Compensation for Loss of Pension Rights in Employment Tribunals

Response from the Employment Lawyers Association

20 May 2016
Introduction

1. We are writing to you on behalf of the Employment Lawyers Association ("ELA") in response to the Consultation published on 30 March 2016 on ‘Compensation for Loss of Pension Rights in Employment Tribunals’ ("the Consultation Paper"). The Employment Lawyers Association (ELA) is an unaffiliated and non-political group of specialists in the field of employment law. Our membership includes those who represent and advise both employers and employees. It is not our role to comment on the political merits of proposed legislation, rather we make observations from a legal standpoint.

2. ELA’s Legislative and Policy Committee is made up of both Solicitors and Barristers who meet regularly for a number of purposes; including to consider and respond to proposed new legislation.

3. An ELA working group was set up by the Legislative and Policy Committee under the co-chairmanship of Robert Davies and Anthony Korn to consider and comment on the Consultation Paper. A full list of the members of the working group is set out in the Appendix. Our response is set out below.

4. At the outset we would wish to acknowledge the considerable amount of work and effort that has gone into preparing the Consultation Paper and the clear and concise proposals for reform set out in that document.

5. You will be aware that ELA was invited to participate in the pre-consultation process and in this context we would refer to the attached letter we wrote to Employment Judge Potter on 25 January 2016 setting out our views at that stage, many of which are reflected in ELA’s response to the 9 questions raised in the Consultation Paper. Our response focuses on those 9 questions.

Question 1

The working group proposes that the tribunal operates a default assumption that claimants will retire at state pension age, with the onus on the parties to persuade the tribunal to depart from it by terminating loss before or after that age. Please say whether you agree or disagree, explaining why.

While selecting state pension age as the "default" date for terminating loss may have the advantages of certainty, ease of calculation and saving of costs, ELA has a degree of concern about elevating this into a presumption which does not reflect either the legal requirements regarding retirement or, increasingly, "real life" experience.

Since the abolition of the default retirement age, employees are legally entitled to work beyond "retirement age" if they wish, and such an assumption could be regarded as discriminatory.

Furthermore, evidence suggests that 1,410,000 workers in Britain were working beyond the state pension age in 2011. Consequently, it is reasonable to assume that a considerable proportion of successful claimants will intend to work beyond the state pension age (even though the state pension age is increasing incrementally). In particular, workers who are presently aged under 35, for socio-economic reasons, are likely to have to work longer to finance mortgage payments. Conversely, in some industries and sectors, early retirement remains common, particularly where there has been
ELA is therefore concerned that having a default assumption that all employees will work until their state pension age could result in unfairness to both claimants and respondents in a number of cases. ELA respectfully suggests that rather than operating a default assumption, the claimant should be required, in their schedule of loss, to state their intended retirement age (supported by evidence, where available). It would be open to the respondents, in an appropriate case, to challenge that evidence and for the Tribunal to then determine a just and equitable period of loss.

**Question 2**

The working group proposes that the tribunal operates a default assumption that claimants will suffer no loss to their state pension, with the onus on claimants to persuade the tribunal otherwise. Please say whether you agree or disagree, explaining why.

ELA agrees with this proposal, subject to one particular caveat in the final paragraph of this section below.

ELA’s principal reason for welcoming the proposal that underlies Question 2 is that the amounts involved in issues relating to the loss of the state pension are normally small and it is both inconsistent with the overriding objective and, arguably, disproportionate for time (and money) to be spent on the lengthy calculations that can ensue if the suggested assumption are not adopted.

Although there may be some cases where a claimant could show that as a result of their dismissal, they will be unable to build up sufficient national insurance contributions to qualify for the full state pension, our view is that these cases will be the exception rather than the rule. The qualifying requirements of 35 years’ national insurance contributions already allow for periods of unemployment and so we agree that the starting presumption should be that loss of employment would not have any negative impact on state pension entitlement.

However, there may be relatively rare cases where those issues of loss of state pension are of significant practical effect for claimants, and such claimants may be elderly and of limited means (and therefore unlikely to be represented). Tribunals should therefore be alert to identify those cases where injustice may arise in applying the assumptions made in Question 2 and this should be reflected in the Presidential Guidance.

