

EXPLANATORY MEMORANDUM TO
THE EMPLOYMENT EQUALITY (AGE) REGULATIONS 2006

2006 No. 1031

1. This explanatory memorandum has been prepared by the Department of Trade and Industry and is laid before Parliament by Command of Her Majesty.

This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Description

- 2.1 The Employment Equality (Age) Regulations 2006 prohibit age discrimination in employment and vocational training. They apply to all individuals in work or seeking work or access to training, to all employers, and to all providers of vocational training (including further and higher education institutions) and vocational guidance. The regulations include a number of exemptions - for example, in relation to retirement and service related benefits - and provide for other differences of treatment if they can be objectively justified.

3. Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 The regulations are made under section 2(2) of the European Communities Act 1972. They implement the UK's obligations (and matters arising out of or related to those obligations) in relation to discrimination on grounds of age under Council Directive 2000/78/EC. A copy of the Directive is being sent separately to the Joint Committee on Statutory Instruments and the Merits Committee.
- 3.2 The Secretary of State is designated under the European Communities (Designation) (No. 3) Order 2002 for the purposes of s.2(2) in matters relating to discrimination.
- 3.3 A copy of the Notes on Regulations, which explains how each of the provisions in the regulations operates, is being sent separately to the Joint Committee on Statutory Instruments and the Merits Committee.

4. Legislative Background

- 4.1 The Directive establishes a general framework for equal treatment in employment and occupation, including vocational training. It requires Member States to ensure that they have legislation in place outlawing discrimination on the new grounds of sexual orientation, religion or belief, age, as well as disability. As in the other strands of equality legislation, education of pupils in schools is excluded since this is not vocational training within the meaning of the Directive.

4.2 The Government implemented the other new strands – sexual orientation and religion or belief – in December 2003. Regulations, which primarily amended the Disability Discrimination Act 1995, to implement most disability provisions of the Directive came into force in October 2004, and in 2005 in respect of children with special educational needs and disabled students. Regulations to complete transposition of the Directive’s disability provisions in relation to vocational training into the law of England, Wales and Scotland will come into force by 1 September 2006. The Directive allows Member States until December 2006 to implement age and disability discrimination legislation. In line with our policy of introducing employment legislation on two common commencement dates every year, the age discrimination regulations are due to come into force on 1 October 2006.

4.3 A copy of the transposition notes, which explain how the regulations transpose the main elements of the Directive as it relates to age, is being sent separately to the Joint Committee on Statutory Instruments and the Merits Committee.

5. Extent

5.1 The regulations extend to Great Britain. Separate regulations are to be made to implement the Directive in Northern Ireland. Therefore, they do not extend to Northern Ireland except in the case of those amendments to legislation which itself extends to Northern Ireland.

5.2 The regulations do not extend to Gibraltar, the Channel Isles or the Isle of Man.

6. European Convention on Human Rights

6.1 Gerry Sutcliffe, the Minister for Employment Relations and Consumer Affairs, has made the following statement regarding Human Rights:

In my view the provisions of The Employment Equality (Age) Regulations 2006 are compatible with the Convention rights as defined in section 1 of the Human Rights Act 1998.

7. Policy background

7.1 In developing these regulations the Government has been governed by three important principles.

7.2 First, the Government has aimed for a light touch implementation that strikes the right balance between tackling age discrimination effectively by giving important new rights for individuals, whilst allowing business to continue to operate productively but fairly.

7.3 Secondly, it has aimed to make the provisions as consistent as possible with those in other discrimination strands, in particular the other new strands on sexual orientation and religion or belief. Consistency will help employers,

providers of vocational training, and employees to get to grips more easily with their new responsibilities and rights under the Directive.

7.4 Thirdly, the regulations have been developed as the result of extensive consultation both formal and informal, with the full range of stakeholders:

- a. December 2001: "Towards Equality and Diversity" sought views on proposals for equality legislation on race, disability, sexual orientation, religion or belief, and age. On age we were particularly interested in exploring what age-based practices employers had, why they had them, if they needed to retain them, and if so, why;
- b. October 2002 – "The Way Ahead" consultation published proposals for equality legislation on sexual orientation and religion or belief, including some related to age
- c. July 2003 – "Age Matters". This was the first consultation to focus exclusively on age, and sought views on options for legislation;
- d. July 2005 – "Coming of Age" sought views on draft regulations. We wanted to know whether the details of our decisions would give rise to significant practical difficulties, and whether they reflected the policy as set out in the consultation document. In order to help ensure that subsequent guidance on the regulations was clear, we also sought views on the clarity of our explanations in the consultation.

