

EMPLOYMENT ACT 2002

EXPLANATORY NOTES

SUMMARY OF REGULATORY IMPACT ASSESSMENT

Overview of the impact of the Act

169. The overall intention of the Act is to support the development of more productive workplaces in the UK by encouraging participation in the labour market through the retention and development of skills, and by improving the way that disputes are managed, both at work and within the employment tribunals system. This impact assessment considers the individual proposals and their overall effect. Where they overlap or enhance each other this will be addressed. Self-standing impact assessments are attached for each element of the Act expected to affect business.
170. All the provisions in the Act will have some impact on the productivity and competitiveness of UK employers, and on the workforce as a whole. Those parts of the Act which relate to dispute resolution are intended to bring benefits, both quantifiable and unquantifiable, to employers and employees through encouraging in-house resolution of disputes without recourse to Employment Tribunals. Unresolved conflict in the workplace can damage morale, increase stress, and may lead to employees quitting their jobs. Equally, disputes taken to Employment Tribunals reduce productivity because of the resources taken up in the legal process and because of their effects on the morale and motivation both of the individuals directly affected, and in the workplace more generally.
171. The parts of the Act dealing with maternity, paternity and adoption pay and leave are intended to encourage greater participation in the labour market, and the retention of skills, for parents who might otherwise leave the labour market. In addition, there are motivational and productivity benefits through relieving the stress and strain felt by new parents. The provisions in the Act which place union learning representatives on a statutory footing will also enhance productivity by encouraging workforce development. The proposal to extend the European Directive on fixed term work to include pay and pensions will ensure that fixed term contract employees are not discriminated against and will thereby increase employee security and remove a potential distortion in the labour market. The provisions that introduce work-focused interviews for partners of people receiving working-age benefits will also have a positive impact on participation in the labour market but are not included in the Impact Assessment as they do not impose any cost or burden on business.
172. Quantified costs and benefits are expressed in current (2000/01) prices with the exception of the provisions for maternity pay, paternity leave and pay and adoption leave and pay. For consistency with public expenditure plans, these are expressed in 2003/04 prices.

Better dispute management

173. The Act provides for improved dispute resolution in the workplace and in the employment tribunal system. Existing problems in the current system of dispute resolution have contributed towards increasing numbers of Employment Tribunal

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applications. These are putting employers, employees and the tribunal system itself under strain. A dispute resolved in the workplace, especially one resolved early and informally, will reduce workplace tensions and increase retention of valuable staff. A dispute resolved in a Tribunal often leads to the end of the employment relationship. For the employee this means the loss of a job; for the employer it means unnecessary recruitment and lost skills. And where a dispute does have to go through the Tribunal process, cases should be resolved more quickly, reducing uncertainty for applicants and employers alike.

174. The Act contains several measures to address this. Not all of them have implications that need to be assessed in a regulatory impact assessment. Those included in the RIA are:
- Implied term of contract to confer right/obligation to follow ‘three steps’ grievance and discipline procedures;
 - All written statements of terms and conditions to include reference to workplace procedures (removal of small firms exemption);
 - Tribunals to mitigate awards to reflect whether three steps were followed and whether terms and conditions were provided;
 - Removing procedural traps in unfair dismissal cases;
 - Fixed period of conciliation in all Tribunal cases;
 - Changes to reduce wasted costs;
 - Introduction of questionnaires in equal pay cases.
175. The individual paragraphs below contain costs and benefit estimates for these provisions. There are strong overlaps between most of these proposals. The total benefits and costs are less than the sum of the individual benefits and costs.
176. Proposals for (i) Implied term of contract to confer right/obligation to follow ‘three steps’ grievance and discipline procedures; (ii) All written statements of terms and conditions to include reference to workplace procedures (removal of small firms exemption); and (iii) Tribunals to mitigate awards to reflect whether three steps were followed and whether terms and conditions were provided
177. All employers will have to introduce a satisfactory (that is, according to minimum standards) 3-step dispute and grievance procedure to deal with employment issues arising in the workplace. Employees are also obliged to use this procedure. If either party does not fulfil their obligation, this will be reflected in the award.
178. This provides both employees and employers with an incentive to start a discussion about any problems, which may arise. This should in the medium to longer term improve employment relationships and open up the way both parties handle conflicts. Employers will feel the benefit of a clear transparent process that helps them to resolve problems. Employees who otherwise would have left because they felt they had been treated unfairly, or because the relationship had deteriorated over the months leading up to a Tribunal case, may now decide to stay.
179. The evidence suggests that most large employers have procedures that already meet the minimum standard. A disproportionate share of tribunal applications arise in workplaces where procedures are absent or have not been followed adequately. Greater use of procedures should therefore reduce significantly the volume of tribunal applications.
180. The estimated reduction in the number of applications is between 30,000 and 40,000 applications per year. Employers save time and money (£60– 80 million), employees save their own time and reduce stress levels and there are savings to the taxpayer through fewer cases (£11–15 million). There will be a time lag between the more

