TUPE, service provision change and second generation outsourcing: is a change (of client) better than a rest?

The recent Court of Appeal decision in the case of McCarrick v Hunter [2012] EWCA Civ 1399 has confirmed that the service provision change rules under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (“TUPE”) will only apply on a second generation outsourcing where the activities carried out before and after the change of contractor are carried out on behalf of the same client. However, despite this decision, there is a potential route by which TUPE could still apply in situations such as this.

The decision will be highly relevant to businesses where the engagement of contractors is widespread and those involved in second generation outsourcing deals, particularly in commercial property transactions where the owner or management company of a building changes at the same time as a facilities provider.

The facts

Mr McCarrick was dismissed in March 2010 and subsequently brought an unfair dismissal claim against his employer, Mr Hunter. Before considering the merits of his claim, the Tribunal had to decide whether Mr McCarrick had sufficient length of service to bring such a claim. The answer to that question depended on whether, when Mr McCarrick became employed by Mr Hunter, it was by way of a transfer of undertaking or a service provision change under TUPE.

Mr McCarrick started work for Waterbridge Group Limited (“WGL”) in November 2005 and was employed by WGL to manage its property portfolio. In February 2009, WGL appointed WCP Management Limited (“WCP”) to carry out property management services on the portfolio on WGL’s behalf. As a result of this change, Mr McCarrick became employed by WCP. However, in August 2009, the situation changed again as the mortgagee of the property portfolio (“Aviva”) appointed receivers to take control of the properties.

A new property management company (“King Sturge”) was also appointed to manage the properties instead of WCP. As a result, property management services ceased to be carried out by WCP on WGL’s behalf and were instead carried out by King Sturge on Aviva’s behalf. Following the August 2009 developments, Mr Hunter (who had an interest in the properties) employed Mr McCarrick to assist King Sturge in managing the properties. When he was dismissed seven months later however, Mr McCarrick brought an unfair dismissal claim against Mr Hunter.

The Employment Tribunal decided that both the February 2009 and the August 2009 transfers were service provision changes under TUPE and so Mr McCarrick had sufficient service to bring an unfair dismissal claim against Mr Hunter. However, Mr Hunter appealed in respect of the August 2009 transfer on the grounds that to be a service provision change the same activities needed to be carried out for the same client by different contractors. If Mr Hunter was right and TUPE did not apply, Mr McCarrick would not have sufficient service to bring his unfair dismissal claim as without the transfer he only had seven months service with Mr Hunter. The EAT agreed with Mr Hunter. Mr McCarrick appealed to the Court of Appeal.

The Court of Appeal decision

The Court of Appeal agreed with the EAT. In its view, the service provision change rules under TUPE require that the activities carried out by different contractors before and after the transfer, have to be for the same client. As there was a change of client (from WGL to Aviva) when the services were outsourced to a new contractor (from WCP to King Sturge) in August 2009, the service provision change test was not met. Given this, TUPE did not apply to preserve Mr McCarrick’s continuity of service and he could not bring his unfair dismissal claim.
Impact

This case is helpful as it confirms that there will be no service provision change for the purposes of second-generation outsourcing where the activities carried out by different contractors before and after the change are not for the same client.

It is quite common to find that property management services may be changed from one service provider to another when ownership or management of a commercial property changes. However, the case applies equally outside the property management area, and we think it is likely that parties, looking to avoid the application of TUPE, may choose to make a number of changes at the same time to take advantage of this case. Although the EAT had previously given its opinion that the client needed to remain the same, and only the service provider could change in order for service provision changes to be made, it is very useful that this has now been confirmed, in such clear cut terms, by the Court of Appeal.

However, it is very important for parties to bear in mind that there are two entirely separate ways in which to argue that there has been a TUPE transfer. The most common one, at the moment, is to argue that there has been a service provision change. This is because the rules on service provision change were brought in to try to clarify the law relating to TUPE and to avoid the need for significant legal debate in relation to service transfers. However, the original TUPE rules (which still apply) may apply even if the rules around service provision change do not. The original TUPE rules state that there will be a TUPE transfer if there is a transfer of a business or part of a business which retains its identity after the transfer. On that basis, in the McCarrick case, TUPE may still have applied if the case had been decided under the original TUPE test. The fact that a change of client (from WGL to Avia) took place at the same time as services were outsourced to a new contractor (from WCP to King Sturge) would not have prevented the original TUPE test from applying.

Ultimately, therefore, the impact of this case is that parties looking to argue that TUPE applies, will rely on both TUPE tests (i.e. the original “business transfer” test and the service provision change test) and it will be unwise to assume that there is no risk of TUPE applying merely because there are two changes occurring at the same time.

Recommendations

If parties are looking to avoid TUPE applying, then it may be possible to bundle together several changes, so that the service provision change rules do not apply, because there is a change of client at the same time as a change of service provider. Intra-company transfers and internal re-organisations may be another area where this case is particularly helpful.

However, it is going to be necessary to take a realistic view of the risk of a challenge coming in, pursuant to the original TUPE rules and to make provision for TUPE risk in any documentation, given that the original TUPE rules may apply.

This is unlikely to be the last word on the service provision change rules in the coming months. Whilst this case does bring some helpful clarity on one particular aspect of the rules, there have been a number of criticisms levelled at the concept of service provision change since its introduction in 2006. Many commentators believe that the rules create too much uncertainty for those working with them in practice. As a result of this feedback, the Government has recently announced that it will consult in due course on whether to retain or repeal the law relating to service provision change. As such, for those working with the service provision change rules (whether in the commercial property context or otherwise) it is a case of watch this space.

If you have any questions, please contact:

Nicholas Robertson
Head of London Employment Group
T: +44 20 3130 3919
E: nrobertson@mayerbrown.com

Miriam Bruce
Senior Associate
T: +44 20 3130 3695
E: mbruce@mayerbrown.com