We published our analysis of responses to "*Coming of Age*" at the same time as laying these Regulations before Parliament. A copy is being sent separately to the Joint Committee on Statutory Instruments and the Merits Committee.

7.5 These formal consultations attracted over 2000 responses in total – with over 800 specifically on age.

7.6 Throughout the period since 2001, officials have continued to consult informally, holding round-table meetings, and other individual and group meetings, and attending workshops and seminars.

7.7 The Age Advisory Group, reinforced in 2004 by the Age Task Force, has met throughout the process, chaired by the Minister for Employment Relations. Its remit has been to advise Ministers on matters to do with the implementation of the age aspects of the Directive. Its members include our social partners.

7.8 As a result of responses to "Coming of Age", and subsequent discussion with key stakeholders, we have made a number of changes before finalising the regulations, which we have discussed with the main stakeholder organisations. The changes are mainly to ensure that the policy aims outlined in the *Coming of Age consultation document* are achieved effectively. They do not represent significant policy changes. The issues which consultations showed to be of most significance to stakeholders are set out below.

Retirement age (including unfair dismissal and the “duty to consider”)

- 7.9 The Government announced its approach in relation to retirement age on 14 December 2004. Age discrimination legislation, whilst providing for employers to objectively justify mandatory retirement below 65, will also provide for a default retirement age of 65 accompanied by a right for employees to request working beyond retirement age. This means that employers will be able to use a retirement age at or above 65 without having to justify doing so.
- 7.10 A default retirement age legitimately pursues a number of social policy objectives, but principally workforce planning and avoiding an adverse impact on the provision of occupational pensions and other work-related benefits. As far as workforce planning is concerned, it provides a target age against which employers can plan their work – including the recruitment, training, and development of employees and the planning of wages structures and occupational pensions against a known attrition profile - and employees can plan their careers and make adequate plans for retirement.
- 7.11 If all employers only had the option of individually objectively justified retirement ages, this could risk adverse consequences for occupational pension schemes and other work related benefits. Some employers would instead simply reduce or remove benefits to offset the cost of providing them to all employees, including those over 65.
- 7.12 The Government will monitor the impact of the default age and will conduct an evidence-based review in 2011 on whether or not it is still needed.
- 7.13 Whenever an employer decides to retire an employee, he will have a duty to inform the employee of the right to request working beyond the intended date of retirement. If the employee does not make a request, the employer can then retire the employee without any further procedures. If the employee makes a request, the employer will have a duty to consider it, and there will be a meeting between employer and employee to discuss the request. The employee will not be able to challenge the employer when it is a genuine retirement. However, if the employer does not comply with this procedure while retiring the employee, the employee may challenge this dismissal as unfair. These provisions, which are modelled in part on the right to request flexible working, aim to promote a culture change by encouraging both employee and employer to consider whether the individual could continue to work beyond retirement age.
- 7.14 The regulations aim to ensure that employees will have the right to complain of unfair dismissal for other reasons at any age, and employers will not be able to avoid their responsibilities by calling dismissal for other reasons retirement. The responses to “*Coming of Age*” showed that the provisions relating to unfair dismissal and retirement were much too uncertain and open to challenge. The drafting has, therefore, been changed in the course of further consultation with stakeholders, to tighten up the procedures and reduce the risk of unnecessary tribunal cases.

Service related benefits (pay and non-pay benefits)

7.15 Benefits that recognise length-of-service are widely supported. The Government appreciates the positive role they play in rewarding loyalty, providing incentives, and helping motivation. For that reason we have legislated in such a way as to avoid jeopardising the provision of these benefits, and have not required employers to justify every benefit on an individual basis. The Government believes that it cannot be sure that all age-related aspects of benefits will always be justified. However, it is justified to provide exemptions in relation to length of service in the way we have in order to minimise the risk of downgrading or removal of pay and non-pay benefits.

Occupational pensions

7.16 Occupational pension schemes necessarily have a number of age-based rules. Our aim is to disturb pension arrangements as little as is consistent with eliminating unjustified age discrimination, and so avoid the possibility of occupational pension provision being levelled down.

