CLEARY GOTTLIEB

ALERT MEMORANDUM

SEPTEMBER 26, 2013 clearygottlieb.com

UK Government Response to Consultation on Proposed Changes to TUPE

1. Introduction

On 5 September 2013, the Government published a response to its January 2013 consultation (the "Consultation") in which it proposed a package of reforms to the Transfer of Undertakings (Protection of Employment) Regulations 2006 ("TUPE"). TUPE implements the EU Acquired Rights Directive (the "ARD") in the UK and provides an important legal framework for the transfer of employees in business sale transactions and certain service provision changes. In launching the Consultation, the Government was principally responding to concerns that, in certain areas, TUPE goes beyond the minimum requirements of the ARD (so called, "gold-plating"), carries unfair legal risks and is unduly burdensome.

The resulting changes will be implemented through regulations that the Government intends to lay before Parliament in December and which, subject to transitional and savings provisions, are expected to come into force in January 2014. Many respondents to the Consultation called for additional or improved guidance on TUPE and the Government has also committed to provide this in due course.

2. Executive Summary

In light of respondents' submissions, the Government has abandoned several of its proposed reforms in its Response. In particular, TUPE's service provision change rules will not be repealed, transferors will not to be allowed to rely on transferees' reasons to dismiss employees prior to a transfer, transferors' obligations to provide transferees with employee liability information will remain and TUPE's provisions on substantial changes to working conditions will not be amended.

Although the package of reforms being taken forward has been scaled back, it comprises several key changes. Notably, TUPE's provisions on dismissal by reason of the transfer and changes to terms and conditions are to be amended to remove ARD gold-plating. At the same time, the meaning of an "economic, technical or organizational reason" entailing changes in the workforce is to be expanded to cover changes in workplace location. TUPE will also be amended to provide that transferees' consultations that begin pre-transfer are capable of fulfilling collective redundancy consultation obligations and micro businesses will, in the majority of circumstances, be permitted to inform and consult with their employees directly.

3. Key changes

3.1 *Dismissals by reason of the transfer*

TUPE protects employees assigned to a transferring business from dismissal, as dismissals are considered automatically unfair if the sole or principal reason is: (a) the transfer itself; or (b) a reason connected with the transfer that is not an "economic, technical or organizational reason" *entailing changes in the workforce* (an "ETO Reason").

By referring to reasons "connected with" the transfer, the Government noted that TUPE arguably goes further than required by the ARD (which provides that "the transfer…shall not in itself constitute grounds for dismissal") and that it will amend TUPE to more closely reflect the ARD and bring it into line with case law of the Court of Justice of the European Union ("CJEU"). The precise language has not yet been provided, but the new provision is expected to refer solely to the "transfer itself" being the "reason" for the dismissal. However, the Government notes that the change will not necessarily mean that a dismissal for a reason "connected with" the transfer will, under the new provisions, necessarily be substantively fair, rather, there will be a new test to follow and the Government intends to provide guidance on this.

3.2 *Changes to terms and conditions*

The test outlined above applies also to changes to terms and conditions, which are void if the sole or principal reason for the change is: (a) the transfer itself; or (b) a reason connected with the transfer that is not an ETO Reason. In addition to removing the reference to changes that are "connected with" the transfer, the Government also intends to expand the meaning of an ETO Reason. The change will apply wherever the phrase is used, but it will be of particular relevance in the context of changes to terms and conditions.

Judicial interpretation of the requirement for an ETO Reason to involve "changes in the workforce" has focused on changes in the numbers or functions of employees and the Government acknowledged that this does not necessarily enable a transferee to agree with employees a change in workplace location. The new regulations will expressly provide that a change in workplace location can constitute an ETO Reason (i.e., even if employee numbers or functions are not affected). For clarity, the new regulations will also confirm that variations made pursuant to contractual variation clauses (e.g., mobility clauses) are not limited or prevented by TUPE.

The Government acknowledged concerns that TUPE restricts a buyer from making harmonizing changes post-transfer, but as it is constrained by the jurisprudence of the CJEU the Government declined to make any more significant changes to address these concerns. Instead, the Government has committed to engage with European partners to demonstrate the potential benefits of a harmonization framework for individuals and the economy.

