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Employment Legal Alert

Enhanced Redundancy Payments – The New Risks

Introduction

Given the recent spate of economic news it is not surprising that reports of redundancies are increasing and set to rise further. At a time when employers could be forgiven for hoping that collective redundancies would be relatively clear-cut, a significant new risk has become apparent. Three recent cases have considered age discrimination claims in respect of enhanced redundancy schemes. Every employer needs to review its enhanced redundancy scheme, whether it is contractual or discretionary. Failure to do this could result in the redundancy payments being vastly higher than predicted by the employer.

Background

The legislation prohibits direct or indirect discrimination against an individual on the grounds of age. Both forms of discrimination can be justified. The employer must demonstrate that the discriminatory measures are for a legitimate business aim and that the discrimination is a proportionate way of achieving that business aim. UK legislation acknowledges that length of service is often used as a way of calculating benefits for employees during employment, but provides no general exemption for payment on termination.

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There is a specific exemption for any redundancy scheme which operates as an enhancement to the statutory scheme. The precise ambit of this exception is unclear. However, we consider that the employer must follow the statutory scheme in all respects other than the size of the payments or the multiplier used. This is often unpopular, given that the statutory scheme continues to differentiate between employees aged 18 to 21, 22-40 and 41 and above, and may not match the employer's objectives.

Recent cases

The concerns facing employers have been brought into sharp focus by three cases which have been reported in the last two months. In one, the Employment Tribunal found that the scheme was not justified and therefore upheld the claim against the employer *(Galt v National Starch and Chemical)*. In the other two cases, BAE and ICI, both the Employment Tribunals upheld the employer's contention that the schemes were justified, but the Employment Appeal Tribunal overruled them. In both cases, the EAT decided that the Tribunal had not asked itself whether the scheme was a proportionate means of achieving the aims of the employer. We understand, that there are a significant number of similar cases in the wings. It therefore appears that employee advisers are realising at the same time that age discrimination could well be a way of pushing up the size of redundancy payments.

What should employers do?

Certain lessons are now clear from the cases which have come through. Any employer who might want to make enhanced redundancy payments in the next 12 to 18 months needs to review its redundancy scheme urgently and start planning now, how it will meet any challenges to that scheme.

First, it is clear that enhanced redundancy schemes will tend to be discriminatory. Almost all schemes will rely on age and/or length of service to some extent, in calculating the level of the enhanced payments. This is scarcely surprising given that UK's statutory redundancy scheme does so too. However, it does mean that an employer will need to justify its scheme (unless it mirrors the statutory scheme) and provide evidence to back up assertions as to the objective of the enhancements.

It is suggested that the following questions should be asked by every employer with any form of enhanced redundancy scheme, who may need to make redundancies in the current climate.

1. *Does the scheme match the statutory scheme?*

   This is the strongest possible situation for an employer. The scheme must mirror the statutory scheme save for the level of the payments.

2. *Is the scheme contractual or discretionary?*

   If it is genuinely discretionary, then the good news is that the employer can probably change past practice unilaterally and come up with a scheme which is capable of being justified (see below). If the scheme is contractual then the employer needs to consider urgently, whether to negotiate, to amend the scheme or, indeed, to remove the scheme by revising terms and conditions. Clearly, this is a big step but in view of the potential consequences of a finding of age discrimination (see below) an employer should consider it. Importantly, if the employer tries to remove redundancy terms once a redundancy situation is envisaged, this will almost certainly be too late to be effective. If there is a pre-existing redundancy situation then an employer probably cannot remove redundancy terms, even by giving notice of termination under the contract.

3. *Is there any evidence as to the aims of the redundancy scheme when it was first introduced?*

   In the BAE case, the scheme had been introduced 30 years ago. The employers were allowed to give evidence to indicate why it was being kept, now. However, evidence (if available) of an employer's intentions when a scheme was introduced will be relevant.

4. *What is the legitimate aim of the enhancement?*

   The cases so far have identified a number of potential justifications. Schemes may be said to reward loyalty. One scheme which paid out enhanced sum to older employees was said to encourage older staff to take voluntary redundancy, enabling younger staff to progress through the ranks. If older staff receive larger payments (as is usually the case), it may be a legitimate objective for an employer to give protection to those older staff because they are more vulnerable in the job market.

5. *What is the evidence of the redundancy scheme achieving the employer's objectives?*

   In the absence of evidence that the scheme has the desired effect or can reasonably be expected to have the desired effect, it is difficult to see how a Tribunal would consider that the redundancy scheme was proportionate, notwithstanding its discriminatory impact. The employer needs to think carefully how to obtain such evidence. For example, if it rewards loyalty what is the evidence that staff take this into account in deciding to remain with the company? If it is said to protect older staff because they are more vulnerable in the job market, what is the evidence for the vulnerability in the job market? Evidence may come from staff surveys, market practice in a particular industry, or indeed anecdotal evidence from staff. It is in general, in this area, that employers are going to have to be most creative if they wish to have any scheme that departs from a straight enhancement of the statutory scheme.

