

<b>Title:</b> Legislative proposals to promote equal pay <b>IA No:</b> GEO 1029  <b>Lead department or agency:</b> Government Equalities Office	<b>Impact Assessment (IA)</b>	
	<b>Date:</b> 04/30/2012	
	<b>Stage:</b> Final proposal	
	<b>Source of intervention:</b> Domestic	
	<b>Type of measure:</b> Primary legislation	
<b>Contact for enquiries:</b> David Ware Tel: 0207 035 3355		
<b>Summary: Intervention and Options</b>		<b>RPC Opinion:</b> AMBER

Cost of Preferred (or more likely) Option			
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANCB on 2009 prices)	In scope of One-In, Measure qualifies as One-Out?
£-0.03m	£-3.8m	£0.4m	No
			N/A

**What is the problem under consideration? Why is government intervention necessary?**

Equal pay remains a key concern in the UK. Despite a legal framework around equal pay being in force since 1975, there is still a significant gender pay gap, and continuing evidence of non-compliance with the law in the public, private and voluntary sectors (estimated 32,000 claims per year in employment tribunals). Individually enforceable rights such as the right to equal pay do not always enable employees to challenge wider or systematic unfairness in pay and reward by their employers. Therefore, as part of a broader package of measures aimed at tackling the gender pay gap, government intervention is necessary on equal pay enforcement to ensure that employers who are found to breach the law take the necessary corrective action to ensure that they do not continue to do so.

**What are the policy objectives and the intended effects?**

The overall objective of these particular measures is to ensure that employers, who have breached equal pay law, correct any remaining gender pay inequalities within the workforce, and to supplement the voluntary approach to equality reporting, which GEO is separately developing with business organisations, as outlined in the Government's Equality Strategy<sup>1</sup>. It is also an objective to avoid needless burden on business, where recommending a pay audit is not appropriate.

**What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)**

Government has considered a range of measures to improve transparency in pay matters and strengthen enforcement of equal pay law, to complement a general voluntary approach to equality reporting, including pay.

**Option 1: do nothing.** This relies on employers taking suitable corrective action following a finding.

**Option 2 (preferred): require an employment tribunal to impose pay audits except in particular circumstances.** This would target intervention in cases where there has shown to be a need for corrective action to be used, and it would make best use of the information available.

Instead of the general voluntary approach to equality reporting, including option 2 as presented above, Government also considered requiring employers of 150 employees or more to carry out mandatory pay audits. This approach was considered to be excessively burdensome on employers who are compliant with the law.

<b>Will the policy be reviewed?</b> It will be reviewed. <b>If applicable, set review date:</b> 04/2019					
Does implementation go beyond minimum EU requirements?				N/A	
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.		<b>Micro</b> No	<b>&lt; 20</b> Yes	<b>Small</b> Yes	<b>Medium</b> Yes
What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)		<b>Traded:</b> N/A		<b>Non-traded:</b> N/A	

**I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.**

Signed by the responsible Minister: \_\_\_\_\_ Date: \_\_\_\_\_

<sup>1</sup> The Equality Strategy - Building a Fairer Britain (December 2010); <http://www.equalities.gov.uk/pdf/GEO%20Equality%20Strategy%20tagged%20version.pdf>

# Summary: Analysis & Evidence

# Policy Option 2

**Description:** Require an employment tribunal to impose pay audits except in particular circumstances

## FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2012	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: -0.25	High: 0.19	Best Estimate: -0.03

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	N/A	0.47	4.14
High	N/A	0.47	4.14
Best Estimate	0.10	0.47	4.14

### Description and scale of key monetised costs by 'main affected groups'

There may be small transitional costs to the Tribunals Service of implementing these proposals that has been estimated as at most £100,000.

There would also be annually recurring costs to private and voluntary sector employers whose settlement behaviour is affected by the increase in the expected cost of proceeding to a hearing of £440-445,000.

The annually recurring cost of remedy hearings to the Exchequer is estimated at £24-29,000.

Note: Cost of imposed pay audits or remedy hearings to employers are not included as these would only be incurred by those found to be in breach of equal pay law

Note2: The increased costs to employers are incurred only by those choosing to settle an equal pay case, and are therefore the result of implied non-compliance with equal pay law. Hence, this measure is out of scope for the purposes of OIOO.

### Other key non-monetised costs by 'main affected groups'

There may be a small loss in transparency if equal pay cases are settled rather than receiving a judgement at hearing because employers wish to avoid the risk of an audit being recommended. This impact should be minimal as a claim which is successful at hearing does not guarantee increased transparency unless non-claimants in the workforce then challenge the pay structure further.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	N/A	0.45	3.88
High	N/A	0.48	4.32
Best Estimate	0	0.46	4.10

### Description and scale of key monetised benefits by 'main affected groups'

As a result of the impact on employer settlement behaviour, both in terms of higher payments and a reduction in the number of claims progressing to a hearing, there will be benefits to the following groups:

Individuals: Annually recurring - £440-445,000

Exchequer: Annually recurring - £12-32,000.

### Other key non-monetised benefits by 'main affected groups'

The principal benefits of this measure are to individuals where the imposition of a pay audit will correct pay systems and provide equal pay, both to the individuals themselves, and the groups they represent. Where pay audits identify widespread pay inequality that was not previously known of or expected pay audits may help employers avoid future equal pay cases.

Key assumptions/sensitivities/risks

Discount rate (%)

3.5

- The estimated, average cost of a conducting a pay audit is presented in Annex 1
- The possibility of an equal pay audit being imposed following a finding increases the ability of the claimant to negotiate a higher settlement award from an employer
- There will be a reduction in the number of claims proceeding to a hearing by 10-25% as a result of the increase in incentive for employers to reach settlement. A broad range has been used to account for uncertainty about the exact nature or size of this impact.
- Of the 29-35 annual equal pay claims where claimants succeed at hearing against private and voluntary sector employers, equivalent to approximately 8-9 individual employers, 25% will result in an equal pay audit being imposed, resulting in on average 2 audits being imposed per annum.

## BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: 0.4	Benefits: 0	Net: -0.4	No	N/A

# Evidence Base (for summary sheets)

## Introduction

These proposals have been the subject of public consultation. They were set out in the Modern Workplaces consultation document, and the consultation period ended in August 2011. Over 100 responses were received to this part of the consultation, and meetings were held with a range of business groups and the Trades Unions. In general respondents said they agreed with the underlying principle that greater transparency was needed following a breach of the law, and that pay audits were an effective method of improving transparency. But respondents had doubts about the effectiveness of the proposals, and felt that the threat of audits would persuade employers to settle cases more frequently. Respondents also provided comments on the cost of audits. This impact assessment takes the responses into account. A full response to the consultation document is being published separately.

## Summary of adjustments made to Impact Assessment resulting from public consultation

A number of points raised during the public consultation have been taken into account during revision of this impact assessment. These are set out in appropriate places in the text below, but for convenience the key changes are summarised here:

- Responses to the consultation generally supported the notion that enabling a tribunal to impose a pay audit would increase settlement incentives for employers. However, no responses to the consultation suggested any specific estimate of the magnitude of this effect, and therefore here we have relied on a wide range to reflect this uncertainty about the true size of the impact. We have now estimated that the number of claims that would settle, and subsequently not proceed to hearing, would increase by 10-25%.
- Respondents to the consultation rightly pointed out that while the law of equal pay governs the pay practices of micro employers in exactly the same way as it does large ones, it does not follow that applying an audit requirement to a micro employer would be an effective and proportionate method of improving their pay practices. The proposal will not initially apply to micro businesses.
- Responses to the consultation suggested that the previous estimated average cost of a pay audit was too low. To reflect these comments we have increased the estimated average expected cost to approximately £12,800, by altering assumptions, while recognising that the range of costs would be significant.
- Responses suggested that the cost of legal advice to an employer in equal pay claims had been underestimated. This has now been revised.
- Financial penalties were clearly the favoured option for enforcement of the pay audits proposal – we have taken this preference into account.

## Problem under consideration

The case set out in the original consultation impact assessment was that despite the legal framework around equal pay being in force since 1975, there is still a significant gender pay gap, and continuing evidence of non-compliance with the law. In 2011, the ONS estimated that women working full-time were still paid on average 10.5 per cent less than their male counterparts; if you compare the pay of all men and women in work, including those working part-time, the gap is as much as 20.2 per cent. Research published by the GEO in February 2010 found that one third of the pay gap could not be explained by any observable factors<sup>1</sup>.

