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BIS Call for Evidence:

Dealing with Compensated No Fault Dismissal – Micro Businesses

Response from the Employment Lawyers Association

7 June 2012

EMPLOYMENT LAWYERS ASSOCIATION

RESPONSE TO BIS RE NO FAULT DISMISSAL

1 INTRODUCTION

The Employment Lawyers Association ("ELA") is a non-political group of specialists in the field of employment law and includes those who represent Claimants and Respondents/Defendants in the Courts and Employment Tribunals. It is therefore not ELA's role to comment on the political merits or otherwise of proposed legislation, rather to make observations from a legal standpoint. ELA's Legislative and Policy Committee ("the L&P Committee") and the working party set up to respond to this particular consultation are made up of both Barristers and Solicitors, working in private practice and in-house, who act for both Claimants and Respondents. The working party members who responded to this Call for Evidence are listed at the end of this document. The L&P Committee meets regularly for a number of purposes including to consider and respond to proposed new legislation.

2 RESPONSE TO BIS CONSULTATION

Call for evidence: Dealing with Dismissal and "Compensated No Fault Dismissal" for Micro Businesses ("the Call For Evidence")

2.1 The pros and cons of Compensated No Fault Dismissal ("CNFD")

2.1.1 Introduction

The basic proposition of CNFD, i.e. enabling micro businesses to dismiss at will (other than for an impermissible reason connected to a Protected Characteristic or for an automatically unfair reason) without the risk of facing an unfair dismissal claim in return for payment to the employee of an appropriate sum of money by way of a pre-defined compensation sum, may be desirable on many levels. This is because it would dispense with the need for a micro business to engage in what are often long winded and costly procedures, which they can often ill afford, both from a management time perspective and in relation to expenditure on legal costs.

However, there are numerous problems associated with the introduction of CNFD which are highlighted below and which would need to be addressed.

2.1.2 Assumptions

We have made the following assumptions when compiling this response:

(a) That there would be a very limited process (if any) involved in carrying out a CNFD. Any requirement for due process would ultimately defeat the purpose of CNFD.

(b) That, in order for the concept of CNFD to be feasible, a micro business would be able to use CNFD to dismiss for any potentially fair reason. In other words, an employer could

elect to use CNFD not just where an employee is underperforming, but also for conduct, capability (ill health), redundancy, and some other substantial reason (such as a personality clash). Employers who did however carry out a dismissal where the actual reason was for an automatically unfair reason (such as trade union activities) or connected to a Protected Characteristic, would still be exposed to the risk of an unfair dismissal claim. CNFD would need to be all encompassing to minimise the risk of satellite litigation about the true reason for the dismissal, which would largely defeat its purpose. For example, if CNFD only covered performance related dismissals, and the employee disputed that performance was the reason for the dismissal, the employee may bring a tribunal claim to challenge the reason for the dismissal. Further, it is not always easy to distinguish between conduct and performance, and the two are not necessarily mutually exclusive. Finally it would avoid the rather absurd position whereby an employer would be able to dismiss under CNFD for poor performance (which may be trivial poor performance), but would have to carry out a disciplinary process for an employee guilty of serious misconduct.

(c) That the employer must expressly elect to use CNFD to avoid any uncertainty as to the fact that the CNFD process has been invoked.

(d) The employer will retain the ability, if it chooses not to opt for a CNFD, to follow the usual processes for dismissal of an employee and therefore not have to pay compensation up front but leaving itself exposed to a potential unfair dismissal claim, presuming the employee has the requisite qualifying service.

(e) The decision to go down the CNFD route must be at the employer's sole election. The employee would have no ability to refuse to be dismissed by way of a CNFD. If the employee had the ability to refuse/employee consent was required, this would remove the benefit of CNFD for a micro business.

(f) That the government would create a template letter for use in CNFD's to assist micro businesses.

(g) That, to minimise any satellite litigation, the legislation and government guidance would clearly set out:

(i) for what potentially fair reasons an employer was entitled to use a CNFD;

(ii) the definition of a micro business, including the definition of an "Associated Employer", how to calculate headcount and the date on which the assessment should be made as to whether the employer is a micro business (i.e. the date of employment, notice, or termination);

(iii) what specific level of compensation should be paid to the employee and the tax treatment of that payment; and

(iv) the process (if any) which an employer needs to follow when carrying out a CNFD.