6. *Would alternative schemes achieve the same outcome with a less discriminatory impact?*

   An employer should look at alternative ways of enhancing redundancy schemes. A Tribunal will not necessarily expect an employer, when designing a revised enhanced scheme, to increase its costs significantly. The question is whether a fairer system can be devised without dramatically increasing the overall cost to the employer. In the ICI case, for example, there was a considerable disparity between the redundancy payments made to staff aged less than 40 and staff aged 50.

7. *Does the redundancy scheme have tapering provisions?*

   The Court has considered the issue of tapering provisions in the ICI and BAE cases. The EAT accepted that it would be a legitimate factor to take into account, if the individual was going to retire or be able to receive a non-discounted pension in the foreseeable future. It is legitimate to avoid a situation where an employee made redundant shortly before retirement receives a windfall. However, if the enhanced redundancy scheme has been in practice for some time, the pension rules or retirement ages may have changed. Accordingly, in the ICI case the tapering provisions were no longer closely tied into retirement or pension ages. The tapering provision in the BAE case is being challenged. Accordingly, an employer can legitimately design a scheme which avoids paying out a windfall to an employee close to retirement or pension retirement age, but the employer needs to ensure that tapering provisions are proportionate.

8. *Was the redundancy scheme negotiated with a staff council or trade union?*

   The EAT was very clear in the BAE case that it may be helpful for the employer if the scheme has been negotiated with a trade union or works council or otherwise has the full support of the workforce. However, it does not amount to an automatic justification. It is still necessary to consider whether the scheme has a proportion means of achieving a legitimate aim.

9. *Does the scheme have age bands?*

   Taking into account age in calculating redundancy payments amounts to direct age discrimination. One of the issues in the Heyday case, currently in the European Court, is whether there is any difference between direct and indirect discrimination and the standards required to show that a particular measure is justified. At the moment it looks as if the European Court will not set a different formal test. However, in our view the essence of a proportionality test is to consider the discriminatory impact against the legitimate aim. Consequently, a directly discriminatory provision will be harder to justify.

10. *Does the scheme apply to voluntary redundancies?*

The Claimant in the BAE schemes case was a volunteer for redundancy. This did not prevent the employee having a claim for the alleged discriminatory impact of the redundancy terms. In other words it is of no relevance that an individual has volunteered for redundancy rather than being made compulsorily redundant.

Consequences of age discrimination

The consequences of a finding of unlawful discrimination may vary. The individual discriminated against is entitled to level up his or her benefits. If a tapering provision is found to be discriminatory on the grounds of age, it will be disapplied and the employee will receive the full untapered redundancy payment. However, it is more difficult to see what a Tribunal would do if a scheme is found to be discriminatory because it was not proportionate. For example, if the Tribunal found that the scheme was unduly generous to older employees, younger employees are entitled to level up their redundancy payments. So, the starting point is that individuals are entitled to calculate their redundancy payments on the most generous formula. This could be very expensive for an employer who had calculated redundancy sums on the basis of lower exposure.

In the *National Starch* case the Tribunal took a different approach. The employee received three weeks pay for each year of service but an older employee received four weeks pay. The Tribunal found that the difference was discriminatory and awarded 3.5 weeks pay per year of service. There was some evidence that this compromise would have been reached had the parties appreciated the impact of the age discrimination legislation. This was the agreement, which had been reached elsewhere in the organisation, where the question had been raised. This was an unusual set of facts and, in our view, the starting point will be for the disadvantaged employee to receive a payment calculated on the more normal favourable enhanced basis.

Options for employers

For contractual schemes:

- Establish whether or not the scheme is likely to be capable of being justified.
- If it cannot be justified consider altering terms and conditions of employment now, before a redundancy situation arises.

If the scheme is not contractual:

- Consider mirroring the statutory scheme, with enhanced payments. In our view, this is going to become an increasingly common approach.
- Consider having a flat rate payment (e.g. one month per year of service) regardless of age. The scheme will indirectly discriminate on the grounds of age. However, given that Tribunals have shown themselves willing to accept that older employees are likely to find it harder in the job market, this way, is an easier scheme to justify than one which has a combination of age factors (direct discrimination) and length of service in it.

- Where the redundancy payments are generous secure all severance payments with a compromise agreement. That way, even if a test case does succeed, the retrospective effect will be limited. Clearly, the worst case scenario would be for employees made redundant in earlier waves to bring claims.
- If the employer is sticking with its current scheme, consider how best to gather evidence to be used, if there is a challenge. Consider whether a working party could be set up to review the issue now, so that the employer can show it had considered matters before a challenge, rather than trying to recreate matters retrospectively, after a challenge has arisen.

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