A survey of 550 senior HR professionals working in predominantly larger enterprises in 2010, representing around two million employees, found that 16% could not state that there was no material gender inequality of pay in their organisation – 12% thought there was significant gender inequality of pay and 4% stated that they had no way of measuring this.<sup>2</sup>

There is still a large number of equal pay claims (see figure 1) estimated here at 32,000 per annum, the majority of which are brought against public sector employers. These claims, particularly those relating

<sup>1</sup> Olsen, W, Heuvelman, H, Gash, V, & Vandecasteele, L. (2010). *The Gender Pay Gap in the UK 1995-2007*, Government Equalities office

<sup>2</sup> Austerity or Prosperity, The State of HR Survey 2011, Speechly Bircham & King's College London

to work of equal value and those involving a large number of claimants with similar claims (referred to here as “multiples”) can be complex and take considerable time and effort to resolve. It is likely that the number of claims will continue to take up a significant proportion of the resource available to the Tribunals Service; it is also likely that full use may not be being made of the considerable volume of information that has been gathered during a tribunal hearing, and the effort put into that tribunal by all parties. While the immediate claimants have their pay corrected, other employees who may be disadvantaged may still have to raise a claim to have this happen. Steps to prevent these further claims being necessary are therefore desirable.

However, individually enforceable rights such as the right to equal pay do not always enable employees to challenge wider or systemic unfairness in pay and reward by their employer, because the resolution of a single case does not necessarily expose all the gender-related pay inequality within the workforce. Therefore, changes are needed to the enforcement regime so that those who are disadvantaged in this way can bring a claim if the employer does not himself correct the situation. Analysis of a number of judgements in equal pay cases has shown that private sector employers who lose equal pay cases often have no transparency about their pay systems, and indeed are not able to show any clear rationale at all for the pay rates that they offer individuals. Of a sample of 41 successful equal pay judgements over the last decade, primarily involving private sector employers, less than a quarter appeared to have a transparent salary structure.<sup>3</sup> For example in one case the tribunal said that ‘its [the employer’s] failure to monitor and control salary in a completely transparent way led it to create the problem of unequal pay in this case. The respondent created an atmosphere whereby it discouraged employees to discuss their respective salaries. The claimant raised the issue of salary occasionally but in a quiet way.’ In another the tribunal described the employer’s pay practice as ‘opaque’, and said that it was not clear at all to the tribunal how the employer had arrived at the complainant’s and the comparator’s salary. There was no evidence that the company had ever considered the salary structure of its employees. Furthermore, the survey of senior HR professionals indicated that only 58% of organisations had taken steps or made plans to assess or monitor gender inequality of pay.<sup>4</sup>

The Government is committed to supporting voluntary action by employers on gender pay, and the Home Secretary launched a business-led voluntary approach to equality reporting, “Think, Act, Report” on 14<sup>th</sup> September 2011. The Government believes that employers who give the necessary thought to their own position through this voluntary approach are not likely to lose equal pay cases - but where employers do not give thought to their own pay structures, and so lose cases at tribunal, the Government considers intervention to require them to give thorough consideration to their pay systems is justified. The Government has noted concerns raised during the consultation process about the potential effect on settlement behaviour of employers, and issues raised about the proportionality of audit requirements. However, some at least of those employers who settle cases will go on to correct pay inequalities within their systems on a voluntary basis in order to avoid future cases. In other cases, the ordering of an audit will be of real benefit to the workforce of that employer. Government remains convinced that these measures are needed to ensure that where breaches of equal pay law are found to have taken place by a tribunal, employers and the tribunals are given the most appropriate and cost effective tools to correct pay inequality, and mitigate future liability to legal action. A further consultation will be held as proposed in which the content of the audit requirement will be explored more fully, and efforts will be made in constructing that to ensure that proportionality concerns are addressed, and settlement effects minimised.

### **Rationale for intervention**

Government intervention is considered necessary to help ensure that women achieve equal pay where an employer has already been shown to discriminate in this way.

It is right to ensure that those employers who have breached the law once, having taken the matter all the way through tribunal, have learned the right lessons, and to use whatever means possible to help them correct the issues which led to that breach the law.

Failure by employers to correct the factors which might have led to a successful equal pay claim against them following a hearing may leave them vulnerable to future claims. Exposing and dealing with any

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<sup>3</sup> Legal analysis of equal pay case judgements, Government Equalities Office

<sup>4</sup> *ibid.*

remaining inequality immediately may enable them to resolve those issues by negotiation without tribunal process.

Full pay audits are an established way by which an employer can ensure fair treatment of employees. Although currently there is no one agreed form of an audit, the general principles are well established, and can be related to the requirements of the law; however, there is no requirement on employers to conduct such audits.

A further requirement of this kind made on employers in the limited circumstances where they have been found to have breached the law will support the voluntary approach to equality reporting, including pay information, which Government is also proposing. It will also supplement the increased transparency which may result from section 77 of the Equality Act 2010, which made pay secrecy clauses unenforceable where discussions may expose pay inequality.

With this in mind, it is right to limit the imposition of penalties of this kind following a finding to those cases where the imposition will have the desired effects. This means the tribunal considering the case must have some facility, whether of its own discretion or in line with a predetermined standard, not to apply it, and to ensure that what is required will not be disproportionate. Where an employer is acting, as a result of the case or otherwise, to correct his pay structure generally he will be able to argue at a tribunal that no requirement to conduct an audit should be made of him. This will ensure that the requirement will be imposed only where it will add value to the finding itself.

### **Policy objective**

The overall objective of these particular measures is to ensure that employers, who have breached equal pay law, correct any remaining gender pay inequalities within the workforce, and to supplement the voluntary approach to equality reporting, which GEO is separately developing with business organisations, as outlined in the Government's Equality Strategy<sup>5</sup>. It is also the objective to avoid needless burden on business, so employers who have already taken steps to ensure their pay structures are compliant, by undertaking an equal pay audit or otherwise ensuring that their systems are transparent and non-discriminatory, should not be made subject to a further, unnecessary requirement. Similarly there may be some businesses, particularly very small ones, for which an audit might not be helpful.

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<sup>5</sup> The Equality Strategy - Building a Fairer Britain (December 2010); <http://www.equalities.gov.uk/pdf/GEO%20Equality%20Strategy%20tagged%20version.pdf>

## Options

These options should be considered complimentary to government's overall approach to voluntary equality reporting.

**Option 1: do nothing.** This relies on employers taking suitable corrective action following a finding with limited further support.

**Option 2 (preferred): require an employment tribunal to impose pay audits except in particular circumstances.** This would target intervention in cases where there has shown to be a need for corrective action to be used, and it would make best use of the information available.

## Micro enterprises

The Government announced in March 2011 that a moratorium would apply to new regulation within the scope of one-in one-out affecting micro businesses and start-ups, and the consultation document specifically asked questions about applying the audit proposals to smaller and micro businesses. Respondents to the consultation rightly pointed out that the law of equal pay governs the pay practices of micro employers in exactly the same way as it does large ones. But it does not follow that applying an audit requirement to a micro employer who loses an equal pay case will be an effective and proportionate method of improving their pay practices. Therefore the Government's intention, given that the size and complexity of an employer's workforce is recognised as a relevant factor when considering the application of an audit requirement to them, is that the moratorium **should** apply to these proposals – although it is also agreed that the proposals will not in any case come into force during the period of the current moratorium. The Government will review the situation after the proposals have been in operation for some time before deciding whether to apply them to micro employers.