(h) There will be no anti-avoidance provisions which seek to act as a deterrent to employers who may be tempted to manipulate the rules on headcount and the date of assessment of whether or not they are a "Micro Employer". In the Agency Workers Regulations 2010, there are relatively simple anti-avoidance provisions which are designed to deter abuse of the provisions which provide agency workers with greater legal protection. It may be appropriate to introduce similar anti-avoidance provisions here but we consider that any such provisions would result in additional satellite litigation about whether or not they had been breached. To be effective they would also need to be enforced, presumably through the employment tribunals, which would result in additional time and cost to a micro business (and burdening tribunals), largely defeating the purpose of CNFD.

(i) That the government would set the level of compensation at an appropriate level, striking a balance between the need properly to compensate the employee for his/her dismissal, but also not making the payment too onerous to micro businesses as this would be a disincentive to use CNFD.

(j) That the compensation payment made for a CNFD would be tax free up to £30,000 in accordance with existing rules on the taxation of termination payments.

(k) That the government has sound reasons for proposing to fix the definition of a micro business as one which employs fewer than 10 employees. We are not aware of any explanation for setting it at this level, and note that previously, the two years unfair dismissal service qualification requirement that was in place under the Employment Protection (Consolidation) Act 1978, only applied to employers with fewer than 20 employees.

2.1.3 What are the pros of introducing CNFD?

(a) Conducting a performance management process or a dismissal process takes time. In a micro business, management resources are more scarce and micro businesses are less likely to have the support of any trained HR function to deal with these issues. In micro businesses, the employer is more likely to have already made its decision before any process is followed, rendering the process a charade which does neither party any favours. CNFD would free up valuable management time, leaving managers to focus on getting their businesses to prosper.

(b) CNFD would provide micro businesses with a mechanism to dismiss employees quickly, without the risk of a claim for unfair dismissal (save in cases of automatically unfair dismissals or for a Protected Characteristic). This would save small businesses from the time and expense associated with having to defend an unfair dismissal claim, including the cost of having to instruct legal advisers and potentially paying uncertain levels of compensation.

(c) In a micro business, the impact of an employee not performing is magnified and the employer should, arguably, be able to take prompt action to deal with it and protect business interests.

(d) Micro businesses often find it hard to keep up to date with changing employment law, including evolving case law relating to unfair dismissal. Introduction of CNFD may help micro businesses avoid unfairly dismissing someone because the business was unaware of the strict legal requirements.

(e) An employee who is found to have committed an act of misconduct may benefit from being dismissed for a CNFD, as any future reference provided by the dismissing employer would presumably refer to the fact it was a "no fault" dismissal.

2.1.4 What are the cons of introducing CNFD?

(a) It is likely to result in significant satellite litigation even greater than was generated by the 2004 Statutory Dismissal and Disciplinary Procedures. We envisage significant litigation over:

(i) The definition of a micro business. This would need to be very carefully drafted and deal with the position in relation to any "Associated Employer" to ensure that companies within a group do not abuse the micro business exemption. It would also need to set out very clearly how and at what point headcount is assessed and this might not be straight forward given the increasing range of atypical working arrangements in the modern workplace. For example, should only full time employees be included or should part time or temporary workers also be included? What about women on maternity leave? Litigation could also result where there is a dispute about employment/worker status – if a worker is found to have employee status this could propel the employer out of the micro business category.

(ii) The date on which the assessment of whether an employer is a micro business is made. Headcount may change in the period between the employee being recruited and the employee being dismissed. We anticipate that, whatever date the government decides should be determinative, there would be litigation challenging any evidence provided by the employer as to what its headcount was at a particular point in time.

(iii) The genuine reason for the dismissal, and whether it was for a discriminatory or automatically unfair reason.

(iv) Whether any process (if there is any required) has been carried out properly.

(b) The trend for the past few years has been for the number of unfair dismissal claims to decrease. With the introduction of the two year qualifying service requirement for unfair dismissal claims, and the proposal of the introduction of tribunal fees for employees

bringing claims, we expect the number of unfair dismissal claims to continue to decrease. CNFD may therefore be less important given the decreasing risk to employers of unfair dismissal claims, than previously.