7.17 The regulations make it unlawful for trustees or managers of an occupational pension scheme, when carrying out their functions, to harass or discriminate against a member or prospective member of the scheme on grounds of age. Every occupational pension scheme will be treated as including a non-discrimination rule and trustees and managers will be given power to alter schemes in order to comply with the rule.

7.18 The consultation had revealed a number of issues:

- the occupational pension provisions could have been interpreted as including an exemption for a lower age limit for enhanced early retirement pensions, although it was not our intention to do so;
- there was no exemption for employer contributions to personal pension arrangements;
- the exemption for age-related contributions could not be justified without qualification.

7.19 These are reflected in schedule 2 to the regulations, which provides that certain age-related rules or practices in occupational pension schemes are effectively exempted. These include:

- closing pension schemes or parts of pension schemes to new workers;
- the use of minimum and maximum ages for admission to pension schemes, including setting different ages of admission to a pension scheme for different groups or category of worker;
- having lower and upper ages in a pension scheme, between which a member who retires will not have his benefit actuarially reduced to take account of early retirement nor enhanced for late retirement;

- age-related contributions to defined benefit schemes, where contributions increase with age to reflect the increasing cost of benefits in respect of members as they get older;
- age-related contributions to occupational and personal pension schemes, which are aimed at producing near equal outcome in pension benefits;
- flat-rate employer contributions into occupational pension schemes;
- the use of age criteria in actuarial calculations;
- different amounts of pension for workers with different lengths of service, provided that for each year of service rights to benefits accrue on the same fraction of pensionable pay;
- a lower age limit, below which a scheme member cannot receive an enhanced pension in the event of early retirement – but for existing employees only;
- different rates of employer contributions to occupational and personal pension schemes for different workers, which are attributable to differences in the remuneration payable to those workers.

Statutory redundancy payments scheme

- 7.20 There is currently an upper age limit for entitlement to statutory redundancy payments. The upper age limit is the retirement age set by the employer in question, or 65 if the employer has no retirement age. There is also a lower age of 18, below which service is not counted. We do not believe that it would be right to continue to ignore employment before the age of 18 or deny those above the upper age limit compensation for redundancy where those in other age groups are receiving it. The regulations, therefore, abolish the lower and upper age limit. They also remove the rule that currently gradually tapers down to zero the redundancy payment for those who are approaching the upper age limit.
- 7.21 The calculation of the redundancy payment is based on multiplication of a weekly amount of salary with the number of years of service, with a certain multiplier. The multiplier currently varies across a number of age bands, ranging from one half for younger workers to one and a half for older workers. We had proposed in our consultation to remove the age bands for the multiplier, and to apply a unified multiplier for all age groups. However, we now conclude that we should retain the current banding system.
- 7.22 Following the publication of *‘Coming of Age’* we have been discussing the redundancy scheme with key stakeholders and exploring the different options in greater detail. Evidence demonstrates that younger, prime age and older workers fall into three distinct economic categories, with older workers facing a particularly difficult position in the employment market. We now believe that there is, therefore, a good case for providing different levels of compensation for each of these groups under the scheme. A copy of the

Government's written statement of 2 March is being sent separately to the Joint Committee on Statutory Instruments and the Merits Committee.

Exceptions for statutory authority and statutory benefits

- 7.23 Age criteria are used widely in legislation. As a consequence, those who have to comply with such legislation may have to discriminate on the grounds of age. They should not have to fear that in doing so they would violate these regulations. The exception for statutory authority provides absolute protection in those circumstances.
- 7.24 As part of the preparation for introducing the regulations, all Government Departments have conducted a review of their legislation to ensure that any age-based provisions in the field of employment and occupation, including vocational training, are justified or removed. The same considerations will apply to future legislation.
- 7.25 The Regulations also provide that employers who follow statutory requirements in the provision of redundancy pay and use the development bands of the minimum wage will not have to justify any age provisions that are laid down in the legislation.