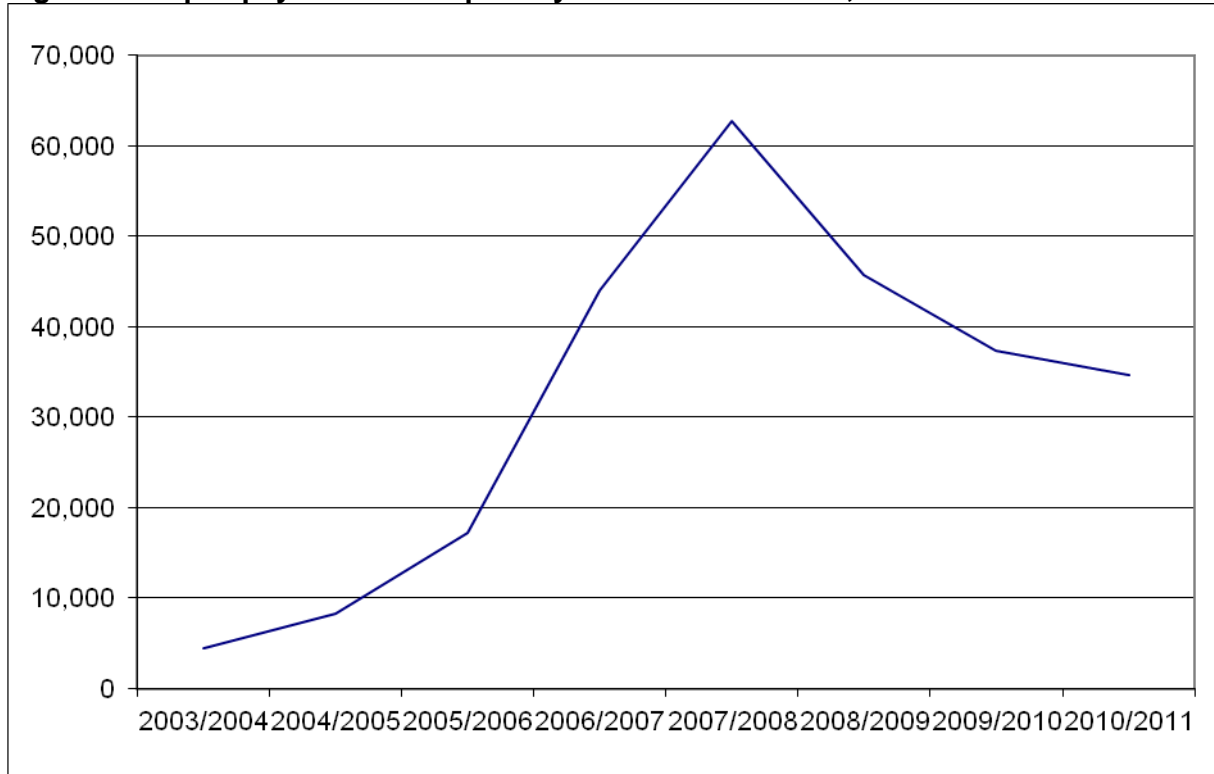
## Costs and benefits

*Throughout this assessment all prices have been inflated to 2012 prices using HM Treasury GDP Deflator Series consistent with 29 November Autumn Statement 2011 unless stated otherwise*

### **Option 1: Do nothing**

In recent years there has been a large surge in equal pay claims (see figure 1). This has primarily been driven by large multiple claims against NHS and Local Authority employers. The rise in NHS claims followed largely from the 'Agenda for Change' programme of pay restructuring. A national agreement from 1997 committing all local authorities in England and Wales to implement 'single status' pay systems by 1 April 2007<sup>1</sup> has revealed anomalies in pay that have contributed to a large number of claims.

**Figure 1 – Equal pay claims accepted by the tribunal service, 2003/2004 – 2010/2011**



*Source: Employment Tribunal Service annual reports and statistics, 2003/2004-2010/2011*

The estimated average number of equal pay claims per annum is 32,000. This has been calculated by taking an average over the past 8 years to account for the large surge in the last few years. There were only 4,400 equal pay claims accepted in 2003/2004, rising to a peak of 62,700 in 2007/2008, and falling to 34,600 in 2010/2011. Whilst surges in tribunal claims do occur, across all jurisdictions, it would not be correct to assume that the recent surge in equal pay claims might be persistent – this surge is largely a result of particular public sector pay restructuring exercises, which have exposed historic inequalities (see table 2 below), and that this effect is unlikely to be replicated elsewhere in the economy. Therefore taking an 8 year historical average is deemed to be a reasonable estimate for the underlying baseline. This provides the best estimate of the expected number of claims per annum going forward, from which we can then consider the number of claims which occur against private, public and voluntary sector employers.

Likewise, the average outcomes of equal pay claims disposed, as listed in table 1, have been calculated as an average over the past 8 years. This method in part accounts for anomalous outcome rates in individual accounting periods. However, in 2005/2006, 33% of claims disposed were successful at hearing, which can be linked to a small number of very large multiple claims against NHS employers, and so this particular period has been excluded from the average to avoid misrepresenting what is typical.

<sup>1</sup> An earlier implementation date of 1 April 2006 was set for Local Authorities in Scotland

**Table 1 – Percentage of equal pay claims disposed reaching stated outcome**

	Percentage reaching outcome
<b>Total that reach hearing</b>	<b>4.0%</b>
<i>Of which...</i>	
<i>Successful at tribunal (claimant)</i>	2.0%
<i>Unsuccessful at hearing (claimant)</i>	1.9%
<b>Total that settle</b>	<b>50.8%</b>
<i>Of which...</i>	
<i>Privately settled</i>	32.2%
<i>ACAS conciliated</i>	18.6%
<b>Other Outcomes</b>	<b>45.2%</b>
<i>Withdrawn</i>	23.4%
<i>Struck out (Not at Hearing)</i>	19.2%
<i>Dismissed at a preliminary hearing</i>	0.5%
<i>Default judgement</i>	0.0%

Source: Employment Tribunal Service annual reports and statistics 2003/2004-2010/2011, adjusted to account for private settlements using SETA 2008

Over recent years the vast majority of equal pay claims have been against public sector employers. Of the claims with the tribunal service (as opposed to the number which are accepted or disposed in any given accounting period) in 2008/2009 99% are against NHS and Local Authority employers.

**Table 2 – Breakdown of origin of equal pay claims at tribunal, 2008/2009**

	Number of equal pay claims	Percentage of total claims
NHS	28,511	24.4%
Local Government	86,668	74.2%
Other	1,574	1.3%
<b>Total</b>	<b>116,753</b>	

Note: other comprises central government and private sector employers

Source: Tribunals Service

However, this underestimates the exposure of other sectors to equal pay claims as a large number of the claims still with the tribunals relate to large multiples, as previously discussed. Taking the breakdown of the origin of equal pay claims as they occur at tribunal in any particular accounting period may not provide an accurate representation of the likely future exposure of different sectors to equal pay claims, as the judgements in existing cases clarify the effect of the law. Therefore, the estimated breakdown of new claims by sector going forward, as stated in table 3, corrects for the fact that recent statistics have been affected by a specific caseload surge from NHS and Local Government employers.

