GIBSON DUNN

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UK EMPLOYMENT -- KEY DEVELOPMENTS FOR 2011

To Our Clients and Friends:

In this client alert we identify key developments in UK employment law expected in the coming year and highlight those steps which employers should be taking to prepare their UK businesses for these developments.

A headline summary is provided below. A more detailed explanation and analysis is available by clicking on the appropriate link. For further details or for assistance on any UK Employment or Labour law matter, please contact James Cox or Daniel Pollard in Gibson Dunn's London office.

- **UK Employment Law Reform**. The coalition Government has recently announced a series of reforms to the Employment Tribunal system which will make it more difficult for employees to pursue unmeritorious claims and which are designed to simulate the creation of new jobs. The changes are, on the whole, to be welcomed and will ensure that the UK retains its reputation as being one of the more flexible European labour markets. Click here for details.

- **Financial Services Pay**. On 1 January 2011, the Financial Services Authority's revised Remuneration Code came into force and applies to approximately 2,500 FSA registered firms. Controversially the Code has extra territorial scope and not only applies to subsidiaries and branches of overseas firms doing business in the UK but also to subsidiaries of UK headquartered groups or sub-groups worldwide. Click here for details.

- **Bribery Act Compliance Procedures**. The UK Bribery Act 2010 is expected to come into force in coming months. The legislation was expected to come into force in April 2011 but the Justice Minister has today announced that the implementation will be delayed pending a last minute ministerial review. The current version of the Act would impact not just UK companies but any organisation that carries on a business in the UK. The Act would criminalise corruption of public officials and private parties, regardless of where the bribe is paid or received. Corporations potentially faced strict criminal liability for the acts of persons associated with them, the only defence being that the company has "adequate procedures" in place for tackling bribery. Even if they do not pay bribes themselves, senior officers may face personal liability for consenting to or conniving in the organisation's violative acts. All organisations with UK operations need to consider their exposure under the Bribery Act and, if necessary, implement new compliance policies and programs to mitigate their corruption risk appropriately. Click here for details.

- **Equality Act**. During 2011, employers will continue to grapple with the changes to UK discrimination laws introduced by the Equality Act which came into force in October 2010. In particular, new rules on pay secrecy clauses, pre-offer health questionnaires and the protections afforded to disabled employees on long term sick leave create challenges for businesses operating in the UK. In addition, from 1 April 2011, positive discrimination in recruitment and promotion will become lawful, but in very limited circumstances. Click here for details.

- **EU Agency Workers**. On 1 October 2011, the UK Agency Workers Regulations come into force and will entitle temporary agency workers (so called "temps") to the same basic working conditions as employees doing equivalent work after they have completed a 12 week qualifying period. Similar rules are being adopted across the EU. Click here for details.

- **Mandatory Retirement Abolished**. The coalition Government has announced that the current blanket rule which allows employers to retire employees upon a default retirement age (usually but not always 65) is to be abolished. We examine the circumstances in which employers may be able to retain a mandatory retirement rule. The change will be phased in between April and October 2011. Click here for details.

Employment Law Reform

The coalition Government has recently announced a major review of the way that employment disputes are resolved. Although Employment Tribunals, created in the 1970s, were designed as a low cost and accessible way of resolving workplace disputes, in recent years the number of claims has dramatically increased and employers have complained of the very substantial costs that they incur in defending claims – many of which are, in our experience, entirely without merit.

The highlights include:

- Increasing the ordinary qualifying period for bringing an unfair dismissal claim from 1 year to 2 years.
- Requiring all claims to be submitted for conciliation before they can be issued and encouraging workplace mediation.
- Requiring employees to pay a fee for issuing a claim or before allowing it to proceed to a full hearing.
- Requiring employees to provide more detailed information about the nature of their claim and their losses at the time they issue the claim. This will make claims easier to respond to.
- Developing a system whereby offers of settlement made by the employer can be taken into account when awarding compensation or assessing whether to make an award of costs. This is similar to the rules that apply in the civil courts whereby a

party can be penalised if they unreasonably fail to accept an offer made by the other party and then go on to lose their claim or recover less than the amount offered.

- Increasing the number of claims which will be heard by an Employment Judge sitting alone (i.e. without the two lay tribunal members who currently make up the three person panel) to include most unfair dismissal claims.
- Increasing the power to require employees to pay a deposit before continuing with weak cases and doubling the maximum size of the deposit from £500 to £1000.
- Making it easier for weak claims to be struck out without the cost and expense of a full hearing.
- Doubling the current limit on the amount of costs that may be awarded against a party where, for instance, it has acted "vexatiously, disruptively or unreasonably" or where the bringing of the claim was misconceived. The limit is currently £10,000 and the proposal is to increase it to £20,000.