(c) We envisage that the introduction of CNFD will lead to an increase in other types of claims which the employees will not be prevented from bringing, including discrimination and whistleblowing claims. According to government statistics, over half of all current unfair dismissal claims already cite another jurisdiction in them. CNFD is unlikely overall to actually reduce the level of litigation in the employment tribunals, or the cost to the micro business in defending such claims. It may in our view lead to more claims of a different nature, which may actually be more complex and time consuming for the tribunals to dispose of. These types of claims may also be more costly to the employer, as there is no cap on some awards (e.g. discrimination). The rise of claims of a different nature will be exaggerated by the fact that an employer is only obliged to provide employees with written reasons for their dismissal after they have reached the qualifying service for unfair dismissal (two years for employees commencing employment from and including 6 April 2012). We envisage that many employees, who are dismissed for a CNFD and provided with no proper reasons for their dismissal, may infer that an unlawful reason was the motivation behind their dismissal, and this may well result in tribunal claims, spurious or otherwise, against their former employers.

(d) Dismissal and disciplinary processes may not be a major concern for employers and may not be a major deterrent when considering whether or not to recruit more employees. Government research (see page 29 of the Call For Evidence) found that dismissal was not even one of the top ten concerns for employers when hiring employees. The research showed that, of those organisations that claimed employment regulation deterred them from hiring employees, only 1% identified dismissal and disciplinary as the top concern. The top deterrents according to the research are: health and safety, maternity/paternity, tax, NMW, NIC, employer's liability insurance, WTR, sickness absence, time off to train and discrimination. All of these concerns are unaffected by the introduction of CNFD.

(e) The BIS Survey of Business Views on Employment Legislation (BDRC International) (September and October 2011) (referred to on page 6 of the Call For Evidence) suggested that employment regulation put 50% of businesses with fewer than 5 employees off employing more staff, but that this rate dropped to 29% for employers employing 5 to 9 employees and down to 11% for "large businesses". This seems to suggest that employers with experience of employing and managing employees are not as intimidated by employment regulation as the government fears.

(f) Arguably many performance and disciplinary issues will arise within the first year or two years of service. As the qualifying period for unfair dismissal has now increased to two years, this already gives micro businesses up to two years to dismiss without fear of an unfair dismissal claim (again, save for automatically unfair dismissal claims and discrimination claims) and without having to pay any form of compensation. It may be

prudent for the government to wait to see the impact of the increase in the unfair dismissal qualifying period and other changes to employment tribunals before considering the introduction of CNFD.

(g) Following on from (f) above, there is a risk that CNFD will be used by employers to dismiss longer serving employees (with two years or more service) for potentially very trivial reasons (without the need for any real proof of poor performance or misconduct etc.) and the employee would have no recourse to claim standard unfair dismissal. In these situations, for example where a long serving employee under performs following a promotion or change of management/work processes, we can see an incentive for a micro business to dismiss by way of a CNFD, rather than following a potentially protracted performance management process, dismissing, and facing a claim for unfair dismissal. Where CNFD is used, there is no band of reasonable responses test to keep the employer in check as there is in current unfair dismissal law.

(h) Removing the ability of employees who work for micro businesses to claim unfair dismissal will effectively amount to "employment at will". It removes a fundamental cornerstone of employment protection for employees.

(i) The current median unfair dismissal award is only £4,591 (according to government statistics for the year 2010-2011). Depending on the level of compensation, the cost of compensating an employee under these proposals may actually be greater that the average compensation a tribunal may award (albeit, this does not take into account additional legal costs an employer may incur in defending a tribunal claim).

(j) CNFD may lull micro businesses into a false sense of security that they are able to dismiss without the employee making any tribunal claim, when that is not the case (e.g. the employer still cannot dismiss for an automatically unfair or discriminatory reason).

(k) Where a CNFD relates to incapacity or poor performance, there is a risk that there could be potential disability discrimination issues of which the employer may be unaware. For example, failing properly to investigate why an employee has been underperforming or has been ill may result in the employer being faced with disability discrimination claims, including a failure to make reasonable adjustments if the employer has moved straight to a CNFD rather than attempting to deal with the problem first.

(l) Recruitment and retention in micro businesses may be seriously prejudiced by the advent of CNFD, as employees with the choice of working for a micro business with little job security, and a larger employer with better employment protection will select the larger employer. This will likely have ramifications on the productivity of micro businesses.

(m) The introduction of CNFD may discourage business growth as a result of micro businesses with nine employees not wanting to recruit an additional employee and lose its ability to dismiss via CNFD.