8. Impact

- 8.1 Regulatory Impact Assessments (RIA) have been prepared and were included in the consultations on proposals for legislation and on the draft regulations themselves. They are attached to this memorandum. They are:
- a. summary
 - b. Retirement ages
 - c. Recruitment, Training and Promotion
 - d. Statutory Redundancy Payments
 - e. Unfair dismissal
 - f. Occupational pensions
 - g. Service-related benefits [Pay and non-pay benefits]

9. Contact

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Age Discrimination - Summary

March 2006

<http://www.dti.gov.uk/er>

1. This Regulatory Impact Assessment (RIA) considers the impact of age discrimination legislation on employers and individuals, and on the macroeconomy and the Exchequer. There is currently no legislation in the UK covering age discrimination. Proposed legislation to implement the age strand of the European Employment Directive (Council Directive 2000/78/EC) covers employment and vocational training, including retirement, occupational pensions, recruitment, training provided by employers, promotion, pay and non-pay benefits and vocational training. This summary RIA should be read in conjunction with the six RIAs prepared on these specific age discrimination rules. Some existing legislation with age-based rules applying to employment – for example, certain elements of statutory redundancy payments and unfair dismissal – is also to be changed. Legislation outlawing discrimination on the grounds of age is scheduled to come into force on 1 October 2006.

Purpose and intended effect of measure

Objective

2. The aim of the legislation is to maximise the participation and economic (and social) contribution of groups that are currently subject to discriminatory practices *both* inside and outside the labour market because of their age. At the same time the Government recognises that there are exceptional circumstances when some age-based practices are capable of being objectively justified, and the Directive allows this. In implementing the Directive, the Government will therefore aim to improve opportunities and choice for individuals, and encourage labour market participation, whilst still allowing employers to manage their businesses effectively.

Background

3. The legislation will affect individuals of all ages but evidence suggests that those affected most by age discrimination tend to be older workers (about 50 years or over) and young workers (up to about 25 years). It is also aimed at benefiting job seekers who face discrimination entering the labour market. The legislation should, both by providing protection to those subject to discriminatory practices and by stimulating a cultural change, increase the participation of older and younger workers in the economy, while at the same time helping employers draw on a wider pool of workers.

4. The legislation will make it unlawful to discriminate against individuals on the basis of age in employment (including promotion, recruitment, terms and conditions including retirement and redundancy, pay and pensions), vocational training (including further and higher education) and in respect of membership and representation in professional organisations (including employers organisations and trade unions) except where these can be ‘objectively justified’. The Directive provides for the objective justification of differences of treatment on the grounds of age so that an aged-based difference in treatment is not unlawful discrimination where it is objectively justified by a legitimate aim and the means of achieving that aim are appropriate and necessary.