Whilst the bulk of the changes are good news for employers there is a sting in the tail. The Government propose that employers who are found to have breached an employee's rights will face a fine of up to £5,000 payable to the Government. This would be in addition to the remedies already available to the employee which are mainly but not exclusively compensatory in nature.

The proposals are all subject to a detailed consultation exercise and much of the detail has yet to be fleshed out.

Financial Services Pay

On 1 January 2011, the Financial Services Authority's revised Remuneration Code (the "**Code**") came into force and now applies to approximately 2,500 FSA registered firms. For a detailed analysis of the Code and UK and European Remuneration Reform please click here.

In summary:

- The Code applies equally to branches and subsidiaries of non-EEA firms which are based in London.
- The Code has extra territorial reach applying to the remuneration of employees of a UK headquartered group worldwide. Where an institution is headquartered outside the EEA the Code also applies to non-UK members of a UK consolidation sub-group.
- The FSA has devised a high-level, four-tier proportionality framework, meaning that not all firms are required to fully comply with each of the principles set out in the Code.
- The Code is based upon twelve Remuneration Principles which apply primarily to Code Staff (as defined by the Code including senior management, risk takers,

control functions and other employees in a similar pay bracket) although firms are encouraged to apply the principles on a firm wide basis.

- Code Staff whose remuneration exceeds the *de minimis* threshold will find that:
  - at least 40% of variable remuneration will be deferred over at least three to five years (with awards vesting no faster than on a pro-rata basis and the first vesting no earlier than one year after the award);
  - at least 60% of variable remuneration will be deferred where the amount of the variable remuneration is particularly high (generally over £500,000); and
  - at least 50% of the total of any variable remuneration (including both deferred and undeferred elements) will be paid in a non-cash form and subject to minimum retention periods.

    The deferred components of both cash and share based remuneration will be subject to performance adjustment and run the risk of forfeiture. This means that Code Staff can expect to receive just 20-30% of variable remuneration by way of an "up front" cash payment.
- Guaranteed bonuses are restricted to one year and should not be routine but may be given only to new hires in exceptional circumstances -- for instance where "sign-on" bonuses are justified in order to "buy out" the arrangements offered by the employee's previous employer.
- The Code is backed up a statutory power which renders certain contractual provisions void to the extent that they breach Code provisions regarding: (a) guaranteed bonuses; and (b) deferral. A voiding provision of this nature is without precedent and gives the Code real teeth.

While the Code does not mandate that vesting should be subject to a requirement that the employee be "in employment" at the relevant vesting date, neither does it prevent employers from imposing such requirements. Employers seeking to deter key employees from leaving should consider making continued employment a condition of vesting of deferred awards. Such a requirement could help employers protect themselves against losing high profile teams to competitors. For further guidance on retaining key employees, please click here.

Bribery Act Compliance Procedures

The Bribery Act 2010 (the "**Bribery Act**") was originally scheduled to come into force in October 2010 and was then delayed until April 2011. However, following the announcement of a last minute ministerial review, Justice Minister Ken Clarke has today announced that the implementation of the Bribery Act will be further delayed pending the outcome of the review.

The Bribery Act is likely to dramatically impact the criminal exposure of corporations that carry on a business in the United Kingdom. For a detailed analysis of the provisions of the Bribery Act, subject to the outcome of the review, please click here and here.

The Bribery Act was to have direct consequences not just for UK companies but for all companies that carry on any part of a business in the UK, as it was to criminalise their corrupt behaviour regardless of the location of bribe or its receipt. The Bribery Act, which addressed the bribery of public officials and private parties alike, created personal criminal liability for senior officers of a company that commits a bribery offence with the consent or the connivance of that senior officer. Significantly, among the Bribery Act's four new bribery offences is the corporate offence of failing to prevent bribery. The only defence to this new strict-liability offence was to be that the company had in place "adequate procedures" for tackling bribery at the time of the conduct.

What elements of a compliance program qualify as "adequate procedures" was and remains unclear. Draft guidance from the Ministry of Justice was published in September 2010 (click here for details) and the final guidance will follow the outcome of the ministerial review. Regardless of what the Ministry of Justice recommends, it is clear that companies will need to take a hard look at their compliance programs to ensure they adequately address the specific corruption risks facing their particular businesses around the world.

Gibson Dunn has extensive experience in evaluating and designing corporate anti-corruption compliance programs. This includes assessing the structure and effectiveness of corporate compliance programs, reviewing reporting mechanisms, internal payment controls, and compliance messaging, and drafting new compliance materials, such as ethics and anti-corruption handbooks.

During the consultation on the Bribery Act that has taken place, Gibson Dunn attorneys have twice met with representatives of the Serious Fraud Office to discuss the practical implementation of the Bribery Act. Please click here for further details.

