based System: Statement of Intent*' (<http://www.bia.homeoffice.gov.uk/sitecontent/documents/managingourborders/pbsdocs/statementofintent/highlyskilledunderpbs.pdf>).

2. BACKGROUND TO CHARGING

- 2.1 During the course of 2003 and 2004, the Home Office introduced charges for a range of immigration and nationality applications. The first phase of full cost recovery charging sought to ensure that those who use and benefit from the UK's immigration service met the costs of delivering the administrative service (including staffing and overhead costs) of processing applications to the point of making and conveying a decision.
- 2.2 The IND Review (<http://www.homeoffice.gov.uk/documents/ind-review-250706/ind-review-eng>) published in July 2006 stated that we should charge a fair and economic rate for our services but also one that reflects the true operational costs of the immigration system rather than just administrative costs.
- 2.3 As the Home Office – including UKvisas - implement the various measures outlined in the Review, including the Government's plans to introduce the new Points Based System (PBS) for managed migration, we need to consider how these improved immigration services are paid for. We know that migrants contribute to our economy, and we are clear that any new fees we set for migrants to come to the UK must not adversely impact on the many benefits that legal migration brings. But it is right to take the approach that our charging strategy should better reflect the end-to-end cost of the whole immigration system, from initial application to enforcement and compliance activity.

3. RATIONALE FOR GOVERNMENT INTERVENTION

- 3.1 The IND Review signalled the biggest shake-up of the immigration system in its history, with a key component of the new approach being a step-change in the enforcement and compliance activity to ensure that the immigration laws are enforced.
- 3.2 The Government's position on this was laid out in the cross-Government enforcement strategy '*Enforcing the Rules: a strategy to ensure and enforce compliance with our immigration laws*' published on 7 March which committed around £100m extra for immigration policing, detention space, and systems to share data and intelligence on those here illegally, designed to bear down on those seeking to cheat the system and live illegally in the UK

It was agreed that there should be no increase to general taxation to fund this strategy. Resources will be raised through a new approach to the pricing of visas and immigration products so that those who directly benefit from our services pay more to fund the end-to-end process from initial application to enforcement and compliance activities. This approach to pricing applies directly to the Highly Skilled tier, and is fully outlined in the Government's charging strategy for immigration and nationality fees:

<http://www.bia.homeoffice.gov.uk/sitecontent/documents/aboutus/consultations/closedconsultations/newchargingregime/responses.pdf>

- 3.3 The Government's policy objectives on charging are:
 - To rebalance the funding of the immigration system to ensure that those who benefit most from the service make a larger contribution
 - To raise an extra £100m above administrative cost recovery to fund the true end-to-end costs of the immigration system from initial application to enforcement and compliance activities
 - To develop a fees model that is clear, straightforward and easily understood to our customers

4. OPTIONS

4.1 Three charging options are considered for the Highly Skilled tier.

4.2 Option 1: Do nothing

Maintain the existing fees charged for the routes on which the Highly Skilled sub-categories are based.

This option would mean that there would be a wide range of different fees for the Highly Skilled tier, depending on whether the migrant was inside or outside the UK at the time of application, and which sub-category they were applying under (see table 1 below). The stated charging policy objective having fees that are clear and straightforward would not be met. The aim of recovering the true end-to-end costs of the immigration system would also not be met unless fees for other parts of the Points Based System were increased to compensate. This would run counter to the Government's stated policy that those who benefit most from the immigration system should pay more. Alternatively, the extra funding could be raised from general taxation, but this is again incompatible with the Government's policy that there should be no increase in general taxation to fund the improvements to the immigration system.

4.3 Option 2: One fee of £600 for out-of-country applications and one fee of £750 for in-country applications and extensions across all Highly Skilled sub-categories.

This will simplify the fee structure. Historically, lower fees have been charged for out-of-country applications as it is believed that they are more price sensitive and have different cost bases. This differential will remain to minimise the negative impact of any substantial price changes. This option meets our stated charging policy aim of recovering the true end-to-end costs of the immigration system and reducing the burden on the taxpayer. It also meets our aim of having a simplified, easy-to-understand fees model.

However, this option does not meet our stated policy aim of setting fees so that those who benefit most from the system should pay comparatively more. It may be unfair to charge the same fees for applications to the Post-Study Work sub-category. Unlike the other sub-categories, Post-Study Work is there to provide a bridge to highly skilled or skilled work. People with Post-Study Work leave will be expected to switch into another part of the system as soon as they are able to do so. To encourage people to switch, leave will be fixed at a maximum of two years; it will not be possible to apply for further leave; and time spent in the sub-category will not count towards the threshold for being eligible to apply for settlement (for further information, please refer to '*Highly Skilled Migrants under the Points Based System: Statement of Intent*').