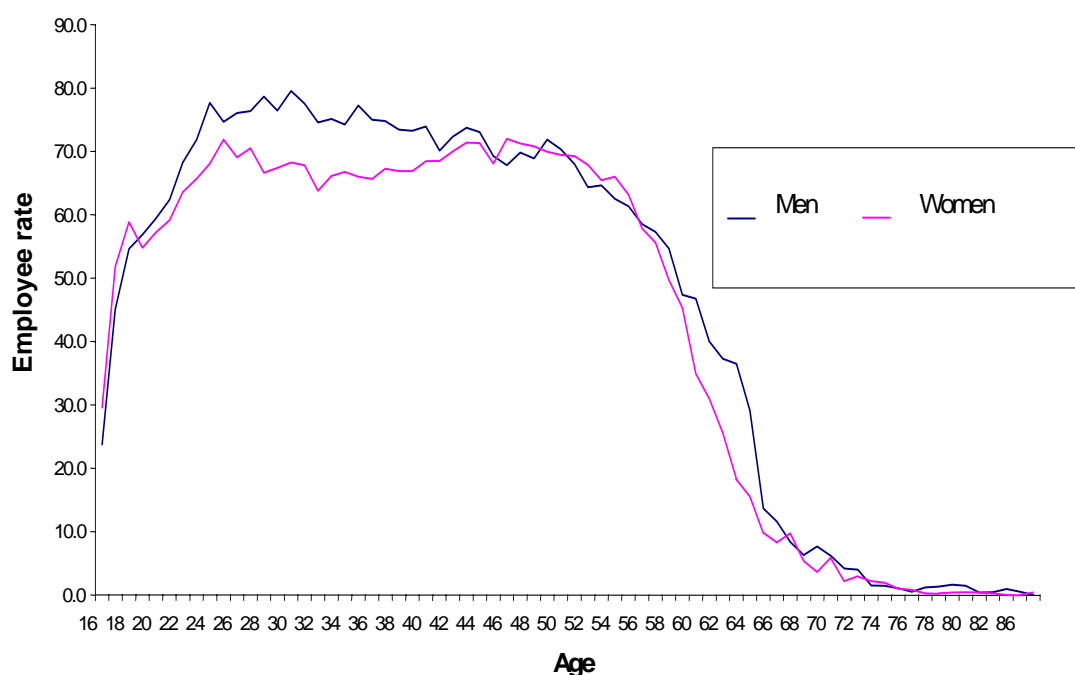
Rationale for government intervention

5. Discrimination results in poorer quality matches in labour markets, which leads to lower national output¹. The evaluation of the age Code of Practice and other studies find direct evidence of age discrimination in employment². Older workers may find it difficult to re-enter the labour market after a period of absence because of negative stereotypes, even though they are still productive. Young workers may also find it difficult to enter the labour market initially. The risk that exists currently is that these people are not participating fully in the workforce and so human resources are wasted. Age discrimination is consistent with lower employment rates for younger and older workers (see graph 1), as well as the higher incidence of redundancy, inactivity and long-term unemployment for the latter group. These patterns persist over the economic cycle. However, these are not just due to discrimination.

¹ Mankiw (1997) defines discrimination as ‘the offering of different opportunities to similar individuals who differ by colour of skin, ethnicity, gender, age or other characteristics.’ For an introduction to the economics of discrimination in labour markets, including a discussion of the theory of discrimination, its impact on the economy and why it can persist in a competitive market, see chapter 14 of ‘Economics of Work and Pay’ (1996), R. Filer, D. Hamermesh and A.Rees.

²“Code of practice on Age Diversity in Employment and Age Diversity in Employment Guidance and Case Studies (DfEE 1999)”. Casey, B and Wood, S (1994), “Great Britain: firm policy, state policy and the employment of older workers.” Hayward, B, Taylor, S., Smith and Davies G (1997), “Evaluation of the campaign for older workers”, London: The Stationary Office.

1. Employees as a proportion of population by age and sex in Great Britain



Source: National Statistics

6. **Other discriminatory practices in training and promotion could reduce productivity because of the resulting ineffective matching of talent, aptitude and abilities to these advancement opportunities. Employers will also have a smaller pool of workers to draw on and will either not be making the most of the existing potential skills base of the workforce or will be losing valuable skills. As an illustration of the scale of these risks, a Cabinet Office Report estimated that low employment rates among older workers reduced GDP by around £16 billion per annum.³**

Consultation

Within government

7. **These proposals have been developed in consultation with various interested Departments including the Department for Work and Pensions, the Department for Education and Skills, HM Treasury, HM Revenue and Customs, Cabinet Office and the Small Business Service.**

Public consultation

8. **The Department has taken a progressively consultative approach on how to implement age discrimination legislation in Great Britain. The first formal consultation in 2001⁴ covered all the new equality strands.**

³ See "Winning the Generation Game Improving Opportunities for People aged 50-65 in Work and Community Activity – A performance and Innovation Unit Report" – April 2000. Weblink: <http://www.cabinet-office.gov.uk/innovation/2000/winning/generation.pdf>

⁴ Towards Equality and Diversity: Implementing the Employment and Race Directive.

On age it sought to find out what age-based practices were used by employers, why they used them, whether they wanted to keep them and why this was the case. At the end of 2002 the Department launched a second consultation⁵ that focused mainly on strands other than age, as well as the general approach to discrimination legislation. In 2003 the Department launched its third consultation⁶, which asked for views on proposals for outlawing age discrimination in employment and vocational training, including options for retirement ages.

9. As well as informal consultation, the Department has had a strategy of continuing engagement with its main stakeholders both informally, and formally, with the Age Advisory Group that is chaired by the Minister. We have sought views on policy options, as well as drawing on stakeholders' expertise to inform ourselves better about employment practices.

10. The policy of positive engagement and consultation with stakeholders will be applied to the development of good practice guidance on age legislation. This work will be undertaken by Acas.

11. Throughout the policy development process we have paid particular attention to what our consultees have told us. Although they have shown broad support for the policy of abolishing age discrimination, there have been instances where we have had to change our proposed policies. For instance in *Age Matters* the Department proposed introducing a default retirement age of 70. The fact that this received very little support influenced the decision on the approach to retirement ages. We have subsequently considered a wider range of options. We have made reference to the results of the consultation in the individual RIAs.

