SLAUGHTER AND MAY

Pensions and Employment: Employment/Employee Benefits Bulletin

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Legal and regulatory developments in Employment/Employee Benefits

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For more information, or if you have a query in relation to any of the above items, please contact the person with whom your normally deal at Slaughter and May or Clare Fletcher

New law

STOP PRESS: European Union (Withdrawal) Bill published

The European Union (Withdrawal) Bill was published on 13th July and laid before Parliament, along with explanatory notes, and a workers'rights factsheet. The Bill (previously known as the Great Repeal Bill, and latterly the Repeal Bill) provides as expected for the repeal of the European Communities Act 1972 (ECA). It also:

- converts directly applicable EU law (e.g. EU regulations) into UK law;
- preserves all the laws which have been made in the UK to implement EU obligations (e.g. in EU directives);
- incorporates any other rights which are available in domestic law by virtue of section 2(1) of the ECA, including the rights contained in the EU treaties, that can currently be relied on directly in national law without the need for specific implementing measures; and
- provides that pre-exit case law of the Court of Justice of the European Union (CJEU) be given the same binding, or precedent, status in UK courts as decisions of the Supreme Court.

The Bill is not expected to be debated in Parliament until the Autumn. We will track the progress of the Bill and report further on key developments as they arise.

Good work: the Taylor review of modern working practices

The Taylor Review of Modern Working Practices published its final findings and recommendations on 11th July. The Report, Good work: the Taylor review of modern working practices, makes suggestions for amending and clarifying the law governing employment status, as well as some far-reaching proposals on the scope of various employment protections.

Whilst much of the media coverage has focused on the implications of the 115-page Report for employment status and the gig economy, the Report could in fact have significant implications for all employers, if its recommendations are taken forward.

The key recommendations of the Report, in terms of changes to employment law, are set out below.

Employment status: The Report recommends:

- retaining the current three-tier approach to employment status (employee, worker and self-employed)
- enshrining the key criteria that define 'employee' status in primary legislation, with the detail governed by secondary legislation and guidance that can be updated quickly as required;
- changing the definition of 'worker' so that the obligation to provide personal service is no longer critical. Instead, the Report recommends that the principle of 'control' should be of greater importance, with legislation outlining what this means in a modern labour market and not simply in terms of the supervision of day-to-day activities; and
- introducing the term 'dependent contractor' to refer to those who are 'workers' but not 'employees'.

Interplay with tax: the Report suggests that the definition of 'self-employment' for employment law and tax purposes should be aligned, so that being 'employed' for tax purposes would mean that an individual is either an employee or a dependent contractor. It also calls on the Government to consider how tax tribunal and employment tribunal rulings could be applied across jurisdictions – for example, where a tax tribunal determines that an individual is an 'employee' for tax purposes, that decision could be binding for employment law purposes.

Written statements: the Report recommends that the right to a written statement of employment terms should be extended to 'dependent contractors'. The statement should also include a description of statutory rights, and should be given on day one of employment. There should be a stand-alone right to compensation for failure to provide a written statement (rather than the current two to four weeks' pay which can only be added on to a separate claim).

Pay: as expected, the Report recommends that the Government should ask the Low Pay Commission to advise on the impact of bringing in a higher National Minimum Wage (NMW) for hours which are not guaranteed in a contract. It also recommends changes to the NMW rules for individuals working via platforms such as Uber, to clarify what will be considered "working time", and to allow individuals to be paid based on their output (i.e. number of tasks performed) provided that an average individual successfully clears the NMW with a 20% margin of error.

Holiday and sick pay: the Report suggests that individuals should have the choice to be paid 'rolled-up' holiday pay instead of paid time off. The Report also suggests that increasing the holiday pay reference period from 12 to 52 weeks would improve access to holiday pay for seasonal, casual and zero-hours workers. The Report advocates reforming statutory sick pay (SSP), so that it becomes a basic employment right, comparable with the NMW, which should accrue on length of service (so that employers do not have to give the full six months of SSP to individuals who have only worked for them for a short time).