**Table 3 – Equal pay claims by economy sector**

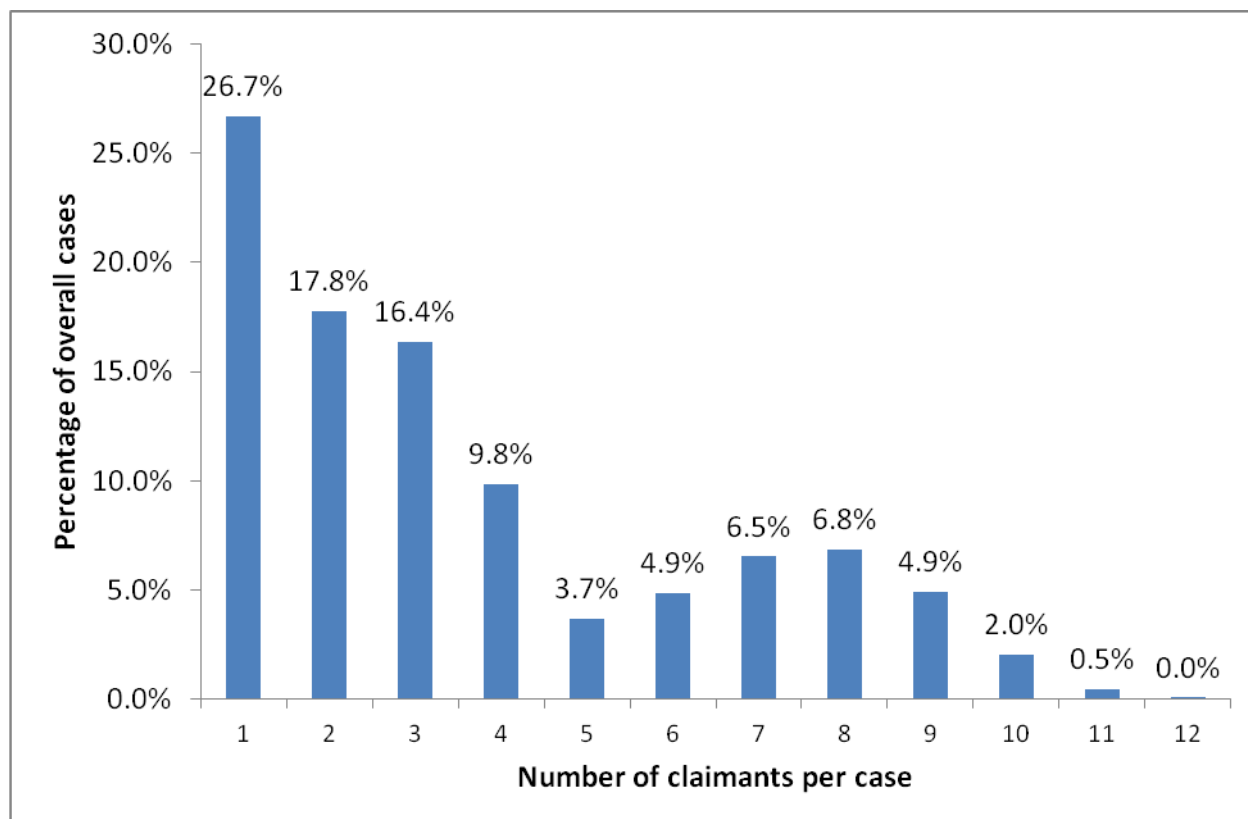
	Percentage of equal pay claims	Estimated Annual Number of Claims
Public Sector	94%	29,899
Private Sector	5%	1,590
Voluntary Sector	1%	318

Source: GEO estimates, Tribunals Service



Equal pay claims are commonly brought as multiples – that is more than one claimant – against the same employer. This is particularly the case for public sector claims, but also true to some extent for claims originating in the private and voluntary sectors. The Government Equalities Office has used Tribunals Service administrative data covering all cases from 1996-2010 to derive an estimate of the average number of claimants per case (employer).<sup>2</sup> This was done by looking at equal pay judgement case numbers, and then comparing the number of unique cases against 1 million unique claimant judgements. Using this methodology there are approximately 3.7 claimants to each case, or employer. It should be noted also that some of these multiples may themselves be sub-multiples in larger cases against the same employer, indicating that this may be a minimum value. Figure 2 below shows the distribution of equal pay cases by number of claimants derived from the Tribunals Service data.

**Figure 2 – Distribution of Equal Pay Cases by number of individual claimants, 1996-2010**



Source: GEO analysis of Tribunal Service administrative data, 1996-2010

Under this option, non-legislative means of supporting employers have also been considered for example:

- Strengthening and updating available guidance with regards equal pay audits which could be distributed to employers who have been found in breach of equal pay law at tribunal
- Signposting employers who breach equal pay law to available information sources and good practice with regards equal pay subsequent to tribunal findings.

However, these non-legislative measures have not been costed because it is considered that they would not materially mitigate the risk of future claims. It is unlikely that, where an employer has been taken all the way to a final hearing in an equal pay case and has not up till that point been able to conciliate the claim or corrected their pay systems, additional signposting or generic guidance will be of benefit.

<sup>2</sup> The data available only enabled us to look at the number of claimants per case. We were not able to accurately assess the number of cases per employer. Hence here we use case and employer interchangeably, whereas in truth, this may have led to a small overestimate of the number of employers typically affected.

## **Option 2: Require an employment tribunal to impose pay audits except in particular circumstances (preferred)**

*All benefits and costs discussed for option 2 are additional to the Do Nothing option, and are direct impacts of the policy options. Annex 2 sets out in more detail the approach we have taken to monetise the costs to individuals, employers and the exchequer of this government intervention, with regards altering incentives to pursue equal pay claims to hearing.*

### Non-Monetised Benefits of equal pay to individuals and others

The main benefits are of businesses and other organisations changing their pay practices to reflect equal pay requirements: these however are difficult to quantify, and have not been monetised in this assessment. This is because the scale of benefits to individuals will depend on the extent to which they are currently underpaid, and the benefits to firms will depend on the amount of unfairness still present in their pay systems, and the extent to which they are able to reduce their exposure to fresh cases by negotiating compliant pay systems. However, there is some evidence that employers do use equal pay audits already, implying that for those who are concerned about unequal pay in their organisation, they can be beneficial. For example, the equal pay reviews survey carried out in 2008 by IFF research stated that 87% of employers who conducted a pay audit did so because they saw it as good business sense.<sup>3</sup> Furthermore, 82% of those who conducted audits did so because they wanted to be seen as good practice employers. Clearly the majority of those who do undertake audits believe there are economic benefits from ensuring equal pay throughout an organisation; for example in demonstrating commitment to staff and to fairness, in ensuring that they are making maximum use of their employees' capacity, and in protecting themselves from the cost of legal action.

The results from the survey of senior HR professionals highlights a difference between the fraction of organisations who highlight that they have no material gender inequality of pay, and the fraction who actually assess or monitor this. The survey shows that many organisations must believe they have no pay inequality without having taken steps to actually check this. As noted above, employers who lose cases appear often do so because they are amongst those that have not considered their pay structures. Employers who have lost cases will be less vulnerable to further cases if they are required to look systematically at what they pay and why.

It has not been possible to quantify the reduction in the number of cases reaching tribunal which will result from the requirement to conduct audits – this is because to do so would require an estimate of the remaining unfairness within the pay structures of non-compliant employers, and this would be very speculative.

There will also be benefits for individuals in the wider workforce of an employer, because the discipline of conducting the pay audit will put the employer in a position where he will have to recognise, and correct, any remaining unfairness in his pay structures. It will enable the employer, by acting before fresh cases are raised, to negotiate settlements without legal action. This will promote equal pay in the workforce where it is needed, and increase fairness in employment, without unfairly burdening good, compliant employers.

Due to the difficulty in robustly quantifying any monetised benefits to individuals and employers from moving closer towards equal pay in the work place, we have included these real benefits only in the non-monetised summary. It should nevertheless be noted that in fair and flexible labour markets, for work of equal value, the demand and supply of labour ought to be the sole factor in determining an equal rate of pay for men and women, and that anything else is evidence of market inefficiencies. Therefore, there must also be real benefits in ensuring equal pay, for which pay audits are useful in identifying the issue and promoting action.

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<sup>3</sup> Equal pay review survey, 2008, IFF research; Equality and Human Rights Commission; [http://www.equality-ne.co.uk/downloads/349\\_Equalpay.pdf](http://www.equality-ne.co.uk/downloads/349_Equalpay.pdf)

### The impact of a tribunal being able to impose a pay audit on employer and claimant settlement behaviour

Employers, their representatives, and other respondents to the consultation suggested that incentives to settle an equal pay case will increase as a result of the proposal due to the increase in the expected cost of a finding of unequal pay. One approach that could be used to assess this impact is as follows:

1. By understanding the factors which affect the expected cost of a pay audit to the employer at the point a claim is brought against them
2. By estimating the increase in the average expected cost of a hearing for an employer from a tribunal being able to impose an audit and equating this to the increase in the maximum amount an employer would be willing to settle a case for.
3. Approximating how claimants will respond to this when negotiating a settlement with an employer
4. By estimating the impact that an increase in the expected cost of a claim for the employer will have on the likelihood of that claim proceeding to a hearing.

We have used this approach in Annex 2 to estimate this impact of government intervention, and monetise costs and benefits to employers, individuals and the exchequer. These impacts have been included within the summary of the costs and benefits of this proposal, including an annual cost to private and voluntary sector employers of around **£0.4million**, but should be treated with caution due to the strength of the assumptions used (Table 4).