**Question 3**

The working group proposes that the tribunal operates a default assumption that claimants will suffer no loss of additional state pension rights, with the onus on claimants to persuade the tribunal otherwise. Please say whether you agree or disagree, explaining why.

ELA agrees with this. Following the abolition of contracting out on 5 April 2016, individual earners no longer accrue additional state pension. It therefore follows that loss of employment would not be expected to impact on additional state pension entitlement. (ELA’s understanding is that consequently it would only be in circumstances of a period of loss pre-dating 6 April 2016 and where the successful claimant was ‘contracted in’ that this head of loss could be relevant, by virtue of the operation of the relevant transitional measures.)
Question 4

The working group proposes that the tribunal operates a default assumption that claimants will suffer no loss by reason of losing the facility to make employee contributions (including AVCs), with the onus on claimants to persuade the tribunal otherwise. Please say whether you agree or disagree, explaining why.

ELA agrees with this proposal. Although it might be argued by some claimants that there would be some inconvenience in losing access to a workplace pension savings vehicle for voluntary pension saving, this will not always be the case and claimants might reasonably be expected to mitigate their loss/inconvenience by joining their new employer's pension scheme or establishing a personal pension.

In addition, many contract based pension schemes (such as group personal pensions) and some of the main auto-enrolment schemes like NEST, are designed to be "portable" meaning that employees can continue to contribute to them even once their employment with the employer who established the scheme has terminated. In some cases, therefore, loss of employment would not automatically result in loss of the ability to pay voluntary contributions into an existing pension policy.

Even in cases where the AVC facility is not "portable" and the claimant has to stop contributing because of their dismissal, there are a number of ways in which claimants could be expected to mitigate their loss, for instance by joining their new employer's pension scheme or by setting up a personal pension. Following the introduction of increased regulatory governance for DC schemes, we believe there is now much greater consistency across personal and workplace pension arrangements as regards charging structures (with further regulation to come, directed at phasing out practices such as over-charging deferred members) and so, consequently, it is less likely that a claimant would decline to make alternative provision even if the intention had been to increase levels of AVCs in line with longevity of service and seniority.

Question 5

The working group proposes that the tribunal operates the following default assumptions in a simple DC case where the contributions method is deployed:

- The claimant was an eligible jobholder in the job from which he or she was dismissed and was therefore entitled to be auto-enrolled.

- The claimant did not opt out of the scheme into which he or she had been auto-enrolled.

- In the context of any successful mitigation of loss through finding future employment, the claimant would remain an eligible jobholder entitled to be auto-enrolled.

- The claimant would not opt out of that scheme either.

- In the context of assessing future pension loss, the claimant would need to give credit for employer contributions from the hypothetical future employer at the mandatory minimum level.
If the claimant wishes to claim additional pension loss, for example by contending that the respondent would have paid more than the mandatory minimum level of contributions, as a result of membership of a more generous DC scheme, he or she bears the onus of persuading the tribunal.

Please say whether you agree or disagree, explaining why.

ELA has some reservations about this proposal because whilst it is correct that there is a broad definition of those who qualify for automatic enrolment, the focus on minimum contributions under the statutory scheme risks understating the loss of pension and/or may produce a result which is at odds with the prevailing facts. Automatic enrolment is a fall back right where other pension provisions are not already payable. Those other pensions are likely to be more generous than the statutory scheme. Furthermore, the auto-enrolment regime is in its infancy, as it were, and there are questions as to how many contracts of employment in fact provide for auto-enrolment in practice. Therefore it may be argued that it is too early to construct and rely on the proposed assumption.

On the other hand, ELA acknowledges that the ‘assumption’ is rebuttable by evidence, therefore overall, whilst the proposed assumption may be regarded as a sensible "starting point", we believe, for the reasons given above, that there may be many cases where the ‘assumption’ will be rebutted on the evidence. For instance, although "opt out" rates have been relatively low, it remains to be seen whether the forthcoming increases in the minimum levels of employee contributions, combined with continuing low wage inflation, will affect that.

ELA would also suggest that in practice Tribunals should be careful to ensure that the above assumptions should not operate to the detriment of, in particular, unrepresented claimants who may not appreciate the potential significance of pensions as a head of loss and might therefore neglect to produce evidence in cases where, for example, their former employer paid higher contributions than the statutory minimum.