Coming of Age consultation

12. The *Coming of Age* consultation carried out in mid-2005⁷ set out agreed policy on implementing the age strand of the Employment Directive and included draft Regulations. Around 390 responses were received in total, with business accounting for half of these. A further 15% were from non-departmental public bodies (NDPBs) and other government departments (OGDs), 14% were from members of the public, and 10% from the education sector. The legal profession and trades unions accounted for around 8% and 5% of responses respectively.

13. The general tone was supportive of the aims but with significant concerns about the practical effects in some areas, and many detailed points. Trade unions and age groups expressed disappointment that the provisions did not go far enough. Employers welcomed the Government's action to avert the potential difficulties which might arise from the legislation but considered the provisions too complex and open to challenge.

⁵ Equality and Diversity: The way ahead.

⁶ Equality and Diversity: Age matters.

⁷ Equality and Diversity: Coming of Age

14. We have considered carefully all the points made in the consultation. In implementing the Directive we have been concerned to use better regulation principles and have aimed to legislate with as light touch as possible, being careful not to go further than the Directive requires. We have responded as far as possible to employers' points, and have been working to simplify and clarify the regulations where possible. The provisions are necessarily complex, however, and some of business's suggestions would have been successfully challenged as failing to implement our European obligations.

15. Nor have we taken forward consultees' requests for the legislation to go further than the Directive requires, for example by covering goods, facilities and services or unpaid volunteers. This is a matter more properly considered by the review of discrimination law which DTI is currently conducting, and which is due to report next year.

16. Most of the changes we have made to the regulations are drafting changes to better reflect agreed policy rather than policy changes, which are discussed in the individual Regulatory Impact Assessments.

17. There were a number of consultation responses relating to the estimated costs and benefits associated with these proposals. Responses to specific concerns raised are discussed in turn below. The consultation also elicited support for the broader economic and social benefits that are estimated to arise from the proposals as a result of increased employment rates and better job matching.

Options

18. The main options considered by the Government in tackling age discrimination are:

- a. Do nothing;
- b. Introduce a voluntary code of practice;
- c. Introduce legislation, without allowing employers to objectively justify some discriminatory practices; and
- d. Introduce legislation, and provide for employers to be able to objectively justify some discriminatory practices.

19. Doing nothing is not a realistic option as it would mean not implementing the European Directive. It would also mean that, in the field of employment and vocational training, discrimination on the basis of age was likely to continue and employment rates among certain age groups were likely to remain undesirably low.

20. A non-regulatory approach was introduced in 1999, through a voluntary Code of Practice, which was supplemented by guidance and case studies on best practice. These have helped to bring age discrimination issues on to the agenda, and evaluations have shown they have helped to increase awareness.⁸ However, the Code of Practice lacked an enforcement mechanism and the complex nature of these

⁸ For an academic analysis on the Code of Practice see "The Generation Game – Third Age Workers and the Labour Market." Helen Desmond, Nottingham Law Journal http://www.nls.ntu.ac.uk/CLR/PDF/nlj9_2/017.pdf.

issues has always meant that ‘step changes’ in penetration and awareness are needed. Unlike racial and sexual discrimination, there is evidence that age discrimination is still seen as a new and difficult concept to grasp – and needs to be distinguished from the effects of health and fitness.

21. The Government’s preferred option, therefore, is to introduce legislation. The responses to formal and informal consultation have shown that there are some practices that are discriminatory, but are probably objectively justifiable in certain circumstances. Therefore, failing to implement the provision allowing objective justification could result in unnecessary costs with limited corresponding benefits. For instance, employers who insist on certain qualifications in recruitment which were not available decades ago (like media studies), could be accused of indirect discrimination, even though the nature of the business and their particular circumstances might render such an approach objectively justifiable. The consultation in 2003⁹ showed broad support for a number of aims that might justify differences of treatment in exceptional circumstances listed in the consultation document.¹⁰ We, therefore, propose to provide for employers to be able to objectively justify age-based practices. However, if challenged, they will have to show an Employment Tribunal that their approach is an appropriate and necessary way of fulfilling a legitimate aim. This is discussed further in the RIAs of each policy strand.

Costs and benefits

Business sectors affected

22. All business sectors will be affected. However, there may be some sectors that have a higher proportion of younger or older employees. This does not mean that they are more likely to be discriminatory, but it may mean that they need to look at certain policies more closely. Table 1 shows the distribution of employees by age and industry. It shows that the distribution sector, hotels and catering sector, and other services sector are more likely to employ younger workers. The public administration, education and health sector is more likely to employ workers aged between 50 and 59.