4.4 Option 3: Maintain the existing fees charged for the routes on which the Highly Skilled sub-categories are based as far as possible to minimise any negative impact but align some fees to produce a more consistent fees structure.

This option is a hybrid of options 1 and 2, maintaining existing fees as far as possible to minimise any negative impact to ensure that the UK continues to attract and retain the 'brightest and best', and at the same time developing a fees model that is simple and clear to understand. The proposed features of the fees model under option 3 are:

- One fee of £750 for all applications made within the UK (in-country and extensions) for the Highly Skilled General sub-category. This will simplify the fees model by having one fee of all applications made within the UK for this sub-category.
- Marginally increase fees for the Post-Study Work sub-category (in- and out-of-country) to contribute towards end-to-end full cost recovery
- Maintain the same fees for all other ways of applying for the Highly Skilled tier

This option meets our stated charging policy aim of helping to recover the true end-to-end cost of the immigration system. Although there will be a range of fees, a greater contribution is made on average by migrants applying to the General, and Entrepreneurs and Investors sub-categories. This is in line with our stated charging policy aims of rebalancing the funding of the immigration system to ensure that those who benefit most from the service make a larger contribution to funding the end-to-end process of administration, and enforcement and compliance. Successful

applicants to these sub-categories receive the greatest benefits from the system. They will be granted three years' initial leave with the possibility of applying for further leave of two years, and time spent under these sub-categories will count towards the threshold for being eligible to apply for settlement. They will also have unrestricted access to the labour market, without the need to have a sponsor.

As stated under option 2, the Post-Study Work sub-category is there to provide a bridge to highly skilled or skilled work. As such, a lower fee for this sub-category reflects the lower benefits for these applicants, and is in line with our stated charging policy aims. Setting a reasonable fee will provide an incentive to the most able international graduates who have studied in the UK to remain and develop a career in the UK. It will also enhance the UK's overall offer to international students.

Table 1: Proposed fees for each option

Highly Skilled sub-categories	Option 1	Option 2	Option 3
General: in-country	750 (635) ¹	750	750
General: out-of-country	600 (530) ²	600	600
General: extensions	350	750	750
Entrepreneurs & Investors: in-country	750	750	750
Entrepreneurs & Investors: out-of-country	200	600	200
Entrepreneurs & Investors: extensions	750	750	750
Post-Study: in-country	395	750	400
Post-Study: out-of-country	200	600	205

5. COSTS AND BENEFITS

5.1 A model was developed to examine the **additional** costs and benefits to society of options 2 and 3 compared with option 1 over a five-year period (08/09 to 12/13). Note that option 1 has no additional costs and benefits and is the baseline used for comparison. **Volumes are based on historical figures for 2006/07 for the routes which the Highly Skilled tier is based³. No attempt is made in this Impact Assessment to forecast likely changes to volumes as a result of the introduction of the Points-Based System.**

5.2 Impact on volumes

In general, when prices increase, demand falls. So the proposed fee increases in options 2 and 3 are expected to lead to a decrease in applications. To determine how much applications are expected to fall by, the 'price elasticity of demand' must be estimated. That is, the 'responsiveness' of demand to some change in price and it is calculated by taking the percentage change in quantity divided by the percentage change in price. Analyses of fee changes that took place in April 2007 indicate that the effect on volumes of fee increases were too small to detect. However, as migrants demand BIA products in order to supply labour in the UK, the wage elasticity of labour supply could be used to estimate the impact on volumes of the proposed fee changes (note that it is assumed that the change in fee is borne entirely by migrants and not by UK employers thus labour demand is unaffected. Highly skilled migrants are not tied to any employer and can enter/remain in the UK prior to finding and starting employment). Wage elasticity of labour supply provides a measure for how labour supply responds to a change in (expected) wage. The proposed fee increases for BIA products translate one-to-one into a fall in the expected wage of working in the UK for migrants (and alters the differential wages between different foreign labour markets and thus choice of migrant destination). So it is anticipated to decrease the aggregate supply of migrant labour to the UK and therefore demand for BIA products. No empirical studies on the wage elasticity of migrant labour supply to the UK have been found so general studies on the wage elasticity of labour supply are used as an estimate.