(n) CNFD may discourage micro businesses from agreeing to flexible working arrangements where the definition of micro business is determined by headcount and part time employees are of equivalent status to full time employees. If flexible working requests are improperly refused this could lead to additional claims such as sex discrimination.

(o) Given the wide range of potential reasons for a dismissal under a CNFD (including, we have assumed, genuine "no fault" dismissals such as redundancy), a future employer requesting a reference may find it hard to determine which employees were dismissed for genuinely "no fault" reasons (such as redundancy), and those who were dismissed for misconduct. This could lead to employees who have been dismissed by way of a CNFD finding it difficult to secure new employment where the previous employer is unwilling to provide further details surrounding the circumstances of the dismissal (which they are not currently obliged to do).

(p) An employee dismissed for CNFD is limited to compensation as his/her remedy (unless he/she seeks to bring additional tribunal claims), and is deprived of other potential remedies which a tribunal can award such as re-instatement, re-engagement, or a declaration. It is acknowledged, however, that there is not a significant take up of these alternative remedies when complaints are made to the tribunal.

(q) The introduction of CNFD may lead to employees demanding more money to settle additional claims to which the employer remains exposed. It may raise their expectations of compensation levels given that if dismissed for CNFD they will already be entitled to a compensation payment and any other contractual payments, including notice and accrued holiday pay.

2.2 The definition of a "Micro Employer"

The definition of a "Micro Employer" would need to be very carefully drafted. The key issues which would need to be addressed are outlined below.

2.2.1 Associated Employers

(a) The definition of Micro Employer would need to extend to any "Associated Employer" of the Micro Employer, to ensure that companies within a group structure do not abuse the micro business exemption.

(b) We do not consider that the current definition of Associated Employer in Section 231 Employment Rights Act 1996 ("ERA") would require amendment. Although we accept that there have been occasions where the definition has been found to be lacking, for example where companies do not come within the legal definition of "Associated Employers" but are in practice controlled by common owners (such as a husband and wife in the case of *South West Launderettes Ltd v Laidler* [1986] IRLR 305), in the context of the determination of continuity of employment that definition has, for the most part, served well in the recent past.

(c) To amend the definition of Associated Employer in Section 231 of the ERA would constitute a major legislative change. We consider that an amendment to the definition of Associated Employer solely because of the introduction of CNFD would be unnecessary given the comments in (b) above.

2.2.2 The date for assessment

(a) We consider that there should not be a fixed date on which the assessment of whether or not an employer is a Micro Employer should be made.

(b) Any fixing of an assessment date (whether it is fixed at the date of employment, date of notice, date of termination or otherwise) would leave scope for abuse. For example, if the date of assessment was the date of termination, an employer with 9 employees at the date of termination may dismiss someone for CNFD one day, when it has the intention of hiring two more employees the very next day.

(c) The most straightforward option would be to crystallise the headcount test at the Effective Date of Termination ("EDT"). The EDT is a familiar reference point used to determine many issues in employment law, including continuity of service in unfair dismissal claims. However, an alternative approach may be to mirror the approach in the Employment Protection (Consolidation) Act 1978. In brief, this would mean that whether or not an employer was a "Micro Employer" would depend on whether or not at any time, during the period of the employee's employment, the number of employees employed by the employer, added to the number employed by any Associated Employer, exceeded [10]. If it had, then it would not be a Micro Employer. Headcount may change significantly in the period between the employee being recruited and the employee being dismissed, and this may be exaggerated by the increasing range of atypical working arrangements in the modern workplace. Such a definition may therefore deter businesses from manipulating the rules and decreasing headcount just prior to termination of the employee's employment.

2.2.3 How to assess headcount

(a) Assessing whether or not an employer has ever employed more than 10 employees during an employee's period of employment may not be straightforward, particularly where the employee has a long period of service and/or the employer has a large number of atypical working arrangements. It may be difficult to create certainty around who is included in the headcount assessment. As previously mentioned, this may well be an area where we would see satellite litigation and so a simple headcount test would be needed to minimise any such satellite itigation.

(b) The definition would need to deal with the following working arrangements, and clearly state whether or not such individuals are to be included within the headcount:

(i) Part time or other flexible workers;

(ii) Women on maternity leave or employees on other forms of leave (e.g. parental, paternity, long term ill health, sabbatical);

(iii) Employees on fixed term contracts (for example to cover maternity or sickness absence);

(iv) Bank staff; and

(v) Agency workers.