widespread introduction of procedures in firms and a reduction in Tribunal applications of perhaps one year.

181. There are costs to employers. There are one-off costs arising from the introduction or revision of disciplinary and grievance procedures where these do not already meet the minimum requirements, and from incorporating these into the written statement of employment (£46–86 million). There are also on-going costs arising from the management time involved in greater use of these procedures (£42–90 million per year).

Removing procedural traps in unfair dismissal cases

182. Some employers have lost faith in the Tribunal system because they believe they will lose an unfair dismissal case because of a small procedural mistake, even if following the correct procedure would have made no difference to the outcome. The new policy is that, in cases where it can be shown that the mistake would not have made a difference to whether a dismissal was fair or unfair, the Tribunal will have the opportunity of disregarding the procedural error. This will only apply for procedures that go over and above the 3-step procedures that will now be part of the contract of employment.
183. This change should discourage some Tribunal applications based mainly on procedural error. The benefits to employers are £6-11 million per year. Of these about £4-6 million are transfers from employees due to changes in the structure of tribunal outcomes. The benefits to the taxpayer are about £1 million.
184. The costs of the proposal are also related to the shift in outcomes. Individuals have reduced awards and settlement payments of about £4-6 million. Respondents lose £1-4 million. There are costs to the taxpayer of £2-5 million.

Fixed period of conciliation in all Tribunal cases

185. A large number of applications are settled with the help of ACAS conciliations (38%). This proportion differs between jurisdictions. In addition, withdrawn cases are sometimes influenced by ACAS conciliators. Some of the settlements or withdrawals occur just before the hearing. This can be costly for the taxpayer.
186. The provision to be introduced is to use a fixed period for conciliation during which the minds of both parties can focus on the conciliation process.
187. A fixed conciliation period of six weeks aims to increase the number of settlements and reduce the number settling close to a hearing date. The latter effect, in particular, will help the ETS to handle other applications more efficiently.
188. The number of hearings is expected to fall by between 1,700 and 3,400 each year. There are some transfers between respondents and applicants due to a change in the structure of outcomes. There are financial benefits to employers of £3-7 million and to the taxpayer of £2-3 million. Individuals also benefit by £1-2 million from more settled cases at the expense of employers.

Wasted costs

189. The Act includes provisions that provide stronger disincentives to unreasonable behaviour both up to and during the hearing process, through changes to the rules on award of costs and a new provision for awards in respect of a party's preparation time. The tribunal will be able to make an award in respect of time spent by parties in preparing the case where cases or defences are misconceived (which includes having no reasonable prospect of success), or where the other party has behaved unreasonably. Costs awards will be possible against representatives who are acting on a for profit basis where it is their behaviour that has triggered the cost award.
190. The proposals should discourage a small number of weak Tribunal applications (100-500 per year) and will also encourage more settlements and fewer hearings. In

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addition, more cost awards will be made, providing more compensation to those at the receiving end of unreasonable behaviour.