### Non - Monetised Costs

Where earlier settlement takes place, the policy would not result in added transparency about pay, and **might** to a limited extent reduce the opportunity for an increase in transparency that would follow from a finding at tribunal. However if the finding was not accompanied by a requirement to conduct an audit, it only brings limited transparency gains anyway. In the absence of an audit requirement no real benefit accrues directly to others in the workforce unless they themselves bring and win a case. However, an employer who settles **may** take some corrective action. It is not possible to quantify this reduction in transparency, and it may offset any overall gains in pay transparency where audits are imposed. This impact will be monitored as part of the overall evaluation of the measure.

### Familiarisation costs

Employers will need to be aware of the fact that an equal pay audit may be imposed if they are found to have provided unequal pay at tribunal hearing. This is expected to be a minimal familiarisation cost on employers, which will be incurred alongside the requirements on employers to become familiar with the wider changes to the Tribunals Service process (and the flexibility at work provisions) expected to be implemented at the same time as this measure.

Furthermore, familiarisation with specific guidance on the specification of and method of conducting an equal pay audit would only be required of an employer where it was imposed. Hence, this has been accounted for in the overall average cost of an audit (see Annex 1).

Therefore, there will be no significant familiarisation costs as an impact of this policy.

### Transitional costs to the Tribunals Service

It is understood that there will be transitional costs and ongoing costs to the Tribunals Service associated with training staff, providing guidance and generally ensuring this measure is enforced effectively. It is expected that these costs would be at most **£100,000**.

The specific detail of the audit requirement that the Tribunal is to impose is to be decided following a further consultation, and will be expressed in secondary legislation, which will be the subject of further impact assessment. Any associated costs would therefore be explored as part of the development of the secondary legislation. We do not expect that the Tribunal will be in the position of having to examine employers systems to design particular structures.

### Increased costs to the Tribunals Service from remedy hearings

Where an equal pay case is successful, there may be an increased cost to the Tribunals Service from increased length of remedy hearings to decide whether or not a pay audit should be imposed. This will arise because Tribunals will need to consider issues around the scope of the audit, evidence as to what has already been done, and representations by the employer. There would be an estimated average of 29-35 successful claims against private or voluntary sectors employers each year, equivalent to 8-9 employers, where the tribunal would have to consider imposing a pay audit. It is assumed that on average, remedy hearings would cost the Exchequer half the amount for a full hearing, and lead to a total increased cost of **£24-29,000** per annum.<sup>4</sup>

[This is based on GEO's own estimate of the burden. A further consultation period is proposed on the content of the audit requirement, and these estimates will be revised as necessary during that process.]

**Note: We do not consider any extra burden to the employer of the remedy hearing because this would only be as a result of proven non-compliance with current equal pay law.**

### New equal pay claims

As a result of this measure, there could be an increase in the number of equal pay claims being made against employers. This could arise as a result of activists, trade unions and some advisers seeking to encourage and support claims with a view to increasing the chance of challenge to the employer's systems. Individuals who might settle on their own account may be persuaded to maintain their challenge through the tribunal process in order that an audit will be imposed, and other employees will be saved from the risk of similar disadvantage. Some new claims of less merit may be raised if employees anticipate that employers will settle more readily as a result of fear of audits. The specific nature of equal pay rights, depending as they do primarily on a factual comparison of work, should keep this effect relatively small. Responses to the consultation did not provide a clear view on whether there would be an overall increase in the number of equal pay claims brought, though employer's representative bodies in particular thought that increased settlement rates could generate some new weak cases to take advantage of perceived unwillingness by employers to fight them. Most responses indicated that the much more probable impact was on settlement behaviour.

### The cost of pay audits where they are imposed following the claimant being successful at a hearing

It is estimated overall that with no impact on the rate of settlement, there will be on average 640 claims successful at hearing each year (2.0% of the estimated 32,000 claims accepted annually). Of the equal pay cases where the claimant is successful at hearing, a small fraction will have been made against private and voluntary sector employers; 39 claims (2.0% of 1,900). We do not consider here claims brought against public sector employers here as the majority made in recent years have followed large scale pay harmonisation exercises, which have been intended to equalise pay.

As stated above, it is expected that a small percentage of those claims which are successful at hearing will result in a pay audit - no more than 25% of claims successful at hearing against private and voluntary sector employers would lead to the imposition of a pay audit.

Hence, it is estimated, taking into consideration the impact on settlement behaviour described above (leading to an estimate of 29-35 claims, against 8-9 individual employers, being successful at tribunal hearing), and adjusting for the number of employers rather than claims, that approximately **2** pay audits (0.006% of all claims) will be imposed annually. The total direct cost of conducting these pay audits to private and voluntary sector employers, using an average cost per audit of approximately £12,800 (see Annex 1 for derivation of audit cost), would be approximately **£26,000 per annum**.

**Note: As pay audits would only be imposed for employers who have been found to be non-compliant with equal pay legislation, these costs have not been included as an impact of the policy.**

### Summary of Costs and Benefits of Option 2

The overall impact of option 2 is a net present value over 10 years of **£-0.25million - £0.19million**.

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<sup>4</sup> [8,9] x £6,170 x 50%

**Table 4 – Summary of Costs and Benefits of Option 2 (£000s)**

	<u>Costs</u>			<u>Benefits</u>		<u>Net Present Value</u> <u>(10 Years)</u>	
	Transitional	Annually Recurring		Annually Recurring		Low	High
		Low	High	Low	High		
Private and voluntary sector employers	0	440	445	0	0	-3,783	-3,830
Exchequer	100	29	24	12	32	-251	186
Individuals	0	0	0	440	445	3,783	3,830
<b>Total</b>	<b>100</b>	<b>469</b>	<b>469</b>	<b>451</b>	<b>477</b>	<b>-251</b>	<b>186</b>

Source: GEO estimates, SETA 2008, Employment Tribunal Statistics, ASHE 2011

Note: Low and High represent the low and high settlement impacts

### **Risks and assumptions of option 2 (preferred)**

There is a degree of risk and uncertainty around the impact of option 2. Firstly, when considering this measure in isolation, as discussed, there is a need to understand the impact on the behaviour of employers. For example, this measure may lead to an increase in employer incentives for and subsequently the rate of, settlement in equal pay claims. The methodology used to assess the cost of government intervention on employers, through the increase in the amount they are willing to pay to settle a case, relies primarily on an assumption that claimants typically have more control over settlement negotiations and are able to negotiate the maximum settlement payment the respondent is willing to pay. This is a strong assumption and therefore the monetised impacts should be treated as illustrative only.

The wider non-monetised benefits to individuals of ensuring employers correct imbalances in pay systems would be less likely to occur if, to avoid the possibility of conducting an audit where a claim is successful, an employer elects to settle instead. Any change in behaviour may result in monetised benefits to individuals, the Exchequer where a claim does not proceed to hearing. There would however also be costs of this. These costs are less easy to monetise, and they relate to the potential fairness in pay achieved for individuals, and the groups they represent within organisations, not being achieved if claims are stopped from proceeding to a hearing.

This measure will potentially be implemented alongside thirteen other measures with a direct impact on the Tribunals Service, on which consultation has been held,<sup>5</sup> and which are dealt with in a separate assessment<sup>6</sup>. Interaction with these measures could ultimately affect the number of pay audits expected to be imposed as a result of this policy.

Of the thirteen concurrent proposals which will impact on the Tribunals Service, a new measure requiring all claims to be submitted to The Advisory Conciliation and Arbitration Service (ACAS) in the first instance, to increase the frequency of pre-claim conciliation, could have a significant impact on what constitutes the typical number of equal pay claims entering the tribunal process. However, responses to the consultation suggested that this would have a minimal impact on equal pay cases because they generally involve relatively complex examination of facts, argument about identification of the appropriate comparator, and identification and argument about circumstances which might justify a difference in pay. It seems unlikely that the relevant facts could be fully established, agreed between parties and considered during a relatively short pre-claim period.

Furthermore, proposals which are intended to deter vexatious or unmeritorious claims, could also impact on the number of claims reaching the Tribunals Service and raise settlement and success rates (though we might expect the overall number or level of settled and successful claims to be largely unaffected).

<sup>5</sup> Resolving workplace disputes: A consultation (January 2011), BIS; <http://www.dti.gov.uk/assets/biscore/employment-matters/docs/r/11-511-resolving-workplace-disputes-consultation.pdf>

<sup>6</sup> The BIS Impact Assessment on proposed changes to employment tribunals is likely to be published after this impact assessment.