1. Proportion of different aged employees in different industry sectors

	16-24	25-49	50-59	60 and over
Agriculture and fishing	21.1	58.0	14.7	6.3
Energy and water	11.9	64.6	20.6	2.9
Manufacturing	10.4	63.7	20.1	5.8
Construction	16.9	56.7	19.6	6.8
Distribution, hotels & restaurants	32.5	48.1	14.4	5.0
Transport & communication	11.4	63.4	19.9	5.2
Banking, finance &	13.4	66.9	15.5	4.2

⁹ Equality and Diversity: Age matters. For details and results of the consultation see www.dti.gov.uk/er

¹⁰ These were health, welfare and safety, facilitation of employment planning, the particular training requirement of the post in question, encouraging and rewarding loyalty and the need for a reasonable period of employment before retirement.

insurance etc				
Public admin, educ & health	7.7	63.8	23.4	5.1
Other services	24.2	51.9	16.4	7.5
All industries	15.7	60.0	19.0	5.3

Source: National Statistics (www.statistics.gov.uk) Labour Force Survey Autumn 2004

23. The evaluation of the Code of Practice on Age Diversity in Employment shows survey evidence that the communication sector is more likely to include age when advertising vacancies and when selecting candidates than other sectors.¹¹ They will, therefore, need to review their practices more than other sectors, even if these can be objectively justified.

Assumptions

24. We assume only people in work could have faced age discrimination in terms of promotion, on-the-job training practices, pay and non-pay benefits, redundancy and retirement, whereas all economically active individuals could face age discrimination in terms of recruitment and vocational training decisions. There will be others, as mentioned above, who will be affected, such as students and all those who are in receipt of pay but who are not employed. In this RIA we focus mainly on those who are economically active, although the macroeconomic assessment does assume an increase in participation rates that may impact on some economically inactive individuals.¹²

25. Although there are no age limits in the Directive, to assess the potential extent of age discrimination in the workplace and coverage of legislation we consider two specific age groups in Great Britain: those aged 16-25 and those aged 50 and above. The numbers affected will also depend on the particular policy strand under consideration. Detailed assumptions are considered further in the relevant RIAs.

Implementation costs

26. Implementation costs will arise because in order to comply with the legislation companies will have to become familiar with it and will need to make decisions about what action needs to be taken as a result of the legislation. Compared to the other strands of employment equality legislation (religion, sexual orientation, disability), there are additional considerations for companies getting to grips with the age legislation. In particular:

- **What would otherwise be direct age discrimination can in some cases be ‘objectively justified’; and**
- **It may reflect many ingrained day-to-day practices, through conscious prejudice or the unintended by-products of actions.**

¹¹ Source: Department of Work and Pensions (2001) *Evaluation of the Code of Practice on Age Diversity in Employment – Report of Research Findings*

¹² We also briefly refer to those undergoing vocational training but not working.

27. Table 2 shows the expected costs of implementation to firms for each policy strand and for small, medium and large firms. We envisage no quantifiable implementation costs for unfair dismissal and redundancy (see the relevant RIAs).

2. Implementation costs for firms (one-off)			
	Small firms (£m)	Medium and large firms (£m)	All (£m)
Retirement ¹³	58	3	61
Redundancy	-	-	-
Unfair dismissal	-	-	-
Occupational pensions	21	27	47
Recruitment, training and promotion	58	7	65
Pay and non-pay benefits	29	17	46
Total	166	54	219

28. The cost per small firm is expected to be about £140 and the cost per large firm is expected to be about £1,500. The costs per small firm are expected to be lower as there will be fewer individuals who need to become familiar with and consider the consequences of the legislation within each organization. For more details see the individual RIAs and the Small Firms Impact Test.

29. Concerns were raised during the *Coming of Age* consultation that the implementation costs for smaller employers had been underestimated. Some small businesses indicated that familiarisation with the legislation would entail recourse to legal advice, itself amounting to more than the £140 estimate per small business. But others would not feel the need to seek external advice. Overall we believe we have judged the costs right. Whereas larger employers are assumed to seek to understand the legislation at once, smaller businesses tend to read the legislation on a needs basis. The estimated cost of implementation presented here is therefore an *average* cost across all smaller businesses.