191. It is estimated that savings to the taxpayer will amount to a little under £1 million per year, together with benefits to employers from less applications of £0.2-1 million. There will also be increased flows of payment between employers and applicants arising from the increased use of cost awards. Applicants are expected to benefit by £0.4-0.5 million whereas respondents are expected to benefit by £0.7-1.1 million (respondents benefit more because they are likely to incur more management time and legal representation in dealing with a Tribunal application).

Equal Pay questionnaire

192. The Act introduces a formal questionnaire procedure for use in equal pay tribunal cases, with time limits for an employer response. The purpose of the procedure is to help the potential applicant decide whether to institute proceedings and to help them to formulate and present their case. This enables the key facts to be settled quickly and can encourage not only the swift establishment of evidence but also the settlement of cases.
193. Introduction of the questionnaire procedure is expected to lead to a 10% reduction in the number of equal pay Tribunal applications. Benefits to the taxpayer are estimated to be £0.1 million. Employer benefits are estimated at £0.5 million.
194. Total costs to employers of completing the questionnaire procedure are estimated to be between £ 0.2 and £ 0.4 million.

Overall effect of dispute resolution procedures

195. The overall effect of the proposals above is not the sum of each individual proposal. Several proposals address the same or closely related issues. Their effects therefore overlap.
196. The tables on pages 46 and 47, on the overarching effects of the dispute resolution proposals, set out the assumptions made in calculating the overall impact of these proposals.
197. The most significant proposal in terms of impact is the introduction of grievance and disciplinary procedures as a contractual right. If this is implemented, fewer disputes will go to Tribunals - thus reducing the costs and benefits of almost all of the above proposals that address cases that do reach Tribunals.
198. The total effect of the proposals is estimated to be a reduction in the number of applications of 23-31% or by between 30,000 and 40,000 applications (using current application volumes as a starting point)¹. The related benefits to employers are estimated to be £65-91 million once the proposals have fed through into reduced Tribunal applications. The taxpayer will benefit by £13-18 million and individuals by £1-2 million. There are some costs to employers especially due to the introduction of procedures. One off costs are £46-86 million. The use of procedures leads to ongoing costs of £42-90 million. Employers who already have and use procedures will not face additional costs. The other proposals add a further £2-4 million. Costs to the taxpayer are mostly related to changes in the outcome of applications and are therefore policy costs not implementation costs. These are £1-3 million.

¹ ETS has only been able to deal with 70% of application in 2000/01. The benefits to ETS are therefore built on 70% of the estimated reduction in the number of cases.

Participation in the labour market and retention, and development of skills

Paternity leave and pay

199. The law will provide fathers with an entitlement of 2 weeks paid leave (at £100 per week) to be taken during the first 8 weeks of the child's life. The intended effect is to give fathers a chance to support the mother during this crucial period and to assist them in building a relationship with the new child.
200. The main benefits arise for fathers and their families. In total they will receive £63 million in form of the statutory payments. They also have more time off during a crucial period in their family life.
201. There are costs for business. Many firms already offer some form of paternity leave, either paid or unpaid. The additional burdens on business are therefore expected to be small. Costs arise from the provision of coverage for absent fathers of £25-42 million. These are recurring costs. Introducing the system costs business about £10 million (one-off) and running the system costs £21-32 million (recurring costs). There are costs to the Government because of the payments made to fathers of £63 million.

Adoption leave and pay

202. At present, adoptive parents only have the right to unpaid parental leave. It is proposed to give one adoptive parent the statutory right to 26 weeks paid leave at £100 per week or 90% of their average earnings (whichever is lower) and an additional 26 unpaid leave. This will enable adoptive parents to spend one year with the child and establish their new relationship. These changes are expected to come into force in April 2003.
203. The beneficiaries will be adoptive parents and their children. It is estimated that there will be around 3,550 adoptions per year. They will benefit by a total of £10 million per year due to the payments. This represents a cost to the taxpayer.
204. Costs to business are to cover for the absent parent. These costs are estimated at £2-3 million per year. Business also has to introduce the necessary payment system. This will be similar to the system for maternity leave. Additional costs will be no more than £1 million.