Finally, it is not clear from the Consultation Paper whether it is proposed that Tribunals should be given guidance about how to account for the effect of tax relief and investment returns when calculating DC pension losses. For younger claimants in particular the expected impact of investment returns over the period between contributions being made and retirement age can be material. In cases where there has been a material delay (say, 18 to 24 months) between the employee's dismissal and the award of compensation, loss of investment return may need to be compensated.

In the light of these reservations, ELA would suggest that if this assumption forms part of the Presidential Guidance, its impact is kept under review and that the Presidential Guidance directs Tribunals to consider the points raised above.

**Question 6**

The working group proposes that the tribunal operates the following default assumptions in a simple DB case:

- Reliance only on the contributions method, meaning no award for loss of enhancement of accrued pension rights.
If the claimant successfully mitigates loss through finding future employment with comparable DB benefits, or the tribunal expects the claimant to do so, there will be no loss of pension rights beyond the start date of the new employment.

If the claimant successfully mitigates loss through finding future employment with inferior DC benefits, or the tribunal expects the claimant to do so, then (unless a complex approach is merited) the tribunal will adopt the same assumptions about auto-enrolment as set out in relation to DC schemes.

Please say whether you agree or disagree, explaining why.

ELA has strong reservations about this proposal not least because the assumption will apply to the great majority of cases other than those which fall within the ‘complex’ category. Whilst ELA recognises the need for a method of calculating pension loss which gives parties certainty and which is manageable for Tribunals to operate without incurring unnecessary cost, basing compensation for loss of DB pension on the employer contributions will result in very many claimants being undercompensated for their loss.

This is because employer contribution rates are impacted by a number of factors, including the demographics of their pension scheme, the pension scheme trustees’ views of the strength of the employer’s covenant and the investment strategy of the scheme. This should be contrasted with the cost to a claimant of purchasing “replacement” pension benefits by means of an annuity, which is mainly driven by wider economic conditions (and also includes an element of the insurer’s profits).

In addition, there are material differences between average employer contribution rates (and the balance of the funding cost between the employer and employees) as between the public and private sectors. In the public sector, the rate of employer contributions is generally lower for comparable benefits in a private sector DB scheme. Further, the new employer “cost-capping” mechanism set out by the Public Service Pensions Act 2013 means that employer contributions to public sector DB schemes will remain relatively stable, whereas in the private sector there is no such upper limit on pension contributions.

Further, paying compensation in lump sum form is also likely to be unattractive to respondents, and could unfairly penalise them, as it is very different from how employers would more typically fund for DB pensions. When an employer promises its staff a future pension of, say, 1/80th of their salary for each year of service, the employer and pension scheme trustees work out the immediate cost of providing this future benefit using assumptions which take account of expected investment return and various other factors which could affect the ultimate cost (for instance, the expected mortality rate and early retirement rates). There is a marked contrast between this approach and a proposal to base compensation entirely on the value of employer contributions and to pay such compensation as a lump sum.

Also, we would repeat the point made in our response to Question 5 above regarding unrepresented Claimants, particularly those who are older and have made contributions for a long period of years (who potentially may have substantial claims).

Taking these factors into account, although ELA agrees that the balance of convenience may still fall in favour of simplicity of calculation in an appropriate case, for example where there is positive evidence that unemployment is likely to last for less than 12 months and future employment is likely to
involve the same or a similar DB (the example quoted in the Consultation Paper at paragraph 96 regarding the position of an individual teacher is a good example of the type of case that ELA has in mind), ELA also considers that Tribunals need to be cautious about classifying cases as "simple" when they involve DB pensions. We therefore do not agree that "most" DB cases ought to be classed as simple.

As stated above, in ELA’s view, a calculation methodology based on employer contributions may be appropriate where the period of continuing loss is likely to be short (for example, in public sector cases where the claimant is likely to find re-employment in a similar role to that which they have lost) or where the operation of the compensation cap makes detailed debate about pension loss a moot point.

In other cases, ELA proposes that the Tribunal should be cautious about classifying cases as "simple" and should encourage the parties to seek to agree the question of pension compensation between themselves before the Tribunal would resort to using such an approximate method of calculating loss as the contributions method.

