Appendix 1 - Extract from LGA employment relations advisory bulletin 653

Comments

Although this case was about unfair dismissal compensation, a fundamental element was about the interpretation of a week's pay in accordance with section 221 of the ERA. This concept of a week's pay applies to not only unfair dismissal compensation but across several rights including redundancy pay, holiday pay under the Working Time Regulations 1998 and also some collective rights such as protective awards for failure to consult under the Trade Union and Labour Relations (Consolidation) Act 1992.

We have not been able to determine whether the University of Sunderland is appealing but in any event it will be some time before a higher court considers this issue. So while one might question the basis on which the EAT has moved away from the conventional approach and may also have some concerns about the now differential treatment between those employees who are members of a pension scheme and those who are not, authorities must be aware of this judgment and be prepared to act accordingly. This means either following the ruling or being prepared to challenge it. In this respect we set out below how it may or may not impact on statutory holiday pay and redundancy pay.

Holiday pay

Holiday pay would not seem to be a problematic issue generally as an employee taking holiday continues to be a member of the pension scheme. Both the employee and the employer continue to make pension contributions and we would assume that this would satisfy the requirements of the Working Time Regulations 1998. Regulation 16(1) states that "A worker is entitled to be paid…, at the rate of a week's pay in respect of each week of leave". A tribunal following the Drossou ruling is likely to take on board the approach that the 'payment' need not be paid only to the employee and the continued payment of the employer contribution to the pension scheme will satisfy that aspect of the obligation. Alternatively, they might take the approach in regulation 16(5) whereby any contractual remuneration paid to a worker in respect of a period of leave goes towards discharging any liability the employer has to pay holiday pay. However, that logic does not follow through to any payment of Working Time Regulations holiday pay on termination.

Redundancy pay

Statutory redundancy pay is calculated in accordance with the week's pay provisions of the ERA, subject to a cap which is currently £489. Accordingly, following the Drossou approach would mean that employer pension contributions would have to be factored into statutory redundancy pay. However, in terms of any enhanced redundancy pay local authorities have the means to mitigate the effects of this decision by making it clear, if not already so, that such payments do not include any sum in respect of employer pension contributions.

In respect of enhanced redundancy payments the Local Government (Early Termination of Employment) (Discretionary Compensation) (England and Wales) Regulations 2006 ("the 2006 Regulations") provide authorities with the power to go beyond the statutory maximum week's pay and base redundancy payments on a figure up to actual week's pay. Many authorities utilise this discretion to base redundancy payments on an actual week's pay.

Regulation 5 *Power to increase statutory redundancy payments* provides:

5.—(1) Compensation may be paid in accordance with this regulation to a person who is entitled to a redundancy payment under the 1996 Act on the termination of his employment.

(2) The amount which may be paid must not be more than the difference between—

> (a) the redundancy payment to which he is entitled under Part 11 of the 1996 Act; and
>
> (b) the payment to which he would have been entitled if there had been no limit on the amount of a week's pay used in the calculation of his redundancy payment.

This regulation therefore has the effect that an authority can limit payments to the statutory maximum, or base them on actual pay or choose any amount in between, i.e. the policy could state an amount lower than the full actual week's pay.

Until the Drossou case the notion of a week's pay was restricted to wages/salary and most authorities which applied this discretion simply choose actual week's pay.

Following the Drossou judgment authorities would be advised to revisit their discretionary policies in order to assess whether it has any impact. For example, if the policy statement has lifted directly from Regulation 5 and refers to a week's pay calculated in accordance with the ERA but without a limit on the amount, then the effect of the Drossou case would be to lift the actual pay by including pension contributions. If authorities do not wish to make such additional payments we would recommend amending the wording and stating more explicitly how any payment would be limited by for example expressly stating which elements of pay will be included and/or stipulating that payments by way of pension contributions will not be included.

This review should also include the authority's policy on lump sum compensation payments under Regulation 6 Discretionary Compensation. Regulation 6 provides a separate but associated power, i.e. it allows an authority to make payments of compensation in the event of redundancy or in the interests of efficiency of the service which must not exceed 104 weeks' pay (in the event of redundancy this payment also incorporates the statutory redundancy payment and any enhancement made under Regulation 5). Again, for the limit of 104 weeks' pay the notion of a week's pay is to be calculated in accordance with the provisions of the Employment Rights Act. Therefore, authority policies might use different formulations and policies should be checked for references to week's pay and any implications as in some cases amendment might be advised for clarity.

Calculating employer's pension contributions

It is relatively easy to apply the logic of the Drossou case in the context of a defined contribution scheme where the employer makes a very explicit contribution to the employee's personal pension fund as the contribution is easily identifiable. However, the basic principle raises difficulties within a defined benefit scheme such as the Local Government Pension Scheme where employer's contributions are based on regular evaluations of the financial state of the scheme and are not made on an individual basis, and include administration costs and costs based on assumptions made against the scheme design, e.g. ill health retirements.

Having said that, if having identified situations where the conclusion is that the employer's pension contribution needs to be included, a big question that the EAT failed to address remains, which is, what is the value of the employer's pension contribution? In a scheme like the LGPS the employer's pension contribution is an amalgam of the future service cost (i.e. the cost of each year of pension rights built up for each year of employment going forward) and the past service adjustment (being an adjustment, up or down, to cover any funding deficit or overprovision in respect of pension rights already accrued). It is also a composite figure (i.e. the true cost for a 20 year old is much less than the cost for a 50 year old – but the employer pays a rate that reflects the overall age profile of its pensionable workforce. So, given those factors, what would be the "employer pension contribution" in respect of the individual employee?

It might seem convenient for a tribunal to assume that the composite figure represents the employer's pension contribution to the individual's pension as this might be set out in compensation and benefits or total reward statements. However, it may require further cases to clarify this and there may be legitimate arguments to be had about inclusion or non-inclusion of elements of payments in relation to past service deficits. Employers may choose to pay these off by cash or percentage of payroll and over different periods of time. One may choose 3 years in which case the cost will be higher than an employer which chooses a repayment period of say 20 years. It seems questionable as to whether the employer's strategy should affect an individual employee's week's pay.

Further issues may also arise in relation to any Additional Shared Cost Voluntary Contributions (AVCs) or Shared Cost Additional Pension Contributions (APCs) which also can be paid over varying periods of time and questions remain as to how these might be valued.

Given the complexity of the issues it is difficult to give precise advice at this stage and we will continue to consider the issue and observe developments. As stated we would advise that authorities should review their discretionary policies and take any steps necessary to minimise any implications and advise us if they have any particular points or questions.