Agency workers and zero hours contracts: the Report recommends that agency workers should have the right to request a direct contract of employment after 12 months with the same hirer, which the hirer would be obliged to consider reasonably. Similarly, zero-hours workers should be entitled to request a guaranteed hours contract (to better reflect actual hours worked) after 12 months. The Report also calls for the repeal of the 'Swedish derogation' in the Agency Workers Regulations 2010, under which agency workers who have a contract that provides for a minimum level of pay between assignments are excluded from the right to equal pay with permanent employees.

Enforcement and Tribunal claims: the Report suggests that individuals should be able to have their employment status determined by a tribunal without having to pay a fee. Furthermore, the burden of proof in cases where employment status is in dispute should be placed on the employer, which will have to prove that the claimant is not entitled to the employment rights claimed (and will then face further penalties if they do not follow a ruling in the claimant's favour).

Other: the Report makes a number of other recommendations, including that:

- all employers should report on their workforce structures, with larger employers also being required to report on the number of requests received from zero-hours workers for guaranteed hours and agency workers for permanent positions;
- the Information and Consultation of Employees Regulations 2004 should be extended, so that an employer will be obliged to enter into negotiations about establishing workplace representatives when 2% of employees and 'dependent contractors' request it, rather the current 10% (of employees only);
- continuity of employment should be preserved where any gap in employment is less than one month, rather than one week;
- the Government should consider allowing flexible working requests to cover temporary as well as permanent changes to contracts; and
- individuals should have a right to return to work following long-term sickness absence, similar to the right which applies after maternity leave.

Implications: Although the Report recommends some quite significant changes, it is not yet clear whether (or when) these may be taken forward into law. A number of the recommendations touch on sensitive political issues, such as tribunal fees and the Agency Workers Regulations (which many within the Conservative party would prefer to repeal than extend).

Beyond the gig economy: Many of the Report's recommendations, while aimed at the gig economy, will have ramifications outside it. The Report suggests that its proposal to place greater emphasis on control and less emphasis on personal service will result in more people being protected by employment law. This may be true within the gig economy, but the opposite may be true at the other end of the spectrum, where fewer senior contractors and non-executive directors, for example, may benefit from "worker" status. This would be consistent with the re-branding to "dependent contractor".

Impact of Brexit: European law permeates the areas covered by the Report, which means that Brexit will influence how and when its recommendations may be implemented. For instance, workers may already have the right to a written statement of employment terms under EU law (the IWGB is currently claiming just that in proceedings against Citysprint). Conversely, EU law currently prohibits rolled-up holiday pay.

Next steps: The government intends to engage with stakeholders across the country before producing a full response later this year. We will report further once the position becomes clearer. In the meantime, if you have any queries please speak to your usual Slaughter and May contact.

Cases Round-up

Discrimination and backdating pension rights

The Supreme Court has given judgment in two cases which will have implications in terms of pension benefits for civil partners, same-sex spouses and part-time workers.

Walker: The first case (*Walker v Innospec*) concerned a retired employee (W), who retired in 2003, entered into a civil partnership in 2006, and subsequently married his civil partner. His employer (I) denied that it would have to pay a full spouse's pension to his husband, on the basis that it could discount any period of service prior to the Civil Partnership Act 2004 coming into force on 5th December 2005. This is currently permitted under paragraph 18 of Schedule 9 to the Equality Act 2010. The effect was that W's husband would only be entitled to a pension of around £1,000 per annum (the statutory guaranteed minimum), as opposed to the full £45,700 per annum.

Decision: The Supreme Court has now allowed W's appeal, meaning that his husband will be entitled to a full spouse's pension based on all the years of W's pensionable service with I. The Court relied on CJEU case law which has established that, unless there would be unacceptable economic or social consequences of giving effect to W's entitlement to a survivor's pension for his husband, at the time that this pension would fall due, there is no reason that he should be subjected to unequal treatment as to the payment of that pension. The Court therefore ruled that the offending provision of the Equality Act 2010 must be disapplied.