The current prohibition on changes to terms and conditions applies equally to terms that derive from or incorporate terms of collective bargaining agreements ("CBAs"). In exercise of a permitted derogation under the ARD, under the new rules this prohibition will cease to bind a transferee one year after the transfer, with two important qualifications. First, the change must be no less favorable to the employee overall and second, ordinary contractual principles will apply to the implementation of any such change. As a related change, the new regulations will also reflect a recent judgment of the CJEU in which it was confirmed that a transferee cannot be bound by post-transfer changes to CBAs if it is not able to be involved in the negotiations of such changes (i.e., it is only bound by terms existing at the point of transfer, the so-called "static" approach, rather than also terms resulting from changes made post-transfer, the "dynamic" approach).

3.3 *Pre-transfer consultation on collective redundancies*

Where, as a post-transfer measure, a transferee proposes to dismiss 20 or more employees within a 90 day period, overlapping obligations to inform and consult arise under TUPE and the UK's collective redundancy legislation. Although in practice a transferor may permit a transferee to begin collective consultation pre-transfer, it is currently unclear whether any steps taken by a transferee pre-transfer count for purposes of discharging its obligations to consult on collective redundancies.

The Government has recognized that being able to run the two procedures concurrently increases business efficiency and will reduce periods of uncertainty and confusion for employees. As a result, the Government will amend TUPE to expressly provide that collective redundancy consultation by a transferee which begins pre-transfer *is capable* of counting for purposes of the transferee's compliance with collective redundancy obligations. Importantly, however, the transferee will not be *required* to consult pre-transfer, and nor will the transferor be required to *allow* consultation, which will need to be done consensually. In addition, only consultation that is "meaningful" will count.

3.4 *Micro businesses*

At present, all employers regardless of their size are required to inform and, where measures are proposed, consult with "appropriate representatives" of affected employees. The Government has identified that these obligations are not suited to micro businesses (that is, those employing 10 or fewer employees) and, in exercise of a permitted derogation under ARD, will amend TUPE to allow micro business to inform and consult with their employees directly, in circumstances where trade union representatives or other pre-existing employee representatives do not exist.

The Government also noted that, notwithstanding the current moratorium on new regulation for micro businesses lasting until 31 March 2014, micro businesses will not be exempt from the forthcoming TUPE amendments and will be able to benefit from the changes.

4. Abandoned proposals

4.1 *Repeal of service provision changes ("SPCs")*

The Government's widest ranging proposal was the repeal of the SPC provisions in TUPE. Broadly, these provide a special test to determine whether TUPE applies to insourcing, outsourcing and change of service provider transactions, without needing to satisfy the general test for a transfer of an undertaking. Prior to 2006, only SPCs that satisfied the general test were subject to TUPE and it is generally accepted that the SPC rules represent ARD gold-plating. Whilst a number of arguments in favor of repeal were put forward by respondents to the Consultation, including that the automatic transfer of employees from one contractor to another may undermine a reason for the change of contractor, the Government was satisfied that a clear rationale for retaining the SPC provisions was presented. In particular, the Government concluded that removal of the SPC provisions would lead to a significant amount of legal uncertainty as to whether transactions were within the scope of TUPE or not, which could result in longer transaction timetables and a revival of costly litigation on the subject. The Government was also particularly concerned about the impact of the changes on existing contractors who in some cases could become subject to material unforeseen redundancy liabilities that would ruin them.

Although the Government has decided not to repeal the SPC provisions, the new regulations will recognize a requirement developed by case-law that, in order for the SPC test to be met, the activities carried on by the transferee must be "fundamentally or essentially the same" as those carried on by the transferor. This means that substantial differences in the nature of activities carried out by a transferor or how those activities are carried out may defeat an SPC and preclude TUPE from applying.

4.2 *Allowing pre-transfer dismissals in reliance on the transferee's ETO Reasons*

The Government has decided not to amend TUPE to allow a transferor to rely on a transferee's ETO Reasons to dismiss employees prior to the relevant transfer date. Although the majority of respondents were in favor of such an amendment, and cited benefits including reduced uncertainty for employees and greater flexibility for businesses, respondents' submissions also highlighted several significant problems. In particular, the Government noted that such an amendment could lead to employees being selected for redundancy only or predominantly from the transferor's workforce and would therefore be unfair for employees as well as for the transferor. Also, such pre-transfer dismissals might be abused by some transferors in order to make their business more attractive to potential buyers and to achieve a higher price. Given the problems highlighted, the Government concluded that although allowing transferees to make pre-transfer dismissals in reliance on the transferee's ETO Reasons might be beneficial to some businesses, overall such an amendment would increase unfairness in the employment market and should therefore not be taken forward.