¹ £750 is comprised of current fees for the existing 2-stage application process for the Highly Skilled Migrant Programme (HSMP) where the migrant must pay £400 for a HSMP approval letter before paying £350 for leave to remain. The application approval rate was 67%. So the average fee that applicants currently pay is £635 (see table 2 in annex). Under PBS, there will be a single stage application process.

² £600 is comprised of current fees for the existing 2-stage application process for the Highly Skilled Migrant Programme (HSMP) where the migrant must pay £400 for a HSMP approval letter before paying £200 for a visa. The application approval rate was 65%. So the average fee that applicants currently pay is £530 (see table 2 in annex). Under PBS, there will be a single stage application process.

³ Assumptions are made on the dependent ratios for out-of-country applications.

A literature review of empirical studies suggests a wide range of aggregate wage elasticity of labour supply from -0.1 to 1.1 (see table 1 in the annex for further details). For the purposes of this Impact Assessment, the central estimate of 0.5 was used. That is, a decrease in wage of 1% would result in a drop in labour supply and the demand for BIA products of 0.5%. This assumption is tested in the sensitivity analysis.

The proposed changes in fees are expected to result in only a marginal change in expected wages over the duration of leave given to the migrant. The average annual expected wage for the General, Entrepreneurs and Investors sub-categories is approximately £40,000. So expected wages over the duration of initial and extension leave are £120,000 and £80,000 respectively. For Post-Study Work, the average annual expected wage is £17,715⁴. Expected wage over the duration of leave is therefore £35,430. The maximum proposed fee increase for option 2 is £400 and the highest percentage decrease in average expected wage is 1.15% resulting in a drop in BIA products of 0.57%. In total, it is expected that there will be a decrease of 160 applications in 08/09 and 580 applications over 5 years. Similarly for option 3, the maximum proposed fee increase is £400 and the highest percentage drop in average expected wage is 0.51% resulting in a drop in BIA products of 0.25% (see table 2 in the annex for a full breakdown). In total, it is expected that there will be a decrease of 50 and 250 applications in 08/09 and over 5 years respectively.

5.3 Impact on the economy

The benefits to the economy of the proposed fee changes are:

- Additional revenue raised from out-of-country applications through fee increases (note revenue raised from in-country and extension applications are transfers i.e. a loss for applicants but a gain to the Government).
Option 2: This is estimated at £1.4m for 2008/09 and £6.9m for the next five years.
Option 3: This is estimated at £1.0m for 2008/09 and £5.0m for the next five years.

The potential costs to the economy of the proposed fee changes are:

- Revenue loss from a decrease in the volume of applications as a result of fees changes for out-of-country applications (as above, revenue loss from in-country and extension applications are transfers).
Option 2: This is estimated at £3,200 for 2008/09 and £16,100 over the next five years.
Option 3: This is estimated at £2,300 for 2008/09 and £11,500 over the next five years.
- Output loss from a decrease in the numbers of migrants coming/remaining in the UK to work. The value of the expected salary that the migrant would have received for the duration of leave given is used to value the output loss.
Option 2: This is estimated at £3.1m for 2008/09 and £21.1m for the next five years.
Option 3: This is estimated at £1.4m for 2008/09 and £13.2m for the next five years.

So, under option 2, there is a potential net cost to the economy of £1.8m in 2008/09 and £13.2m for the next five years (present value). Under option 3, there is a smaller potential net cost to the economy of £0.4m in 2008/09 and £7.6m for the next five years (present value). Under both options, the value of output lost from those who decide to no longer apply exceeds the gain in revenue from overseas applications.

⁴ Source: HESA

Table 2: Summary results of cost-benefit analysis*

	OPTION 2		OPTION 3	
	08/09	08/09 –12/13	08/09	08/09-12/13
Benefits				
-Additional revenue raised from out-of-country applications through fee changes for those who continue to apply	1,375,100	6,875,300	1,001,200	5,006,100
Total benefits (PV)	1,375,100	6,425,800	1,001,200	4,678,800
Costs				
-Revenue loss from decrease in out-of-country applications as a result of fees changes	-3,200	-16,100	-2,300	-11,500
-Output loss from net decrease in migrants coming/remaining in the UK	-3,138,500	-21,078,400	-1,413,400	-13,222,700
Total costs (PV)	-3,141,700	-19,670,800	-1,415,700	-12,259,200
Net benefit (PV)	-1,766,700	-13,245,000	-414,500	-7,580,400

*Discount rate = 3.5%

If migrant volumes are similar to those for 06/07 for the routes on which the Highly Skilled tier is based, the Government is estimated to generate £41.6m in 08/09 under option 2, an additional £13.7m compared with the do nothing option. Under option 3, the revenue generated will be lower at £36.5 in 08/09, an additional £8.7m. Note that in option 1, revenue raised is below administrative costs estimated at £29.4m for 08/09⁵. For options 2 and 3, revenue raised are above administrative costs, meeting one of our key charging policy objectives. The income will be used to cross-subsidise other routes where we believe that there are concerns on maintaining the UK's international competitiveness of charging the full administrative costs of the service; and to contribute towards the £100m for enforcement and compliance (the end-to-end process).