If we assume that some fraction of those claims which make up the typical caseload (32,000 claims) will now be pre-claim conciliated, then this consequently reduces the number of claims which might be successful at hearing, and therefore, would potentially reduce the number of instances in which equal pay audits are imposed.

As also mentioned previously, there is no definite expectation of how many successful equal pay claims at hearing will result in an equal pay audit being imposed. We have assumed this might be 25% of successful claims against private and voluntary sector employers, which is likely to be a high estimate, and was not challenged during the consultation.

### **One-In-One-Out (OIOO): Direct costs and benefits to business**

There are no direct costs to business or voluntary sector organisations, as a direct result of this policy, since any costs that might result stem from a breach in equal pay law, or implied non-compliance for those who would seek to settle a case. The costs of audits or remedy hearings on employers ought to not be considered for the purposes of OIOO as they are effectively an additional sanction against non-compliance. Therefore this measure should be considered out of scope of OIOO.

### **Enforcement**

We intend to support the proposal with enforcement by means of the civil penalty regime recently consulted on by the Department for Business, Innovation and Skills in the Resolving Workplace Disputes Consultation. Financial penalties were most favoured by respondents to the consultation, and making use of this regime is likely to be more cost effective than setting up an entirely separate system or criminal offence, and more effective than merely taking a failure to conduct an audit into account. The Government intends to vary the civil penalty regime in equal pay cases so that a civil penalty cannot be awarded when a pay audit is ordered – they will be alternatives. But in the event that an audit requirement is not complied with, the civil penalty regime will come into play. Establishing the regime for use in these cases will therefore have no costs additional to those arising from implementation of the financial penalty regime itself.

### **Monitoring and Evaluation**

#### **Review objective:**

- To establish whether the Equal Pay policy has achieved its primary intention and objectives, including whether or not it increases transparency in pay matters, and how this has worked (process, and observed outcomes and differences).
- To understand the effect Equal Pay policy has had on equal pay claim tribunal outcomes (changes in both process and outcome), and whether this is a positive change.

**Review approach and rationale:** The review approach would be developed more widely in conjunction with other monitoring exercises around the voluntary approach to equality reporting, including equal pay. The review approach will consist of specifically commissioned primary research, monitoring of data sources and the input of evidence from related surveys. There already exists a large quantitative survey of employment tribunal applications (SETA) run by BIS, that provides detailed outcome data from the tribunal process. However, this is not expected to report again until 2013 at the earliest. To avoid duplication of this work, remain proportionate in the review costs relating to demonstrable outcomes, and considering the evidential requirements for this impact assessment, the most achievable research would be of qualitative methodology. To provide comprehensive evidence on the changes to the outcomes and costs of equal pay claim process, the review approach will need to include evidence from a number of different sources. There is an evidential requirement to understand the effect the pay audit has both directly (consequence of undertaking a pay audit) and indirectly (those that proceed through the claim process but did not reach a imposed pay audit or those that changed pre-claim and did not enter the full tribunal process). This is especially important if the review is going to demonstrate behavioural change in employers relating to pay transparency.

The review approach will therefore cover:

- Monitoring of Tribunal Service administrative data and ACAS Annual Reports

- Analysis of SETA data (when available) to understand patterns of change in process and outcomes
- In-depth qualitative evaluation of individuals, employers and stakeholders (such as courts and ACAS) at various tribunal stages of an equal pay claim including:
  - those resulting in a pay audit
  - those that settled part way through a claim
  - those with recent equal pay claim that did not enter the tribunal process (not required due to previous and/or voluntary auditor like action by employer)
- Small qualitative evaluation of audit providers (through ACAS)

Where it is possible, all review work will aim to demonstrate the difference the Equal Pay policy has made directly to equal pay; where this has helped employers provide equal pay moving forward and where this has led to greater transparency. However, due to the very small numbers of businesses that are likely to be required to conduct pay audits it will be challenging to demonstrate the prevalence of these changes in a statistically reliable way, within the three to five year period of the review. We are also aware that many public sector organisations will have carried out a pay audit so the impact of this policy will more likely be on private and voluntary sector organisations. As a consequence evaluation activity will be concentrated in these areas.

**Baseline:** A baseline position is still being established for this policy and as such further baseline information, by which the policy can be compared against, will be set out in a report within the first year of the review, it will contain information on:

- Gender Pay Gap: As indicated in the main body of the impact assessment, the current gap in pay between men and women's full time median earnings is 10.5%.<sup>7</sup> The baseline position for the gender pay gap is further set out in detail in the GEO research report "The gender pay gap in the UK: 1995 to 2007"<sup>8</sup>
- Metrics from Tribunal Service administrative data
- Employment Relations Research Series No.107: Findings from the Survey of Employment Tribunal Applications 2008:<sup>9</sup> Provides a baseline of findings from 2008 (non-specific to equal pay claims although some data tables distinguish claims made under the Wage Act 1986). The report includes data from 2008 on outcomes of tribunals, initial expectations, satisfaction with outcome, and the impact of the tribunal on employer policies. It also contains analysis of data on the cost and benefits of the case for both claimant and employers, broken down by finance, time and non financial costs
- Specific work already being undertaken to further develop evidence sources and improve baseline data. This includes:
  - Gathering and synthesising published information and non-published data such as Tribunal Service and ACAS management data, and a variety of further sources such as academic literature and recent BIS literature review
  - Studying an initial targeted sample of ET judgements in cases not involving local government or NHS employers
  - Extending the usability of uncoordinated and un-compiled employment tribunal judgement data

## **Summary and implementation plan**

Option 2 was chosen as the preferred and most proportionate means of meeting the policy objectives. It will require employers to conduct pay audits only where there has been shown to be a need, placing no significant burdens on the majority of employers, who are not in breach of equal pay law.

Full implementation will follow a further consultation exercise on the secondary legislation which will be necessary to provide the detail of the proposal, though enabling legislation will be put in place when the Parliamentary timetable allows.

<sup>7</sup> ONS, Annual Survey of Hours and Earnings, March 2012

<sup>8</sup> Summary:

[http://webarchive.nationalarchives.gov.uk/20100505211508/http://www.equalities.gov.uk/pdf/GPAYGAP\\_gpg\\_summary\\_FINAL.pdf](http://webarchive.nationalarchives.gov.uk/20100505211508/http://www.equalities.gov.uk/pdf/GPAYGAP_gpg_summary_FINAL.pdf)

<sup>9</sup> <http://www.bis.gov.uk/assets/biscore/employment-matters/docs/10-756-findings-from-seta-2008>

# Annex 1. Unit Costs

Unless stated otherwise, all monetary figures have been inflated to 2012 prices using HM Treasury GDP deflator series consistent with 29 November Autumn Statement 2011

## Exchequer

The average cost of an employment tribunal claim is given my Ministry of Justice’s impact 2011 impact assessment regarding *Introducing a fee charging regime into Employment Tribunals and the Employment Appeal Tribunal*.<sup>1</sup> Equal pay cases are termed as ‘Open Track’ cases for the purposes of administration by the tribunal service. The average cost of receipt and allocation of an open track claim is £420, and the average cost of a hearing is £6,170. These are the core mandatory stage in the employment tribunal process.

## Employers

### Time and Legal Advice

The average costs to employers of an equal pay case are calculated using SETA 2008. The costs for cases where discrimination is the primary jurisdiction have been used to estimate the costs for equal pay cases specifically. The issues within a discrimination claim are generally no less complex than those in an equal pay claim. This is calculated as the cost of advice and representation, time spent by corporate managers and senior officials, and time spent by other employees, namely dedicated personnel, training and industrial relations managers, on the case. Responses to the consultation suggested that the cost to the employer had previously been underestimated. It was suggested that unlike in discrimination cases more widely, employers would pay for some form of legal advice or representation in virtually all cases where equal pay claims were brought against them due to the nature of the issues in consideration. The costs here have been amended to reflect this using SETA data. The median hourly wage is assumed to be £50.63<sup>2</sup> and £27.33<sup>3</sup> respectively for these two roles. The overall average cost to an employer of an equal pay case is £6,556. Note, this cost per employer applies to the average per case, which could consist of multiple or single claimants.