Maternity Pay

205. The Act makes changes to Statutory Maternity Pay and Maternity Allowance. The rate of flat-rate weekly payment will increase to the lesser of £100 a week or 90% of the woman's average weekly earnings, and the maximum payment period will increase from 18 weeks to 26 weeks. The notice that a woman must normally give her employer before taking maternity leave will increase from 21 to 28 days.
206. The aim of these measures is to make it easier for women to achieve a better balance between paid work and family life. It does this in combination with changes to maternity leave that are being introduced through secondary legislation². The changes will also help women to spend more time with a new-born child. As a result, more mothers may be able to return to employment after maternity leave, retaining skills in the labour market and reducing recruitment costs for employers.
207. There are direct benefits to mothers in the form of the payments made to them of £325 million per year. The benefits for an individual mother will depend on her personal circumstances. The benefit of £100 is above the earnings threshold for National Insurance Contribution. Recipients will therefore have to pay NI contributions. This benefits the National Insurance Fund by £5 million, whereby each individual mothers pays £1.35 per week.

2 ⁴ Cross-reference to government response on maternity pay and leave, paternity and adoption pay and leave.

208. The Government meets £305 million of the payments to mothers. The £20 million difference between this and the £325 million figure is made up of costs to larger employers who are only able to reclaim 92% of the payments to mothers. Some employers, especially larger ones, will have to change their payroll systems. The costs of this change are unlikely to be significant because many employers use standard software packages that are updated routinely in any case.

Duty to consider requests for flexible working from the parents of young children

209. The impact of the duty to consider requests for flexible working will depend on how many parents exercise the right and how employers respond. A central estimate of take-up suggests that there could be over 500,000 additional requests each year for flexible working and that about 80% of these will be accepted or a compromise reached. This means that hundreds of thousands of working parents and their families benefit from an improved family life. The economy also benefits – savings in recruitment costs alone are valued at £113 million. However, processing requests and accommodating them is not costless. One-off implementation costs are estimated to be £38 million with annual recurring costs of £286 million.

Putting Union learning representatives (ULR) on a statutory footing

210. The objective of this provision is to improve the skills of the workforce by increasing the number of ULRs and improving their effectiveness. The provision will further reduce the current uncertainty regarding the position of the ULRs and the time and resources they may use to fulfil their task.
211. There are benefits to employers and employees. Employers gain from enhanced workforce skills leading to improved productivity, complementary effects between ULRs and the human resources team, increased confidence in staff and improved employment relations and a sense of partnership in the workplace. As far as these benefits are quantifiable, they are estimated to be between £16-33 million, steadily rising with increased effectiveness to between £70-140 million in the eighth year after introduction of this provision.
212. There are some costs to employers which are due to the time spent on training ULRs, the time the ULRs spend in fulfilling their task and the administrative costs of understanding the legislation, handling notices and requests for time off. The increased use of ULRs will increase the first two items of this list. Total costs increase from £7 million in the first year to £26 million in the eighth year after the introduction of the provision.

Preventing pay and pensions discrimination against fixed term employees

213. The Act includes a power to prevent pay and pensions discrimination against fixed-term employees that will be implemented alongside the European directive on fixed term work.
214. There are 1.1-1.3 million FTC employees who are potentially affected by these provisions. A relatively small proportion (28-41,000) will benefit from higher pay with total benefits of £21-30 million per year. Similarly, 55-82,000 FTC employees will benefit from greater occupational provision with total benefits of £33-98 million per year.
215. Costs to employers mirror benefits to employees. The costs of the pay provisions are estimated to be £28-39 million (the difference between costs and benefits is accounted for by employer National Insurance Contributions). The costs of the pension provisions are £33-97 million.