Table 3: Estimated revenue position

	08/09	Total
Option 1	27,864,400	131,242,900
Option 2	41,586,900	192,747,500
<i>Difference compared with option 1</i>	13,722,500	61,504,600
Option 3	36,518,100	174,409,900
<i>Difference compared with option 1</i>	8,653,700	43,167,000

The preferred option is option 3. This option imposes lower costs on the economy and enables the Government to generate an additional £8.7m in the next financial year and £43.2m over the next five years meeting the stated charging policy aim of recovering the true end-to-end cost of the immigration system. Although option 2 also meets this aim and offers a more simplified charging model, it imposes larger costs on society. By charging the Post-Study Work sub-category the same fees as the other Highly Skilled sub-categories, it also fails to meet the policy aim of ensuring that those who benefit most from the service make a larger contribution.

6. Sensitivity analysis

The key unknown variable is wage elasticity of labour supply. A wage elasticity of greater than 0.5 i.e. where labour supply is more responsive to changes in (expected) wages, would increase the net cost to the economy. As noted in section 5.2, some empirical studies suggest wage elasticities as high as 1.1. This could result in 110 and 550 fewer applications for the preferred option in 08/09 and over the next five years respectively resulting in an increase in net costs to the economy of £2.1m and £22.3m respectively. For option 2, a wage elasticity of 1.1 could result in an increase in net costs to the economy of £5.5m in 08/09 and £36.9m over the next five years.

⁵ Note that this is an underestimate as it does not include total costs for UKVisas.

Some empirical studies suggest negative wage elasticity of supply indicating backward sloping or backward bending labour supply curve. For a higher wage, individuals can decrease labour supply and enjoy the same level of consumption⁶. So this implies, for a lower wage, individuals would increase labour supply. This is unlikely to be the case here, for a lower wage in the UK, migrants who are not already in the UK are more likely to just go to another country. So for the purposes of this Impact Assessment, a lower bound of zero is used for the elasticity of labour supply. For the preferred option, this gives an expected net benefit of £4.7m over the next five years from the gain in revenue from overseas applications (there is no output loss). For option 2, the expected net benefit is £6.4m over the same period.

⁶ So the income effect outweighs the substitution effect.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	No	No
Small Firms Impact Test	No	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No

Annexes

Table 1: Empirical studies of the wage elasticity of labour supply

Source	Estimate of wage elasticity of labour supply*	Measure
R. E Lucas and L. A. Rapping, "Real Wages, Employment and Inflation", <i>Journal of Political Economy</i> , 77 (1969).	Short run: 1.12 – 1.13 (95% significance) Long-run: -0.07 – 0.58	Change in real wages on labour supply using US data 1929-1965
Y. Chang and S. Kim, "On the aggregate labour supply", <i>Federal Reserve Bank of Richmond Economic Quarterly Volume 91/1 Winter 2005</i> .	1.0	Aggregate labour supply elasticity
L. Osberg and S. Phipps, "Labour Supply with Quantity Constraints: Estimates from a Large Sample of Canadian Workers", <i>Oxford Economic Papers, New Series, Vol. 45, No. 2. (Apr., 1993), pp. 269-291</i> .	Between +0.1 and -0.1	Wage elasticity of labour supply in the Canadian Labour Market
P. Bingley and G. Lanot, "The Incidence of Income Tax on Wages and Labour Supply", <i>National Centre for Register-based Research (NCRR), Version 5.002 31 October 2000</i>	-0.4	Elasticity of labour supply in the Danish Labour Market

*Note that the estimated wage elasticity of labour supply includes negative values indicating backward sloping or backward bending labour supply curve. This is due to the income effect outweighing the substitution effect. For a higher wage, individuals can decrease labour supply and enjoy the same level of consumption.

