

U.K. Severance Pay and Age Discrimination

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At a Glance

The U.K. age discrimination regime came into force on October 1, 2006, and continues to generate case law at an impressive rate. This Stay Current summarizes recent age discrimination decisions relating to enhanced severance payments. This topic is of increasing relevance in the current economic climate, as reductions in force/redundancies proliferate.

We also briefly highlight a critical compliance date in relation to the new U.K. immigration regime. This is of importance to those persons within employers who are responsible for managing U.K. work permit/visa applications.

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1. Key Date – New U.K. Immigration Regime

The U.K. Government has recently announced that Tier 2 of the new Points Based System will become active from the end of November 2008; the current work permit scheme will close from that date. Employers wishing to ensure that they are able to continue to employ non-EU/EEA foreign nationals in the U.K. after November this year should register with the U.K. Border Agency as a sponsor by **October 1, 2008.**

The registration process will include an audit by the U.K. Border Agency of an employer's current employees' immigration status. Given the time-intensive process and the large numbers of applications likely, it may take some time for employers to become authorized. It is therefore critical that U.K. entities intending to hire foreign nationals or renew work permits for current employees seek immediate advice.

2. Employment Equality (Age) Regulations 2006

The UK implemented the age strand of the Equal Treatment Directive through the Employment Equality (Age) Regulations 2006 (the "**Regulations**"). The Regulations prohibit direct and indirect age discrimination, harassment and victimization on the grounds of age. Employers can avoid liability for direct

and indirect discrimination if they are able to prove that any age-discriminatory impact was objectively justified – that it was a "proportionate means of achieving a legitimate aim." There is also a specific exemption in the Regulations for enhanced redundancy pay schemes. This requires such schemes to be based on the statutory redundancy pay formula, but allows some limited scope for extension.

3. Enhanced Redundancy Pay

(i) *MacCulloch v Imperial Chemicals Industries PLC*

In *MacCulloch v Imperial Chemicals Industries PLC* (UKEAT/0119/08), the Employment Appeal Tribunal ("EAT") considered whether payments made under an enhanced redundancy scheme, which were based on age and length of service, directly and indirectly discriminated on grounds of age. The EAT held that although the Employment Tribunal ("ET") had identified certain legitimate aims of the scheme, it had not properly addressed the question of proportionality.

Ms. MacCulloch (aged 36) was made redundant after seven years' service at Imperial Chemicals Industries PLC ("ICI"). She received a redundancy payment of just over 55% of her gross annual salary. Ms. MacCulloch claimed both direct and indirect age discrimination, arguing that she would have received a larger redundancy payment if she had been older (the direct discrimination claim) or had a longer period of service (the indirect discrimination claim, as length of service is necessarily related to age).

The ET dismissed both claims. The EAT upheld Ms. MacCulloch's appeal on the grounds that, while the ET had identified certain legitimate aims of the scheme, it had not properly determined if the measures adopted were a proportionate means of achieving those aims.

The EAT held that the ET had not erred when it:

- considered ICI's scheme as a whole, rather than its effect on Ms. MacCulloch;
- held that a payment relating to years of service would encourage loyalty, despite the service element of the payment not increasing after ten years' service; and
- held that one of the scheme's aims was assisting older employees to leave employment, by providing a greater financial cushion. Ms. MacCulloch had argued that this aim was tainted with age discrimination, but the EAT held that the ET had not found the aim was simply to encourage older workers to leave. Rather, it had been to encourage turnover and prevent "blockages" in employee flow, which was a legitimate objective.

The EAT commented that when considering proportionality, the ET should have asked whether the means ICI used to achieve identified aims were proportionate, having regard to the detrimental effect on individuals such as Ms. MacCulloch.

(ii) *Loxley v BAE Systems Land Systems (Munitions & Ordnance) Ltd*

In *Loxley v BAE Systems Land Systems (Munitions & Ordnance) Ltd* (UKEAT/0156/08), the ET decided that an enhanced redundancy scheme was not discriminatory on the grounds of age. The scheme contained provisions for a payment calculated on the basis of age and length of service. The amount tapered downwards after an employee attained the age of 57. Employees aged 60 or over received nothing under the scheme, but were instead entitled to a full unreduced pension. The tapering originally prevented those aged 60 receiving a windfall, as they would otherwise have received both pension and enhanced redundancy payment.