(c) Although we understand that only employees should be included within the headcount, determining employment status is not always easy (see in particular the recent case of *Autoclenz Ltd v Belcher* [2011] IRLR 820). There may be scenarios where a consultancy arrangement or an agency arrangement is deemed to create an employment relationship. As we have previously noted, there could be satellite litigation on this point should CNFD be introduced. If a consultant/agency worker is found to have employee status this could propel the employer out of the micro business category.

(d) The definition would also need to consider whether employees who, at the date of termination, are under notice should be included within the headcount (we assume they would be).

(e) Including part time employees or other atypical non full time employees within the headcount may discourage businesses from agreeing to flexible working requests (which if improperly refused could give rise to additional claims such as sex discrimination).

2.3 Should a process be put in place for CNFDs?

In looking at whether there should be a prescribed process which an employer should follow, the following more detailed questions have been considered:

(a) Should an employer have to make a positive choice when treating a dismissal as being a CNFD? Or is it simply a matter of making the appropriate payment of compensation when the decision to dismiss is being made?

(b) What changes to employment legislation will need to be made and how should this be combined with an appropriate code/guidance for a Micro Employer wishing to make a CNFD?

(c) Should the law be different for performance, redundancy and conduct dismissals, as all the government discussions have been about performance-related dismissals?

(d) Any observations as to how the proposals would inter-play with gross misconduct dismissals and payments in lieu of notice?

2.3.1 Should an employer have to make a positive choice when treating a dismissal as being a CNFD? Or is it simply a matter of making the appropriate payment of compensation when the decision to dismiss is being made?

As set out in section 2.1.2 above, we have assumed that that an employer would have to make an express choice or election.

How payments would be calculated is still unknown but express 'election' should be required if an employee is to be given clarity as to the basis for the termination of his/her employment and also to enable the employee to check he/she has been paid the appropriate amount due under any CNFD process that is put in place.

Similarly if an employer is to receive the protection that it seems a CNFD is intended to provide we believe the employer should have to confirm expressly that they are in fact terminating on the basis of CNFD.

It would be helpful for the government to produce some form of precedent letter or document for an employer to give to the employee on termination of employment to confirm that the termination is on the basis of CNFD.

Such clarity may help avoid claims being filed unjustifiably for alleged discrimination and/or claims pursuant to other statutory rights where an employee is simply not informed as to why his/her employment is being terminated (see below).

2.3.2 What changes to employment legislation will need to be made and how should this be combined with an appropriate code/guidance for a Micro Employer wishing to make a CNFD?

Legislative changes that would potentially be required depending on whether CNFDs cover all dismissals or just performance-related ones.

Employment Rights Act 1996

- **S92 – Right to written statement of reasons for dismissal:** will the employer who takes advantage of a CNFD still be obliged to give reasons for dismissal?
- **S98 – Fairness:** would a CNFD constitute a new reason for dismissal?
- **S98A – Procedural fairness:** would have to be disapplied to a CNFD.
- **S111 – Complaints of unfair dismissal to employment tribunal:** this would need amending to prevent claims where a CNFD had been used.
- **S135 – Right to redundancy payments:** the interrelationship between redundancy payments and CNFDs would need to be determined.

Also:

- S136 – Rights re: redundancy; S139 – Redundancy, fair dismissal; S163 – References to employment tribunal; S164 – Claims for redundancy payment; S166 – Application for payments; S167 – Making of payments; S168 – Amount of payments;

Transitional provisions

2.3.3 Should the law be different for performance, redundancy and conduct dismissals, as all the government discussions have been about performance-related dismissals? Any observations as to how the proposals would inter-play with gross misconduct dismissals and payments in lieu of notice?

If CNFDs are limited to performance dismissals then there would be a significant risk that satellite litigation would become as burdensome as unfair dismissal law is now, as employees seek to challenge their employer's reason for dismissal. At the very least we believe the following categories should be covered:

(a) capability i.e. poor performance, but excluding incapacity/ill-health;

(b) conduct, including gross misconduct (but see further below re: gross misconduct); and

(c) some "SOSR" dismissals i.e. those relating to a breakdown in working relationships and personality clashes.

Our reasons are as follows:

(a) It would seem that the aim of these proposals is to assist small businesses in tackling those issues in the workplace that otherwise would be difficult for them to deal with and subject to long drawn-out procedures – this is essentially both performance management and disciplinary issues.