Table 2a: Estimated impact on volumes of Option 2

Highly Skilled sub-category	A Change in fee	B Annual expected wage	C Expected wage over leave entitlement (PV rounded to nearest 500)	D % change in expected wage (A/C)	E % change in volumes (D*elasticity of labour supply)
General: in-country	£115*	£40,000	£116,000	-0.10%	-0.05%
General: out-of-country	£70**	£40,000	£116,000	-0.06%	-0.03%
General: extensions	£400	£40,000	£78,500	-0.51%	-0.25%
Entrepreneurs & Investors: in-country	-	£40,000	£116,000	-	-
Entrepreneurs & Investors: out-of-country	£400	£40,000	£116,000	-0.34%	-0.17%
Entrepreneurs & Investors: extensions	-	£40,000	£78,500	-	-
Post-Study: in-country	£355	£17,715	£35,000	-1.02%	-0.51%
Post-Study: out-of-country	£400	£17,715	£35,000	-1.15%	-0.57%

Table 2b: Estimated impact on volumes of Option 3

Highly Skilled sub-category	A Change in fee	B Annual expected wage	C Expected wage over leave entitlement (PV rounded to nearest 500)	D % change in expected wage (A/C)	E % change in volumes (D*elasticity of labour supply)
General: in-country	£115*	£40,000	£116,000	-0.10%	-0.05%
General: out-of-country	£70**	£40,000	£116,000	-0.06%	-0.03%
General: extensions	£400	£40,000	£78,500	-0.51%	-0.25%
Entrepreneurs & Investors: in-country	-	£40,000	£116,000	-	-
Entrepreneurs & Investors: out-of-country	-	£40,000	£116,000	-	-
Entrepreneurs & Investors: extensions	-	£40,000	£78,500	-	-
Post-Study: in-country	£5	£17,715	£35,000	-0.01%	-0.01%
Post-Study: out-of-country	£5	£17,715	£35,000	-0.01%	-0.01%

*Currently there is a two-stage process for the route that the Highly Skilled General sub-category is based on (Highly Skilled Migrant Programme) (see paragraph 1.5). Applicants have to, firstly, make an application to the programme costing £400 for an approval letter. If they obtain an approval letter, applicants then apply for leave to remain costing a further £350. So the total cost is £400 if the application is rejected or £750 if the application is approved and the applicant goes onto stage two. The application approval rate is 67% (Dec 06 – Sep 07: total grants/initial applications). So the average current fee that applicants pay is £635 [weighted average: (400*0.33)+(750*0.67)].

**As above. The application fee is £400 and the cost of a visa is £200. The application approval rate is 65% (Dec 06 – Sep 07: total grants/initial applications). So the average current fee is £530 [weighted average (400*0.35)+(600*0.65)].

Table 3a: Option 2 – Full results of cost-benefit analysis*

	08/09	09/10	10/11	11/12	12/13	Total
Benefits						
-Revenue raised from out-of-country applications for those who continue to apply	1,375,100	1,375,100	1,375,100	1,375,100	1,375,100	6,875,300
Total benefits (PV)	1,375,100	1,328,600	1,283,600	1,240,200	1,198,300	6,425,800
Costs						
-Revenue loss from out-of-country for those who no longer apply	-3,200	-3,200	-3,200	-3,200	-3,200	-16,100
-Output loss from decrease in migrants coming/remaining in the UK	-3,138,500	-5,166,800	-4,257,700	-4,257,700	-4,257,700	-21,078,400
Total costs (PV)	-3,141,700	-4,995,200	-3,977,600	-3,843,100	-3,713,100	-19,670,800
Net benefit (PV)	-1,766,700	-3,666,600	-2,694,000	-2,602,900	-2,514,800	-13,245,000

Table 3b: Option 3 – Full results of cost-benefit analysis

	08/09	09/10	10/11	11/12	12/13	Total
Benefits						
-Revenue raised from out-of-country applications for those who continue to apply	1,001,200	1,001,200	1,001,200	1,001,200	1,001,200	5,006,100
Total benefits (PV)	1,001,200	967,400	934,600	903,000	872,500	4,678,800
Costs						
-Revenue loss from out-of-country for those who no longer apply	-2,300	-2,300	-2,300	-2,300	-2,300	-11,500
-Output loss from net decrease in migrants coming/remaining in the UK	-1,413,400	-2,811,200	-2,999,400	-2,999,400	-2,999,400	-13,222,700
Total costs (PV)	-1,415,700	-2,718,300	-2,802,100	-2,707,300	-2,615,800	-12,259,200
Net benefit (PV)	-414,500	-1,750,900	-1,867,400	-1,804,300	-1,743,300	-7,580,400

*Discount rate = 3.5%