The normal retirement age was subsequently increased to 65, as was the normal pension retirement age – meaning that the windfall justification was less clear cut. Employees could still take a pension from 60, but this was now reduced by 4% per annum before 65.

The ET held that the scheme did have a legitimate aim (ensuring that those employees who were entitled to a pension after their redundancy did not receive a windfall) and that the steps taken to achieve this were proportionate.

The EAT disagreed, concluding that, while it was potentially justifiable to exclude from a contractual redundancy scheme those employees who are entitled to immediate pension benefits, and to use tapering provisions, the ET had not properly considered the issue of proportionality. The EAT therefore remitted the matter to be reheard by a fresh ET.

(iii) Galt and Others v National Starch and Chemical Limited

In *Galt and others v National Starch and Chemical Limited (ET/2101804/07)* the ET held that an employer had failed to justify its use of enhanced redundancy payments - again calculated on the basis of age and length of service.

When National Starch and Chemical Limited ("NSCL") decided to close one of its operating sites, it offered enhanced redundancy terms to the workforce so that employees received three weeks' gross pay for each year of service aged under 40, and four weeks' pay for each year aged over 40. Mr. Galt and a number of other colleagues claimed that the enhanced scheme treated them less favorably than older employees.

While the ET found that NSCL operated the scheme to achieve a legitimate aim (namely, the avoidance of potential industrial unrest), the majority view of the ET was that the

discriminatory impact was disproportionate to the aim being achieved. Mr Galt and others had therefore been subjected to unlawful discrimination.

Comment:

None of the above cases featured enhanced redundancy schemes compliant with the specific exemption in the Regulations, and therefore all three employers had to rely on the objective justification defense. The cases illustrate the need for employers to show that, when implementing pay policies, they have tried to balance the interests of the business against any age discriminatory impact on their employees – and in doing so have examined alternative options. Other recent cases regarding age discrimination and pay practices demonstrate that those employers which have involved third party advisers to assist in the balancing exercise are more likely than others to be able to justify any discriminatory impact if challenged. Furthermore, a high level of preparation and data appears to be necessary in order to persuade a court that the justification defense has been made out.

4. Share Plans

(i) *Hung v Kellog Brown & Root (UK) Limited and Halliburton Company*

In *Hung v Kellog Brown & Root (UK) Limited and Halliburton Company (ET/2305257/2007)*, Dr. Hung, who was a UK employee of a UK subsidiary, KBR UK, was entitled to participate in a share plan operated by the US parent company ("**Halliburton**"). Under the US share plan, departing employees could keep their share awards if their combined age and years of service equaled at least 70 years. Dr. Hung claimed that the rule was age discriminatory. The ET ruled at a preliminary hearing that the US parent might be liable for unlawful age discrimination only if the ET, at a full hearing, found that the parent's age plus service rule and/or operation of the share plan aided unlawful age discrimination by the UK

subsidiary employer.

The ET reached this conclusion because, given the definitions of "employment" in the Regulations, Dr Hung was an employee of KBR UK and not an employee of Halliburton. Consequently, an ex-employee of an overseas parent working in the UK might be able to bring a successful claim for unlawful age discrimination if deprived of a share award, but an ex-employee of a UK subsidiary of the parent might not be able to bring a successful claim in the same circumstances.

This issue will not be resolved until the full hearing of the claim. The ET will also have to determine the true meaning of the restricted stock and option agreements, whether those

agreements were governed by Texas law, and, if so, whether that choice of law was displaced by applicable English mandatory employee protection rules (specifically, the Regulations).

Comment:

Rules in share incentive plans that treat departing employees more favorably on the basis of age, retirement or length of service (or any combination) have been expected to give rise to age discrimination claims from ex-employees who do not benefit from them. Very often, such plans are operated by the U.S. parent company. It will be interesting to see whether, and how, the U.S. parent might be liable under the Regulations for discriminating against employees of a subsidiary.



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