O'Brien: The second case (*O'Brien v Ministry of Justice*) concerned a retired part-time fee-paid judge (O) who sought entitlement to a pension on terms equivalent to a comparable full-time judge. The issue arose as to whether, in calculating the amount of his pension, account should be taken of the whole of his service from the beginning of his appointment in 1978 to his retirement in 2005 (a period of 27 years), or only his service since 7th April 2000, the deadline for transposing the Part-Time Workers Directive (a period of less than five years).

Reference: In this instance the Supreme Court felt that the law is not sufficiently clear. While it was inclined to think that the Directive applies where the pension falls due for payment after the Directive has entered into force (which would favour O's claim), it decided to ask the CJEU to clarify whether periods of service prior to the deadline for transposing the Directive should be taken into account when calculating the amount of pension for a part-time worker.

Relevance for employers: the *Walker* decision may have significant implications for some occupational pension schemes, however many schemes do already recognise full service for spouses and civil partners. The Government estimated in 2014 that the cost of equalising pension schemes and backdating pay-outs for same-sex couples could be as much as £3 billion for public sector schemes (although for private sector schemes the cost was estimated at under 0.5 billion). We will report further once the CJEU gives its judgment in *O'Brien*.

For further analysis of the implications of the Supreme Court's judgments, see this week's Pensions Bulletin.

Whistleblowing: what is in the "public interest"?

Since 2013, whistleblowers have been required to show that they have a reasonable belief that their disclosure is "in the public interest". The Court of Appeal has now given guidance on this requirement, which it found was met in a claim by an employee whose disclosure concerned alleged financial irregularities affecting the bonuses of around 100 senior managers, including himself (*Chesterton Global Ltd v Nurmohamed*).

Disclosure: N was employed as a director in charge of the sales department of CG's Mayfair office. He made a number of allegations to his managers that there were inaccuracies in CG's statements of profit and loss. He alleged that the deliberate misstatement of £2 to £3 million of actual costs and liabilities (to the benefit of shareholders) adversely affected the bonuses of over 100 senior managers, including his own. N was later dismissed and he claimed detrimental treatment and automatically unfair dismissal for having made a protected disclosure. The Tribunal and the EAT both upheld N's claim.

Reasonable belief: The Court of Appeal dismissed CG's appeal. It held that the tribunal must determine whether the worker believed, at the time of making it, that the disclosure was in the public interest. If so, it then had to go on to ask whether that belief was reasonable. The Court of Appeal recognised that there could be more than one reasonable view as to whether a particular disclosure was in the public interest. Further, the particular reasons why the worker believed the disclosure to be in the public interest were not of relevant. The belief is subjective; its reasonableness is objective. The Court also confirmed that, while the worker must have a genuine belief that the disclosure was in the public interest, that did not have to be the predominant motive in making it.

Public v personal: The Court went on to find that whether disclosure was in the public interest depended on the character of the interest served by it, rather than simply on the number of people sharing that interest. The correct approach was that, where the disclosure related to a breach of the worker's own contract of employment, or some other matter where the interest was personal in character, there might nevertheless be features of the case that made it reasonable to regard disclosure as being in the public interest as well as in the personal interest of the worker, if a sufficiently large number of other employees share the same interest.

Relevant factors: The Court found that the tribunal must consider all the circumstances of the particular case, but in particular that it could be useful to consider:

- the number in the group whose interests the disclosure served (the larger the number, the more likely the disclosure is to be in the public interest);
- the nature of the interests affected (the more important they are, the more likely the disclosure is to be in the public interest);
- the extent to which those interests are affected by the wrongdoing disclosed (the more serious the effect, the more likely the disclosure is to be in the public interest);
- the nature of the wrongdoing disclosed (the disclosure of deliberate wrongdoing is more likely to be in the public interest than the disclosure of inadvertent wrongdoing); and
- the identity of the alleged wrongdoer (the larger and more prominent the alleged wrongdoer (in terms of the size of its relevant community, ie staff, suppliers and clients), the more likely the disclosure is to be in the public interest).