**Table 1 – Cost of an equal pay case to the employer**

Time spent on case by directors & senior staff	£2,126
Time spent on case by other staff	£574
Cost for advice and representation	£3,856
<b>Total</b>	<b>£6,556</b>

Source: SETA 2008, ASHE 2011

Note: Assumes a 7 hour day

### Compensation

The average compensation awarded in discrimination between 2000/01 and 2010/11 in successful discrimination employment tribunal claims is approximately £18,500 in 2011/12 prices. This is considered here to be a proxy for compensation in equal pay cases, which typically consists of up to 6 years back-pay, accounting for the level of inequality in pay discovered.

### The Cost of a Pay Audit

We are aware of no widely-shared understanding of what it would cost to complete a full equal pay audit. Clearly costs to a particular employer would vary depending on how much of the required information had already been gathered and suitably stored, how many employees there were, how complex or varied the work undertaken was, and other factors. The estimates below are therefore based on

<sup>1</sup> <http://www.justice.gov.uk/downloads/consultations/et-fee-charging-regime-ia.pdf>

<sup>2</sup> ASHE, Nov 2011 –111 incl. 21% uplift for non-wage labour costs

<sup>3</sup> ASHE, Nov 2011 –1135, incl. 21% uplift for non-wage labour costs



assumptions that most of the company pay data is already held electronically and can be reasonably easily accessed, and that the mix of tasks undertaken is not unusually complex. We make no allowance for one-off costs to develop systems. Although they are clearly different tasks, we have assumed the same daily charge for external advice as we have assumed would be made by an equal value assessor in an equal pay case.

- Internal time required 8 weeks
- Carried out by a “personnel, training, and industrial relations manager<sup>4</sup>” or equivalent
- External time – 5 days
- Cost per day of external advice, £1,000

Responses to the consultation suggested that the previous estimated average cost of a pay audit was too low. In particular, it should be acknowledged that for smaller and medium organisations, who may not have well defined pay systems or records, they would likely need to put these in some degree of order before an audit could be carried out. To reflect these comments; the assumed length of internal time has been increased here from four to eight weeks.

Given the revised assumptions, the typical cost of an audit would be approximately £12,800<sup>5</sup> to the employer. As consultation responses noted however, it is important to acknowledge that for large employers this figure is likely to be far higher, whilst for some small employers, it could be an overestimate.

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<sup>4</sup> ASHE, Nov 2011 Code 1135, median weekly earnings, incl. 21% uplift for non-wage labour costs; £976.94

<sup>5</sup>  $12,816 = (8 \times £976.94) + (5 \times £1,000)$

## Annex 2.

### Factors which affect the expected cost of a pay audit to the employer

After claims are brought, an employer will seek to settle an equal pay case as soon as possible if they believe the expected costs of proceeding with the case to a hearing outweigh the costs of negotiating and making a settlement now. The expected future cost to the employer currently would be calculated using several factors:

- The expected cost of the employer's time from proceeding with the case to a hearing
- The expected cost of any legal advice and representation needed
- The employer's current understanding of the probability it will lose the case, including whether or not they are risk averse
- If the employer loses the case, the expected amount of compensation it believes it would have to pay
- The cost of any other non-financial negative effects that might be expected from proceeding with the case. E.g. Reputational damage [Note: this cost may be negative, in so far as the expected benefit from proving that an employer's pay systems are compliant at a hearing, may be greater than the cost of the implied non-compliance from settling a case]
- The extent to which the employer discounts future costs relative to more immediate costs

It is estimated using the SETA 2008 that the average of the maximum amount that an employer is willing to settle for at the start of an equal pay case is £11,400 (see Annex 1). This figure should equate to the employer's expectation of all future costs.

As a result of government intervention giving power to the tribunal to impose a pay audit to non-compliant employers, some additional costs would be factored in by the employer:

- If the employer loses the case, the employer's current understanding of the probability that a pay audit would be imposed (and not successfully overturned at appeal)
- If imposed, the expected cost of carrying out a pay audit.

### An increase in the average expected cost of a hearing for an employer and the maximum amount an employer would be willing to settle a case for

The impact therefore of government intervention is to raise the expected cost of proceeding with a case for the employer; where there is a real chance it will reach a hearing. This will increase the maximum amount the employer is willing to state in a settlement offer. To estimate this increase, we calculate the average expected cost to an employer of proceeding to a hearing before and after the government intervention.

The cost of an employer's time and the cost of any legal advice and representation for a case that progresses from initial acceptance by the employment tribunal to a hearing is estimated at £6,566 (see Annex 1). Using table 1, the average success rate of a claimant at hearing in equal pay cases over the last 8 years is 51%. The average compensation awarded for a single claim is £18,500 (see Annex 1). However, as discussed above, a case could consist of multiple claimants, the average being 3.7 claimants per case. Using this, we can estimate that the average, expected cost of proceeding to a hearing for an employer, in a case which has a real chance of doing so, is **£11,210**.<sup>1</sup> This estimated cost does not include some of the non-financial factors mentioned above as it was not possible to find appropriate data or evidence.

After government intervention, the expected cost should also include the cost of carrying out a pay audit. The average cost of carrying out an equal pay audit is estimated at £12,800 (See Annex 1). It is expected that a small percentage of those claims which are successful at hearing will result in a pay audit and it is not envisaged that a tribunal would be empowered to order an audit in such circumstances, where there would be no benefit because any systemic disadvantages have already been exposed and corrected. Audits might not commonly be of use for small employers, and micro

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<sup>1</sup> £11,231 = £18,500 x 51% + £6,556 / 3.7

enterprises will be exempt from this proposal, or where there are clear and transparent pay systems in place. Therefore, initially, we estimate that no more than 25% of claims successful at hearing against private and voluntary sector employers would lead to the imposition of a pay audit.

Therefore the average expected cost of proceeding to a hearing for an employer would increase to **£11,660**,<sup>2</sup> an increase of (3.95%). Applying this percentage to the maximum amount they are willing to settle for on average gives an increase of **£450**.<sup>3</sup> This is an indication of the increase an employer might make to the maximum amount he is willing to pay to settle the case. Whilst the estimates here did not include some of the non-financial factors an employer would take into consideration, these would be largely constant with or without the government intervention and so it is not felt this would affect the derived figure greatly.

### **How claimants will respond when negotiating a settlement**

Currently 50.8% of equal pay cases reach either private settlement or ACAS conciliation. We assume that the ability of the tribunal to impose a pay audit will not alter claimant behaviour in so far as it will not increase the benefits they might receive from a successful judgement. The pay audit would benefit other employees as opposed to the claimant, as their pay would be corrected as a result of the tribunal judgement anyway. Therefore, for those claims that already settle, the claimant may now be able to negotiate a higher settlement as the maximum the employer is willing to pay has increased.

We consider that generally claimants have less incentive to begin negotiating or reach a settlement position than an employer as their expected costs are far lower, and they are generally very optimistic about both the chances of winning the case and also the size of compensation awarded. Furthermore, following the government intervention, an employer's incentives to settle will increase, which will be known to the claimant and may be used to negotiate a higher settlement. In fact, the claimant should be able to negotiate the majority, if not all the **£450** increase from the employer, even based on partial information about the likelihood or cost of a pay audit requirement in the case.

Perfect information could also have been assumed here, in so far as the claimant may, like the employer, know the exact likelihood and expected cost of a pay audit being imposed were their claim successful. However this argument is less realistic.

Given the fact that the majority of equal pay claims against public sector employers have resulted from large scale pay evaluation exercises, it is highly unlikely that for example a Local or NHS authority's incentives to settle cases against them would be impacted by this proposal. It is expected that a pay audit would not be imposed on these organisations even where there was a finding of unequal pay as it would serve no further purpose, since they have recently conducted audits. Therefore, the settlement behaviour of public sector employers will be unaffected by these proposals.

It is therefore estimated that the cost of settlement will therefore increase by £449 for 970 (50.8% of 1,908) claims brought against private and voluntary sector employers each year. This is an annually recurring cost from government intervention of **£436,000**.