Impact on small businesses

216. The measures proposed in the Act affect businesses of all sizes. The consultation exercises carried out for most of the proposals received responses from small and large businesses. In the main areas - the provisions on dispute resolution and on maternity, paternity and adoption pay and leave - focus groups were convened with small firms. The Small Business Service has been consulted on each of the stand-alone RIAs.
217. The proposal to require minimum disciplinary and grievance procedures is likely to disproportionately affect small firms. This is because they are less likely to have procedures that meet this standard or follow them if they are in place. Hence the costs of introducing them will bear most on small businesses - but so will the benefits through reductions in cases going to Employment Tribunals. The proposal to remove procedural traps may benefit small businesses especially as there is evidence that small firms are most likely to make procedural errors.
218. There is some evidence to suggest that small firms can find it more difficult than larger businesses to cover for absences because they have a smaller number of people to whom work can be re-allocated. Hence the costs of covering for absences - especially paternity leave - may be more acute in small firms.
219. Small firms are less likely to employ FTC employees than larger firms.

Summary Table

Quantifiable Benefits

220. All amounts in £m, rounded to nearest million except where amounts are less than £1m

	<i>To employers</i>	<i>To individuals</i>	<i>To the taxpayer</i>
Dispute resolution	65-91 (from year 2)	1-2	13-18(from year 2)
Paternity leave and pay		63	
Adoption leave	2	10	
Maternity pay		325	
Duty to consider requests for flexible working	113		
Union learning reps	16-33 (year 1)		
	70-140 (year 8)		
Fixed term work		54-127	

Quantifiable Costs

221. All amounts in £m, rounded to nearest million except where amounts are less than £1m

	<i>To employers</i>	<i>To individuals</i>	<i>To the taxpayer</i>
Dispute resolution	46-86 (one-off)	3-5	1-3
	44-94 (recurring)		
Paternity leave and pay	10 (one-off)		63 (recurring, transfer)
	39-64 (recurring)		

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	<i>To employers</i>	<i>To individuals</i>	<i>To the taxpayer</i>
Adoption leave and pay	1 (one-off)		9 (recurring, transfer)
	2-3 (recurring)		
Maternity pay	20		305 (transfer)
Duty to consider flexible working	38 (one-off)		
	286 (recurring)		
Union learning reps	7 (year 1)		
	26 (year 8)		
Fixed term work	61 -136 (recurring)		

222. The total one-off costs to employers of the changes proposed amount to £95-135 million. These reflect principally the costs of setting up disciplinary and grievance procedures and changes to personnel systems arising from paternity and adoption leave and pay and the duty to consider requests for flexible working from the parents of young children.
223. Recurring costs to employers amount to £459-629 million. The principal costs arise from greater use of workplace procedures, covering for paternity and adoption leave and longer periods of maternity leave, supporting ULRs, and improving the pay and pensions of FTC employees. Costs will increase over time as ULRs become more widespread.
224. The proposals also benefit employers. Many of these benefits - such as improved morale, skill utilisation and better employment relations - cannot be quantified. Some, however, have been quantified. These include recruitment savings from more mothers returning to work after maternity leave, a reduction in costly Employment Tribunal cases, and greater productivity through ULRs. Initially, these benefits are quantified at £196-239 million. However, they will increase over time as ULRs become more widespread and more effective. It is possible that quantified benefits could exceed quantified costs to employers within a reasonable period of introduction - even leaving to one side the unquantified productivity benefits³.
225. Individual workers benefit by almost £453-527 million from enhanced maternity pay and paternity pay and adoption pay and improved pay and pensions for FTC employees. There are also modest financial benefits to individual applicants arising from the dispute resolution procedures that are roughly offset by costs arising from other elements in this package. But while this part of the Act may be broadly neutral in its financial effects, improved dispute resolution has broader but unquantified benefits.
226. Costs to the taxpayer are expected to be around £380 million per year and arise almost entirely from maternity, paternity and adoption pay. The dispute resolution proposals should produce net savings to the taxpayer once the effect of the proposals has fed through into reduced Tribunal applications.

³ ⁵ Using the range provided in the RIA for ULRs, total benefits to employers could be in the range £100-230 million after eight years.