On the facts… Turning to the present case, the Court was satisfied that the public interest requirement was met. The disclosure had been of what was said to be deliberate wrongdoing in the form of misstatements of between £2 million and £3 million. The Court commented that if the accounts were the statutory accounts, even of a private company, the disclosure would unquestionably be in the public interest. The fact that in this case the accounts had only been internal made the position less clear, but the Court noted that the internal accounts fed into statutory accounts,

and that CG was a very substantial and prominent business. The Court therefore upheld the Tribunal's decision.

Size matters: This case has provided some useful guidance on the public interest requirement, which is likely to be a significant battleground in most whistleblowing claims. Although it is not simply a matter of how many people are affected, this will be a relevant factor. It also seems that employees of larger, more high-profile companies may find it easier to overcome the public interest hurdle than employees of smaller companies (all other matters being equal). Larger companies should bear this in mind when handling protected disclosures.

Age discrimination: Justifying caps in enhanced redundancy schemes for those with pension rights

It is not uncommon for an employer with an enhanced redundancy scheme to include a taper and/or a cap which restricts payments to employees who are (or soon will be) eligible for pension benefits. Although this amounts to prima facie age discrimination, can it be justified? This was the issue before the EAT in a recent case, which gave guidance on justification in these circumstances (*BAE Systems (Operations) Limited v McDowell*).

Taper and cap: BAE operated an enhanced redundancy scheme, which applied a taper to reduce payments from the age of 63.5, and a cap such that payments were not available from the age of 65 (originally the normal retirement age under BAE's pension scheme, when employees would have an immediate entitlement to an occupational pension). The idea was that employees would not receive more in redundancy pay than they would have earned in basic salary if they had worked until their normal retirement age of 65.

Review: The enhanced redundancy scheme operated within BAE's Severance Framework, which had been introduced in 2001 to provide a consistent framework following a merger with another company. The scheme was reviewed again in 2011 when the default retirement age was abolished. BAE nonetheless decided to retain the cap at age 65, even for employees who were not part of its pension scheme or who were members of the new Defined Contribution scheme, in which there was no applicable retirement age.

Redundancy and claim: M was made redundant in January 2015 at age 65, and received no payment under the redundancy scheme (other than statutory redundancy pay). M had intended to continue working until August 2016, some 19 months after his pension retirement age. M complained of direct age discrimination. BAE accepted that the cap was prima facie discriminatory, but argued it was a proportionate means of achieving the legitimate aims of its Severance Framework. It relied on various legitimate aims, including preventing a 'windfall' for employees who are (or soon will be) eligible for pension benefits, and ensuring that "finite funds" were allocated in an effective and equitable way. The Tribunal rejected BAE's arguments and upheld M's claim.

No "windfall": The EAT allowed BAE's appeal in part. It confirmed that this was not a pure "windfall" case (where without the taper/cap the redundancy compensation would exceed any possible loss of earnings), since following the abolition of the default retirement age, there was no longer a clear point at which an employee must retire. In this case, BAE had adduced no evidence or statistics (whether within its own workforce or more generally) to demonstrate that, despite the removal of the default retirement age, people tended to continue to retire and draw their pension at age 65. M was in a more nuanced position; although he had an immediate entitlement to pension benefits at 65, he would also have been able to continue working (but for the redundancy), and would thus suffer a loss of earnings.

Pension benefits are highly relevant: The EAT confirmed that in cases such as this, a taper and a cap might still be "*readily justified…the fact that an employee is entitled to immediate pension benefits will always be a highly relevant factor*" – but that would depend on the nature of both the pension and redundancy schemes in question. The tribunal would need to ask whether the exclusion of the employee from the severance payments scheme achieves a legitimate objective and is proportional to any disadvantage he suffers.

Holistic approach: However, it was at this stage that the Tribunal erred. BAE's case was that the legitimate aims of the Severance Framework

had to be viewed as a whole; the taper and cap were integral to the overall scheme and it did not seek to justify those elements separately. Nonetheless, the Tribunal had gone on to test the cap against each aim individually. It had failed to adopt a holistic approach. The EAT therefore overturned the Tribunal's findings and remitted the claim for rehearing.