**Question 7**

The working group proposes that the tribunal adopts the following approach in complex cases:

- **Cases with a realistic prospect of the tribunal making a significant award for loss of pension rights would be identified at an early stage, through a telephone preliminary hearing, and have a split liability/remedy hearing.**

- **If the claimant succeeded at the liability stage and there remained a realistic prospect of a significant award for loss of pension rights, there would be a two-stage remedy hearing:**

  - The purpose of the first remedy hearing would be to enable the tribunal to set the figures for non-pension loss and to make findings on areas relevant to the calculation of pension loss (following which the parties would be given a time-limited opportunity to agree the quantum of pension loss).

  - In the absence of agreement, the tribunal would proceed to a second remedy hearing to finalise the figures for pension loss. There would be two preferred approaches: (a) the Ogden tables approach using a discount rate of 2.5%; or (b) more rarely, the actuarial expert approach.

  - There would be active consideration of judicial mediation. Please say whether you agree or disagree, explaining why.

ELA supports the proposal for a split liability and remedies hearing in cases involving complex pension issues. In fact, we would go further and suggest that in all but the very simplest cases involving DB pensions, this approach ought to be the norm. It is in neither party's interest to spend a potentially disproportionate amount of time and money calculating pension liability in detail until liability has been established. In this context, we would query whether it is realistic or proportionate for claimants to detail their claims for pension loss in a schedule of loss before liability has been
determined, not least because they may not have the relevant information on which to base their calculations.

In addition, ELA supports the proposal for active consideration of judicial mediation. This is because, once liability and the expected period of continuing loss have been established by a Tribunal, our experience is that this can give the parties the confidence they need to have a meaningful discussion about calculating and compensating for pension loss. As mentioned above, judicial mediation may also be attractive to respondents (and claimants) because it would be open to the parties to agree to an augmentation to the claimant's deferred pension in the respondent's pension scheme, rather than being faced with a potentially considerable award of financial compensation. The Presidential Guidance may usefully make this observation – effectively encouraging parties to explore the scope for a suitably cost effective mechanism to resolve the dispute.

ELA has, however, concerns about the proposal for a two stage remedy hearing in those cases where judicial mediation and/or discussions between the parties does not result in a settlement (which may be relatively rare in practice) and the proposed actuarial methodology to be applied by the Tribunal in such circumstances.

Our primary concern about the two-stage remedy is hearing is that there is a risk that if this becomes standard practice (as we assume it would do if it forms part of Presidential Guidance), this would unnecessarily add to the length and cost of the hearing. ELA believes that a pro-active approach to case management following the liability hearing will often obviate the need for two remedy hearings and that the utilisation of two remedy hearings should not become the norm.

Furthermore, a difficulty with the preference for use of the Ogden tables with a 2.5% discount (as set out in paragraph 138.1 of the Consultation Paper) is that the discount is recognised to be unrealistic in the current market and to have been unrealistic for some time. The result is that a rate of 2.5% discount currently significantly exaggerates the likely return on investments and therefore potentially leads to the award undercompensating the claimant for future loss.

In addition, it should be recognised that the use of the Ogden tables is just one actuarial method of calculating the loss and ELA believe that it should be for the parties to at least be able to seek to determine which actuarial method is appropriate in the particular circumstances: actuaries spend their professional lives producing answers to the relevant questions on pension loss once the basic facts have been determined and those answers are likely to be more accurate than the results of tribunals applying the Ogden method. Unrepresented parties are unlikely to understand, let alone calculate their loss on an Ogden basis.

ELA therefore considers that the proposed Presidential Guidance should recognise that the Ogden tables are just one way of calculating the loss and that Tribunals should not be too ready to rule out obtaining actuarial advice, particularly not purely on grounds of assumed cost in terms of pension loss. Although ELA acknowledges that there would be a cost associated with instructing a joint actuarial expert to advise the Tribunal on quantum of pension loss, it should not be assumed that these costs are prohibitive without further enquiries first having been made. In particular, where a private sector respondent operates a DB pension scheme, that DB pension scheme must already have a scheme actuary (this is a statutory role and the office holder will be a professional actuary, independent from the sponsoring employer). The scheme actuary or a representative of their firm would therefore, in many cases, be well placed to provide an expert assessment of the quantum of
the pension loss. In other words, the costs of actuarial assistance in practice may not necessarily be disproportionate to the value of the potential losses in question.