The Equality Act

The bulk of the Equality Act 2010 (the "**Equality Act**") came into force on 1 October 2010. The key practical changes are summarised in our previous client alert here and include a limit on the enforceability of pay secrecy clauses, a prohibition on generic questions about the health of a job applicant at pre-offer recruitment stage, an enhancement to the protection afforded to disabled employees who are absent on long-term sickness leave and an extension of the existing duty of employers to prevent harassment by third parties on the grounds of sex to cover most other protected characteristics (such as race, sexual orientation, religion, disability, etc.) (please click here for further details).

On 1 April 2011 one of the most controversial measures in the Equality Act will come into force. Employers in the UK will be permitted for the first time to prefer a "protected characteristic" candidate over a non-protected characteristic candidate for recruitment or internal promotion in circumstances in which both candidates are equally well qualified.

In order to engage in such positive discrimination, employers will first need to satisfy themselves that either: (a) persons who share a protected characteristic suffer a disadvantage connected to the characteristic; or (b) that the persons with the protected

characteristic are underrepresented in the job in question. Employers will then need to show:

- that the protected characteristic candidate is as qualified as the non-protected characteristic candidate;
- the employer does not have a policy of treating protected characteristic candidates more favourably then other employees; and
- that the action in question is a "proportionate means of achieving a legitimate aim".

Unfortunately, the statutory language is ambiguous and will require considerable clarification by the courts and tribunals.

Clients who have not already done so should review their internal policies, contracts and application forms to ensure that they have been updated to reflect the changes implemented by the Equality Act 2010.

EU Agency Workers

Employers in a variety of sectors make use of temporary agency workers ("temps") as a flexible and cost effective away of fulfilling their temporary staffing needs. Typically the worker is provided by an employment business and there is no direct contractual relationship with the hirer/client.

The UK Agency Worker Regulations 2010 shall come into force from 1 October 2011 from which time:

- After a 12 week qualifying period, agency workers will be entitled to the same "basic working conditions" as they would ordinarily have been entitled had they been directly employed by the hirer/client.
- An agency worker is an individual with a contract of employment or employment relationship with a temporary work agency who is assigned to a hirer/client to work temporarily under the hirer's/client's supervision and direction.
- Employees of outsourced service providers will not be agency workers (as they are not under the supervision of the client/agency) although those who provide their services through personal service companies may be.
- The equality principle only applies to "basic working and employment conditions" which include pay (widely defined to include performance bonuses, commission or holiday pay), duration of working time, length of night work, rest periods, rest breaks and annual leave. It excludes occupational sick pay, pension, severance, maternity pay or participation in financial participation schemes (such as share option schemes), benefits or loyalty/retention bonuses.
- The provision in the draft version of the regulations that would have allowed a client/hirer to justify less favourable treatment if an agency worker's contract, taken

as a whole, is at least as favourable as that of a comparator, has been removed from the final regulations.

- There is a limited exception that applies if the agency worker is employed by the employment business between assignments.

Employers should review the arrangements whereby they engage agency workers and the terms upon which they engage them in preparation for 1 October 2011.

Mandatory Retirement Abolished

Currently employers are able to dismiss employees by reason of retirement on or after their default retirement age (usually but not always 65) without exposure to compensation for age discrimination or unfair dismissal.

Age discrimination laws introduced in 2006 retained a special exemption which allowed an employer to retire an employee at its default retirement age (usually but not always 65) provided that a required procedure had been followed (the "Mandatory Retirement Exemption").

The new coalition Government has announced that they will abolish the Mandatory Retirement Exemption later this year.

Confusingly for employers, whilst the Mandatory Retirement Exemption is to go, employers may still be able to operate a blanket mandatory retirement rule. However, rather than relying upon a clear statutory exemption, they will instead need to prove that: (a) mandatory retirement at the age in question is objectively justified as being a proportionate means of achieving a legitimate aim; and (b) that the dismissal was fair in all the circumstances. At the time of writing the final statutory provisions have yet to be published and the leading domestic authority may be subject to an appeal to the Supreme Court, which means that employers who wish to continue with mandatory retirement ages should take specific legal advice on a case-by-case basis.

Significantly the change does not mean that employees will be compelled to work on but means that they will not be forced to leave employment before they are ready. The Government intends that the majority of employers will instead reach agreement with employees about retirement dates and, if this is not possible, employers will have to manage out poorly performing older workers.

As part of the review, the Government has recognised the disproportionate costs associated with providing certain insured benefits (such as life assurance) to older workers and has announced that it will introduce an exception to the age discrimination legislation allowing employers to specify a maximum age of 65 for participation in certain insured group risk benefits. Legislation is awaited.

Employers should act now to review the age profile of their workforce before the changes take effect.

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding these and developments. Please feel free to contact the Gibson Dunn lawyer with whom you work or the following lawyers in the firm's London office:

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