Furthermore, as a result of the increase in the expected cost of a hearing for the employer, is probable that the rate of settlement in equal pay claims will increase. This was suggested by most business representatives who responded to the consultation. This might be because of the process costs of conducting the audit, or because of fear that conducting an audit would, instead of enabling them to negotiate any changes to their pay structures that are still needed, simply raise new cases against them. Therefore, this measure will increase the expected impact of the case on the employer, affecting the decision of an employer of whether or not to settle the case or risk a judgement. Whereas previously, an employer may have chosen to risk a hearing, the increased cost will increase the amount they are willing to pay in order to settle the case, thus increasing the likelihood of an agreement being reached with the employee. As per above, the increase in the expected cost of a hearing is used to represent this increase in the maximum an employer is willing to settle for, and therefore the additional impact of the government intervention.

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<sup>2</sup> £11,657 = (£18,500 + £12,800 x 25% / 3.7) x 51% + £6,556 / 3.7

<sup>3</sup> £449 = 3.95% x £11,380

The scale of this effect will to some extent be dependent on the detailed nature of the audit requirement, which is to be decided following a second public consultation, and established by secondary legislation. Responses to the consultation generally supported the notion that enabling a tribunal to impose a pay audit would increase settlement incentives for employers. Some respondents suggested that since the cost of a pay audit in many instances would likely be greater than the compensation awarded, this would actually become the principal driver in determining employer settlement behaviour. However, no responses to the consultation suggested any specific estimate of the magnitude of this effect, and therefore here we rely on a wide range to reflect this uncertainty about the true size of the impact. We assume that the number of claims that would settle, and subsequently not proceed to hearing, would increase by 10-25%.

Using the figures presented in table 1, it is estimated that 76 (4% of the 1,908 assumed annual equal pay claims brought against private and voluntary sector employers accepted) reach a tribunal hearing. A 10 – 25% reduction in this number, offset by an increase in the number of claims settling, will result in an additional 7-19 claims that are settled annually. This represents an additional cost to private and voluntary sector employers of **£3-9,000** per annum.

The Exchequer will make savings if fewer cases proceed to hearing. The average cost of an Equal Pay hearing is £6,170, and given that there are on average 3.7 claims per case, these saving are estimated at **£12-32,000** per annum.

The increase in the settlement payment brought about by the increase in the expected cost of a hearing to the employer is a transfer to the claimant. Therefore, claimants will receive benefits from the government intervention of **£440-445,000** per annum. However, if this were the case, there would be other significant non-monetised costs to individual claimants, and the groups they represent within organisations, from not achieving formal recognition that the employer was in breach of the law.

## Annex 3. Wider Impacts

### Statutory Equality Duties

#### Equality Assessment

<b>Author/ editor/ assessor</b>	Government Equalities Office (GEO)
<b>Partners/ decision-makers/ implementers</b>	Government Departments (Department for Business, Innovation and Skills, Ministry of Justice), the Tribunal Service, employers, trades unions and the legal profession.
<b>Start date</b>	October 2010
<b>Scope</b>	Proposed legislative measures to strengthen enforcement of equal pay law.
<b>End date</b>	When the proposed legislation comes into force (excepting ongoing monitoring)
<b>Relevance</b>	The proposed legislative measures are highly relevant to gender equality. As the legal framework on equal pay relates solely to discrimination on grounds of gender, the measures have low relevance to other protected characteristics.
<b>Policy aims</b>	<p>Government's aim is to promote equal pay. The legislative measures considered in this impact assessment underpin its wider strategy which seeks to improve transparency in pay matters and strengthen enforcement.</p> <p>In particular, the government proposes mandatory pay audits for the small number of employers who are found to have breached equal pay law. This will not only improve transparency in these cases, but for the first time enable a judgement in an individual case to be used to challenge wider or systemic unfairness in pay and reward.</p>
<b>Available evidence</b>	<p>In 2011, the ONS estimated that women working full-time were still paid on average 10.5 per cent less than their male counterparts; if you compare the pay of all men and women in work, including those working part-time, the gap is as much as 20.2 per cent.</p> <p>Although the legal framework on equal pay has been in place since 1975, there are still a large number of equal pay claims. In the Impact Assessment this is estimated at 32,000 per annum.</p>
<b>Evidence gaps</b>	There is limited evidence on whether and how access to justice in relation to equal pay may vary amongst different groups, for example in relation to disability or ethnicity.
<b>Involvement and consultation</b>	Government has consulted fully on these measures and on an initial impact assessment before a decision was made to introduce legislation. The initial impact assessment was updated to reflect evidence from the consultation.
<b>What is the actual/likely impact</b>	<p>These measures will benefit gender equality by strengthening enforcement of equal pay law.</p> <p>Any individual may make use of the equal pay claim process, but the primary benefits will fall to women. These benefits will apply to women who suffer pay disadvantage as against men irrespective of whether they also have another protected characteristic such as race or disability.</p> <p>Although there are exceptions, women across most groups tend to suffer bigger pay gaps than men in those groups – for example, the pay gap for disabled men is 11% when compared with non-disabled men, while the gap for disabled women against disabled men is double this<sup>1</sup>. By strengthening the enforcement of equal pay, these measures should therefore have a positive impact on equality across all groups.</p> <p>We are not aware of evidence to suggest there could be any negative impacts arising from these measures on other groups.</p>

<sup>1</sup> Hills, J et al, 2010 An anatomy of Economic Equality in the UK: a Report of the National Equality Panel Government Equalities Office

<b>Monitoring and review</b>	<p>Government will monitor the effectiveness of its strategy to promote equal pay.</p> <p>Should the legislation on which it is consulting be introduced, GEO will put arrangements in place to monitor the impact of these measures, in particular to establish whether the Equal Pay policy has achieved its primary intention and objectives, and how this has worked (process and the observed outcomes and differences) and to understand the effect these measures have on equal pay claim tribunal outcomes (changes in both process and outcome) and whether this is a positive change.</p>
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## **Economic Impacts**

### Competition Assessment

Using the four key questions of competition impact assessment, as set out below, we do not believe this measure will have any impact on the ability of firms to compete.

Does this measure...?

1. Directly limit the number or range of suppliers?
2. Indirectly limit the number or range of suppliers?
3. Limit the ability of suppliers to compete?
4. Reduce suppliers' incentives to compete vigorously?

This measure is not recognised to have any impacts on suppliers in any specific markets, and therefore no impact on competition more generally.

### Small Firms Impact

We do not believe there will be any significant adverse impact on small firms as a result of this policy.

Firstly, with regards option 2, while a requirement on a small business to conduct an equal pay audit is not ruled out on principle in the consultation proposals, we do propose that the Tribunal should not impose one if it is not likely to be helpful in preventing further offending. It is unlikely to be helpful to very small firms to be subjected to the requirement, and the smaller the firm is; the less likely it is that it will face such a requirement. The consultation specifically drew attention to this issue, and respondents generally agreed that size was a relevant factor for a tribunal to consider when considering the usefulness of imposing an audit requirement. The proposal will not apply initially to micro businesses and start ups, in line with the moratorium announced by the Government. Consideration will be given at later date on whether to extend it to them.

## **Social Impacts**

### Health and Well-being

We do not believe there will be an impact on health and well-being as a result of this policy.

## Human Rights

These proposals do not contravene individuals' human rights.

## Justice

The imposition of an audit is itself a new civil sanction, though it is also to some extent preventative of further offending. The impact assessment now estimates the number of orders to conduct a pay audit at 2 per year. We intend to enforce the requirement by using a variation of the civil financial penalty regime that is being proposed following the Resolving Workplace Disputes Consultation, so that a civil financial penalty could not be applied when an audit requirement is made, but could then be made if the order is not complied with. There are therefore no additional costs to establishing the regime. There would potentially be enforcement costs in a very small number of cases (we assume that most audit requirements would be complied with, and that recovery action would be necessary in approximately half the number of civil penalties imposed), but these would be minimal. Where a penalty was used there would be a benefit to the Exchequer

We have discussed in the Impact Assessment a possible small increase in tribunal cases, but the costs have not been monetised as the effect is likely to be very small. We believe that there will also be some compensatory reduction in potential cases reaching tribunal as a result of the conduct of audits, but have not attempted to quantify this, as noted in the evidence base.

It is possible that the imposition of an audit could be subject of appeal to the EAT. However, structuring the requirement clearly to impose such an audit except in specified circumstances should reduce the likelihood of such appeals, and consideration during the consultation does not lead us to consider that appeals would be significant in number.