Lessons for employers: This case confirms that entitlement to an immediate pension will be highly relevant in justifying a cap on redundancy pay. However, an employer seeking to use a cap should be prepared to adduce evidence of normal retirement ages within its workforce, which should align with the age at which the cap applies. Similarly, employers who seek to rely on a finite budget for a redundancy process must be prepared to adduce evidence of that budget (BAE had failed to do so here, and in fact, M was told during the redundancy process that there was no fixed budget, which damaged BAE's defence).

Supreme Court: Rangers EBT payments were "earnings"

The Supreme Court has ruled in favour of HMRC in its long-running dispute with Rangers Football Club over the club's use of Employee Benefit Trusts (EBTs) (*RFC 2012 Plc (in liquidation) (formerly The Rangers Football Club Plc) (Appellant) v Advocate General for Scotland (Respondent) (Scotland)*).

The Supreme Court held that approximately £47m in payments made to players and other employees using EBTs were not "loans", but were in consideration of services by the employees, and thus had been "earned" by the employees. Therefore, the scheme amounted to "a mere redirection of earnings" which did not remove the liability of employees to income tax. The relevant employing entity should therefore have operated PAYE and accounted for NICs on the payments to the EBT.

Redirected earnings: Although the disguised remuneration rules have altered the tax position on payments into EBTs since the facts of this case arose, the Court's comments are nonetheless useful from a general perspective when assessing whether sums amount to "earnings" for tax purposes – particularly where sums are paid to a third party rather than the employee directly.

Wider implications? It remains to be seen whether HMRC will seek to extend their successful arguments in this case to other situations where there is arguably redirection – e.g. to re-examine treatment of salary sacrifice arrangements and/or deferred bonus arrangements where the employee has some choice about the deferral (although in deferred bonus arrangements there is at least full income tax on ultimate receipt, which may therefore be seen as less objectionable by HMRC).

Points in practice

Government policy paper on EU nationals living in the UK

The Government has published a new policy paper, "The United Kingdom's exit from the European Union: safeguarding the position of EU citizens living in the UK and UK nationals living in the EU". The paper sets out a number of principles which the Government undertakes to apply to EU citizens living in the UK after Brexit (in the expectation of reciprocal arrangements for UK nationals resident in the EU). The key points are as follows:

- Qualifying EU citizens will be granted indefinite leave to remain (settlement) under existing rules. They would be free to live in the UK in any capacity and undertake any lawful activity, to access public funds and services and to apply for British citizenship. To "qualify", they must have been resident in the UK before a specified date and have five years' continuous residence in the UK. The "specified date" is to be agreed, but will be no earlier than the 29 March 2017 (the date Article 50 was triggered) and no later than the date the UK leaves the EU.
- Qualifying EU citizens resident in the UK before the exit will be able to apply for residence status under a new scheme.
- EU citizens who became resident before the specified date but do not have five years' continuous residence at the time of the UK's exit will be able to apply for temporary leave to remain in the UK until they have five years residence, when

they will be eligible to apply for settlement.

- EU citizens who arrived in the UK after the specified date will be able to remain in the UK for a period and may become eligible to settle permanently, depending on their circumstances, but are not guaranteed settled status.

- Family dependants who join a qualifying EU citizen in the UK before the UK's exit will be able to apply for settlement after five years, irrespective of when they arrived. Those joining after exit will be treated in the same way as those joining British citizens.

- EU citizens with settled status will have access to UK rights and benefits on the same basis as comparable UK nationals under domestic law.

- EU citizens that do not meet the qualifying criteria but who remain legally in the UK on a pathway to settled status will have access to the same rights and benefits that they can access now (broadly, equal access for workers and the self-employed and limited access for those not working).

- EU citizens do not need to apply now for settlement or documentation to prove they are currently exercising Treaty rights or have permanent residence in order to secure their status following the UK's exit.

The Government has said that it will publish proposals on how EU migration will work for new arrivals post-Brexit at a later date.

If you would like further information on these issues or to discuss their impact on your business, please speak to your usual Slaughter and May contact.

If you would like to find out more about our Pensions and Employment Group or require advice on a pensions, employment or employee benefits matters, please contact Jonathan Fenn or your usual Slaughter and May adviser.

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