(b) There is no clear-cut rationale for not including conduct dismissals within the same rules as performance dismissals, other than the fact one is arguably fault-based and the other not. Other than in the case of gross misconduct, the employer currently has to follow a very similar drawn-out procedure including: investigations, hearings and a series of warnings prior to dismissal, before dismissal will fall within the range of reasonable responses. Typically, the whole process from start to finish can take a number of months in either case, during which the small employer can be left with a disenchanted and demoralised employee that they have to work with on a daily basis. That said, this would then extend CNFD to fault-based dismissal and so it would no longer arguably be described accurately as a 'compensated no fault dismissal'.

(c) If performance is included on its own, who defines what amounts to poor performance as opposed to misconduct? Small businesses already struggle with the difference between

'can't perform' and 'won't perform' and sometimes it isn't easy to tell which applies, even for the lawyers. Not including conduct dismissals within the CNFD process would therefore be likely to increase, rather than decrease, the likelihood of employment tribunal claims. If restricted to performance dismissals, how widely should performance issues be defined? For example, poor timekeeping and poor attendance are both traditionally conduct issues but should they come within poor performance because of the immediate impact they have on the business?

(d) If performance is included on its own, looking at it from an employee's perspective, how can it be fair and equitable that a poor performer who tries hard but just can't make the grade loses their job quicker (and with no recourse to the ET for standard unfair dismissal) than one who is disruptive, has an attitude problem, etc and has to be put through a full disciplinary process and a series of disciplinary warnings that can take several months (and who can then still claim unfair dismissal at the end of it)? In addition, from an employer's perspective, surely it's more important to get rid of the troublesome employee who is at fault rather than the genuine poor performer? Our experience is that small businesses have to tackle many more misconduct issues than they do capability issues.

(e) If performance is included on its own, in the absence of a change of job role (such as on promotion, etc), poor performance is an issue that employers should be picking up long before the employee has acquired the two years' continuity of employment necessary to claim unfair dismissal and, therefore, in most cases it can be dealt with within that timeframe anyway. Therefore, in practice, how much would CNFDs actually achieve if they only extend to poor performance? How many employees are currently dismissed for poor performance where they have exceeded the threshold necessary to claim unfair dismissal, which is now two years? Of the unfair dismissal claims brought before employment tribunal, what percentage has poor performance as the ground for dismissal?

(f) Similarly if performance is included on its own, when an employee applies for a new job and has to provide a reference and/or an explanation for their reason for leaving their last employment, if CNFD is stated as the reason the prospective employer will know that the applicant had his employment terminated on grounds of capability.

(g) SOSR categories have been included because those are also cases that a small employer finds difficult to deal with in the absence of any actual performance or conduct issues on the part of the relevant employee – there is no guarantee that these types of relationship breakdown or personality clashes are going to be held to be fair on SOSR grounds and yet they can have a significant impact on the daily running of a small business.

Other categories of dismissal (redundancy, other SOSR dismissals, contravention of law dismissals) are less clear cut because, in all cases, the small employer can normally effect a fair dismissal by following due procedure within a matter of weeks – they do not involve long drawn-out processes taking many months, and a significant time investment, to complete.

Provided the decision to dismiss is then within the range of reasonable responses, the dismissal will be fair.

We have included gross misconduct dismissals because, although that does not involve a drawn-out procedure, we did not feel that it could be carved out as separate from other types of conduct dismissal (and ditto the same for cases of gross negligence). In this case, the employer would effectively have the choice: go through a formal disciplinary procedure and dismiss for gross misconduct/gross negligence with no payment but with the risk of a standard unfair dismissal claim being brought, or go for CNFD and make a payment in lieu of notice (PILON) and the compensation element of CNFD but with no risk of a standard unfair dismissal claim. This would be a business/financial decision for the employer. In most clear-cut cases of gross misconduct, the small employer is likely to opt for the disciplinary route (as that is the route of least cost) but in those cases which are not so clear cut, they may well select the CNFD route. This is how we see CNFD inter-playing with cases of gross misconduct/gross negligence.

2.4 What level of compensation should be paid in respect of a CNFD? Should the level be subject to a maximum weekly earnings cap, some form of fixed amount, or a redundancy formula? How should this sit alongside statutory redundancy payments? What age discrimination issues could arise in connection with establishing an appropriate level of compensation?