Finally, ELA agrees with the proposals on joint funding of experts set out in paragraph 138.2 of the Consultation Paper although concerns have been expressed that this could disadvantage certain claimants (and with a minority view within the ELA group that the majority of the costs should be borne by the unsuccessful respondent).

**Question 8**

Do you have anything further to say about the working group’s proposal for a distinction between “simple” and “complex” cases? What additional guidance do you believe should be given about when to choose one approach over the other?

In ELA’s view, the guidance on distinguishing simple and complex cases will be crucial to the success of the proposed measures. We would welcome more focus in the proposed Presidential Guidance on the particular "hallmarks" of a "simple" or a "complex" case. The 2003 version of the current guidance refers to three factors in favour of the ‘substantial approach which may be relevant in distinguishing between the two categories: the length of time the claimant has been employed, the stability of the employment and whether the claimant has reached an age where he or she is less likely to be moving on to ‘pastures’ new. The application of this guidance was considered in *Griffin v Plymouth Hospital NHS Trust [2010] IRLR 962*, *Orthet Ltd v Vince Cain [2004] IRLR 857* where the EAT considered that the substantial loss approach may be more appropriate where the period of loss is more than two years; and *Sibbit v The Governing BFody of St Cuthbert’s Catholic Primary School ([EAT/0070/10]* where the EAT indicated that a substantial loss approach is appropriate where a claimant is in employment which is of a stable nature and had been so employed for considerable time (23 years) and the employment is of a stable nature.

Factors which might make the “simple” approach appropriate would be where the period of loss is relatively short (6 – 12 months) because the claimant has, or is expected to, return to a role which offers comparable pension benefits. This may be the case in many public sector claims, for instance. Alternatively, where a respondent has taken steps to close their DB pension scheme to accrual in the period between the dismissal and the hearing, the period of loss for the DB pension could be relatively easily determined.

**Question 9**

What examples would you like to see in Presidential guidance to assist parties and unrepresented litigants in understanding the proposed revised approach to calculating loss of pension rights?

Any examples or guidance intended to be used by unrepresented claimants will need to be clear and concise and focus on the key messages, in order to maximise the chances of them being understood. Where possible, we recommend that the guidance be written in plain English and without using too much specialist “jargon”.
Worked examples to be included in the Presidential Guidance might include:

- claimant whose former employer offered a DC pension with auto-enrolment minimum contributions, who finds a new job within \([x]\) months with identical pension provision.

- claimant whose former employer offered a DC pension with higher than minimum contributions and who finds a new job within \([x]\) months with auto-enrolment minimum contributions.

- claimant whose former employer offered a DB pension and who is expected to find another job with a DB pension within \([x]\) months (perhaps giving examples of sectors where this may be anticipated, particularly focusing on the public sector (and possibly in a separate section devoted specifically to public sector consideration)).

- claimant whose former employer offered a DB pension and who is not expected to find another role with a DB pension.

- young (say under 35) claimant facing a short period of loss having lost participation in a DC scheme but with the prospects of obtaining entry to a new DC scheme with a new employer.

- claimant closer to retirement facing a longer period of loss having lost a DC scheme but with the prospects of obtaining entry to a new DC scheme with a new employer.

- young (say under 35) claimant facing a short period of loss having lost participation in a DB scheme but with few prospects of obtaining entry to a new DB scheme with a new employer but with prospects of entering a DC scheme such as auto-enrolment.

- claimant closer to retirement facing a longer period of loss having lost participation in a DB scheme with few prospects of obtaining entry to a new DB scheme with a new employer.

- claimant who has lost the ability to participate in DC or DB schemes and with very few prospects of ever being able to benefit from another occupational pension scheme, such as in cases where disability makes future employment in any capacity very unlikely.
Appendix – list of working group members

Hannah Beacham, Gowling WLG
Robert Davies, CMS Cameron McKenna LLP
Anthony Korn, No. 5 Chambers
Richard Lee, Gowling WLG
Adrian Lynch Q.C., 11 KBW
Paul McAleavey, Brahams Dutt Badrick French LLP