4.3 *Provision of employee liability information*

The Government also declined to repeal the current obligation on the transferor to provide the transferee with detailed specified information about each transferring employee no later than 14 days before the transfer and replace it with a general obligation supplemented by guidance, a move that will satisfy the overwhelming majority of respondents who opposed the proposal. However, to address one of the key criticisms of the existing rules that the information is often provided to the transferee too late to be useful or to be taken into account in the information and consultation process, the Government has decided to extend the deadline from 14 to 28 days before the transfer. It is acknowledged that this may lead to an increase in information updates needing to be provided prior to the transfer date. The current exception to the strict deadline, that applies in special circumstances where it is not reasonably practical to comply with the deadline, will remain.

4.4 *Substantial changes to working conditions*

Finally, despite broad support for tracking the wording of the ARD more closely, the Government decided against amending the provision that allows an employee to treat himself as having been dismissed where a relevant transfer involves, or would involve, a substantial change in working conditions to his material detriment, on the basis that it would add unhelpful complexity and be less relevant in practice once location changes were brought within the concept of an ETO Reason. The concern principally related to the fact that, under the current rules, an employee may have an automatic unfair dismissal claim in circumstances that may not justify a constructive dismissal claim and that this may be an unintended consequence of the use of the word "dismissal" in TUPE instead of merely the word "termination" used in the ARD.

* * *

If you have any questions, please feel free to contact any of your regular contacts at the firm or any of our partners and counsel listed under the "Practices" section of our website at http://www.clearygottlieb.com.

CLEARY GOTTLIEB STEEN & HAMILTON LLP

Office Locations

NEW YORK
One Liberty Plaza
New York, NY 10006-1470
T: +1 212 225 2000
F: +1 212 225 3999

WASHINGTON
2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
T: +1 202 974 1500
F: +1 202 974 1999

PARIS
12, rue de Tilsitt
75008 Paris, France
T: +33 1 40 74 68 00
F: +33 1 40 74 68 88

BRUSSELS
Rue de la Loi 57
1040 Brussels, Belgium
T: +32 2 287 2000
F: +32 2 231 1661

LONDON
City Place House
55 Basinghall Street
London EC2V 5EH, England
T: +44 20 7614 2200
F: +44 20 7600 1698

MOSCOW
Cleary Gottlieb Steen & Hamilton LLC
Paveletskaya Square 2/3
Moscow, Russia 115054
T: +7 495 660 8500
F: +7 495 660 8505

FRANKFURT
Main Tower
Neue Mainzer Strasse 52
60311 Frankfurt am Main, Germany
T: +49 69 97103 0
F: +49 69 97103 199

COLOGNE
Theodor-Heuss-Ring 9
50688 Cologne, Germany
T: +49 221 80040 0
F: +49 221 80040 199

ROME
Piazza di Spagna 15
00187 Rome, Italy
T: +39 06 69 52 21
F: +39 06 69 20 06 65

MILAN
Via San Paolo 7
20121 Milan, Italy
T: +39 02 72 60 81
F: +39 02 86 98 44 40

HONG KONG
Cleary Gottlieb Steen & Hamilton (Hong Kong)
Bank of China Tower, 39th Floor
One Garden Road
Hong Kong
T: +852 2521 4122
F: +852 2845 9026

BEIJING
Twin Towers – West (23rd Floor)
12 B Jianguomen Wai Da Jie
Chaoyang District
Beijing 100022, China
T: +86 10 5920 1000
F: +86 10 5879 3902

BUENOS AIRES
CGSH International Legal Services, LLP-
Sucursal Argentina
Avda. Quintana 529, 4to piso
1129 Ciudad Autonoma de Buenos Aires
Argentina
T: +54 11 5556 8900
F: +54 11 5556 8999

SÃO PAULO
Cleary Gottlieb Steen & Hamilton
Consultores em Direito Estrangeiro
Rua Funchal, 418, 13 Andar
São Paulo, SP Brazil 04551-060
T: +55 11 2196 7200
F: +55 11 2196 7299

ABU DHABI
Al Sila Tower, 27th Floor
Sowwah Square, PO Box 29920
Abu Dhabi, United Arab Emirates
T: +971 2 412 1700
F: +971 2 412 1899

SEOUL
Cleary Gottlieb Steen & Hamilton LLP
Foreign Legal Consultant Office
19F, Ferrum Tower
19, Eulji-ro 5-gil, Jung-gu
Seoul 100-210, Korea
T:+82 2 6353 8000
F:+82 2 6353 8099