The logical starting point must be to try and set the level of compensation at a sum that provides sufficient compensation for an employee who has lost their job as there will be no business reason for an employer to use a compensated no fault dismissal ("CNFD") where the employee has less than two years' service - but also one which is affordable to business. If the sum is set too high the process will be unaffordable to employers; if it is set too low the scheme will be seen as simply providing companies with a legitimate method by which they can ride roughshod over the rights of their employees. It would also lead to more insecurity amongst employees with potential consequences for growth in the economy.

With that in mind, the CNFD scheme would be troubling were it to reduce the rights held by employees under their contracts of employment.

Therefore, the first principle must be that an employer wishing to dismiss an employee under CNFD would be obliged to pay an employee all contractual and/or statutory rights to which they would be entitled were their employment terminated by the employer in other circumstances where the employee is not at fault.

There must also, of course, be an additional element of compensation for the employee.

We consider that an employee should retain statutory redundancy rights when dismissed under a CNFD. This would have the effect of providing for an increased entitlement for the longest-serving employees, who may well be affected more by the loss of their employment.

One problem with statutory redundancy entitlements is that in many cases the weekly earnings

cap falls well short of actual salaries. Therefore, we feel that a significant element of compensation should be calculated on actual salary.

A sum equivalent to two or three months' gross salary might represent an appropriate balance. Alongside notice and statutory redundancy pay, we would hope that such a sum would provide a dismissed employee with a decent cushion whilst trying to find new employment. Two months is also the very minimum period we would expect a proper and fair capability procedure to take in cases of an employee who has sufficient service to claim unfair dismissal (it is noted that the government envisages the scheme primarily being used in situations where capability is an issue).

Naturally, using statutory redundancy entitlements in CNFDs is likely to provide for lower entitlements for younger employees, but the government has reasoned that it is appropriate to retain redundancy entitlements despite the prohibition on age discrimination.

We consider that the above mitigates the problem of an employer faced with redundancies who may seek to engineer a situation where the least amount of compensation is due; if the employer wants to pay redundancy entitlements only, all they need do is follow a fair procedure (albeit that they will then be faced with the risk of facing a Tribunal claim - they may seek to avoid this by using a CNFD).

Using the CNFD scheme should oblige an employer to provide the dismissed employee with at least a basic reference setting out details such as dates of commencement and termination, job role, and salary without the fear that positive comments might be used against the employer at a tribunal.

As mentioned above, we assume the compensation entitlement under a CNFD should be paid tax free up to the usual £30,000 limit. This comes at no extra cost to the employer, but provides a potentially significant benefit to the employee. In addition, the unfair dismissal compensation which CNFDs would replace, benefits potentially from the tax free element.

2.5 Impact on other types of claims - what is the likely impact of the introduction of CNFD upon other types of claims such as discrimination? How will all of this affect redundancy law and practice?

2.5.1 Discrimination claims

As mentioned above, it seems inevitable that the use of CNFDs will result in employees who believe that they have been treated unjustifiably, bringing discrimination claims where, in reality, they have been unfairly dismissed.

We believe that by using CNFDs, micro employers may be tempted to cut what they see as unnecessary/troublesome legal formalities/corners and problems. There is a danger that many micro employers will use CNFDs inappropriately and attract unwanted (and perhaps

unnecessary) litigation as a result. Micro employers might become confused and cease to use CNFDs which may become discredited.

In particular we believe that if CNFDs are introduced then micro employers may initially, without necessarily taking advice, see these as an opportunity to avoid:

(i) redundancy and TUPE consultation problems by dismissing staff in advance (or even after) a transfer of the undertaking;

(ii) problems associated with discrimination and harassment conflicts perhaps on the basis that there are 'conflicts of personality' or a similar explanation;

(iii) problems associated with the investigation, disciplining and supervision of staff who are not performing well/properly – perhaps for reasons associated with a disability/age etc.

We know that any issue over protected characteristics and unlawful discrimination cannot be dealt with by a CNFD due to European law. Whether protected characteristics are involved is not always clear even to an expert. We suggest that this will either deter employers from using CNFDs or create unforeseen liabilities for ill-informed employers.

Conversely, we suggest that the immediate natural thought of every employee who becomes the subject of a proposed CNFD (once they are over the shock) will be, "why me". Unless the employee concerned is given a coherent reason for their dismissal it is easy to see that every possible unlawful reason for the dismissal will be suspected.

We assume CNFDs would not cover breach of contract, holiday pay and any other claims which might only become apparent after the CNFD dismissal.

On balance, therefore, we are concerned that the introduction of a CNFD risks promoting more not less discrimination claims.

2.5.2 Redundancy law and practice

It is unclear whether or not it is proposed that CNFDs would cover redundancy situations (see above).

So long as some care is taken and the reasons for the dismissal are genuine it is already easier for a small employer to dismiss by reason of redundancy. With very small employers the decision not to continue with some particular area of the business or process or to combine jobs is often enough – again as long as a little care is taken with the procedure. Perhaps most importantly, it can all be arranged relatively quickly.

Accordingly, subject to cost and given our concerns associated with CNFDs it is difficult to see how CNFDs will assist small employers making employees redundant. Much will depend upon

how the compensation is calculated and how certain the small employer will be that there will be no unpleasant consequence to using the CNFD procedure.

2.6 Observations as to what has occurred in other jurisdictions where something similar to a CNFD process has been introduced?

2.6.1 Australia

Provisions to lower the burden of unfair dismissal legislation on small businesses have existed in foreign jurisdictions for some time. In particular, the BIS Call For Evidence makes reference to the Australian system.

In 2005 the Australian federal government passed a bill excluding businesses employing up to 100 employees from the application of unfair dismissal laws. This exclusion was however narrowed down to small businesses of fewer than 15 employees in 2009. The exclusion is governed by the Australian Small Business Code (the Code), which came into operation on 1 July 2009.

The Code provides that a small business employer (defined as a business that employs fewer than 15 employees) can fairly dismiss an employee without notice or warning when the employer believes on reasonable grounds that the employee's conduct is sufficiently serious to justify immediate dismissal.

In cases other than summary dismissals, the small business employer must first give the employee a reason why he or she is at risk of being dismissed. The reason must be a valid reason based on conduct or capability. The employer must warn the employee and provide them with an opportunity to respond to the warning and give the employee a chance to rectify the problem.

In terms of procedure, the employer must provide evidence of compliance with the Code if the employee makes a claim for unfair dismissal to Fair Work Australia. Evidence may include a completed checklist, copies of written warnings, a statement of termination or signed witness statements. If a small business employer can show Fair Work Australia that they followed the code when they dismissed the employee, the employee's application will be struck out.

It appears that the Code may not be as successful as originally intended and some commentators believe that the Code is not working and needs to be changed to help business.

The Council of Small Business of Australia reports that unfair dismissal laws are forcing small businesses to pay 'go away money' to dismissed employees. Figures show that in the nine months to March 2011, there were 1,876 claims to Fair Work Australia relating to small businesses. Only two complaints by employees were struck out because the employer had followed the dismissal Code.

According to an adviser to the Council of Small Business of Australia, businesses pay between $5,000 and $15,000 to settle claims because it is too time-consuming to fight them. She says that

the vast majority of claims by employees are speculative because it is so cheap and easy for employees to lodge a claim. As a result, employers feel it is easier to pay "go away" money.

Low success rate in small business employers fighting claims suggests that the system may not be working.

There is another possible issue in respect of the Code, namely the lack of detailed step by step guidance, which might put small businesses at risk of being unable to demonstrate "reasonable grounds" for believing the employee to be guilty of serious misconduct, that they had a "valid reason" for dismissal or that they gave the employee a "reasonable amount of time" to improve.

The current BIS proposal is for a compensated no fault dismissal for micro businesses, which we believe addresses from the outset one of the main problems encountered by Australian businesses, namely employees' bringing speculative claims, as a system of dismissal with compensation in full and final settlement would prevent employees from bringing speculative claims.

We consider that the UK model would have to go beyond the Australian Code, a one-page document that we believe fails to provide proper guidance on its practical applications. We consider that it would be essential to provide detailed and accessible guidance to micro businesses on how to implement the non-fault dismissal process so as to avoid potential claims by employees.

2.6.2 Germany

Looking at another European jurisdiction, a different approach has been adopted in Germany where businesses with fewer than ten employees were made exempt from the need to provide cause when dismissing an employee from 2004. The system is a significant reduction on the otherwise heavy regulatory burden on businesses in Germany.

Germany has the lowest unemployment rate in Europe and increased the employment rate level from 66% in 2001 to 71% in 2010, though it is difficult to know whether the exemption contributes to small businesses and new start up businesses taking on more staff.

Members of the Working Party:

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