30. Furthermore, clear and comprehensive guidance on the legislation will be made available by DTI and Acas and, as this has been prepared specifically with the needs of smaller employers in mind, it is envisaged that it will significantly reduce the need for them to seek specialist legal advice.

31. In addition to this we have recently launched a ‘capacity building’ programme to develop the capacity of intermediary organisations (NGOs/trade unions etc) to deliver advice and guidance to individuals on their new rights as a result of the regulations and to inform employers of their new obligations. We have specifically asked for applications that

¹³ This is based on a default retirement age of 65, the ability for employers to objectively justify an earlier retirement age if necessary, and a duty to consider working past the chosen retirement age. For details of implementation costs for the other options considered, see the RIA on retirement ages.

will provide a strategic capability to CEHR, the body with responsibility for age from 2007.

32. There will be further implementation costs for trustees in becoming familiar with the legislation on occupational pensions (about £3.6m) and the Insolvency Service in changing computer systems to cope with the new formula for statutory redundancy payments (£100,000).

Retirement

33. Several options were considered. These were:

- a. No national default retirement age (DRA) and employers not able to set their own retirement ages;
- b. No national DRA, but allowing employers to set their own retirement ages, which they would potentially have to justify at Employment Tribunal, hence the name employer-justified retirement ages (EJRAs);
- c. No national DRA, but allowing employer-justified retirement ages, with a duty on employers to consider employees' requests to work beyond any compulsory retirement age (if they have one)¹⁴;
- d. A national DRA of 65 and employer-justified retirement ages, with a duty on employers to consider employees' requests to work beyond a compulsory retirement age

34. The net benefits to the economy because of the legislation are the sum of the effects of the increase of the labour supply on GDP and the productivity effects on employers.

35. Table 3 summarises and disaggregates the quantified net costs and benefits to the economy into those for individuals, firms and the Exchequer. For further details of the costs and benefits see the RIA on retirement ages.

¹⁴ The duty on employers to consider requests to work beyond any compulsory retirement age ensures a constructive dialogue between employers and employees who do not want to retire.

3. Summary of quantified net costs and benefits of retirement options (£m)

		Option a	Option b	Option c	Option d
Employers (due to changes in total factor productivity)	Year 1	Cost £75-79m	Cost £110m	Cost £120m	Cost £57-72m
	Average annual NPV**	Cost of £32m to benefit of £0.46m	Cost of £6.8-32m	Cost of £6.4-39m	Cost of £9.4m to benefit of £1.5m
Individuals	Year 1	Benefit £44-120m	Benefit £29-100m	Benefits £31-110m	Benefits £12-67m
	Average annual NPV**	Benefit £130-350m	Benefit £83-290m	Benefit £90-320m	Benefit £32-190m
Exchequer	Year 1	Benefit £35-93m	Benefit £22-78m	Benefit £24-84m	Benefit £8-52m
	Average annual NPV**	Benefit £110-280m	Benefit £67-230m	Benefit £73-250m	Benefit £25-150m
Economy (due to changes in the labour supply)	Year 1	Benefit £100-270m	Benefit £67-220m	Benefit £71-240m	Benefit £27-150m
	Annual average NPV**	Benefit £310-800m	Benefit £190-650m	Benefit £210-710m	Benefit £74-420m
Total	Year 1	Benefit £21-190m	Cost £48m to benefit of £110m	Cost £50m to benefit £120m	Cost £46m to benefit £91m
	Annual average NPV**	Benefit £280-790m	Benefit £150-640m	Benefit £170-700m	Benefit £63-420m

** Annual average NPV = the net present value of the costs and benefits from year 1 to year 10, discounted at the Treasury rate of 3.5 per cent and divided by ten.

36. The Government has concluded that legislation implementing the age strand of the European Employment Directive should set a default retirement age (DRA) of 65. Employers would be free to objectively justify setting their own retirement age (EJRA) below 65, and employees would have a right to request working beyond the DRA or their employers' objectively justified retirement age (if appropriate).

37. This approach aims to promote greater choice for older workers without an unnecessary burden on business – many of whom rely on retirement ages as an important means of workforce planning – and to avoid adverse effects on occupational pensions and other employment benefits.

Statutory redundancy payments

38. It was initially assumed that the statutory redundancy scheme would require changing if it were to be consistent with a policy of non-discrimination on the basis of age. Some elements on the basis of age

respond to social policy aims, however, and will be kept where these can be objectively justified.¹⁵ The changes include:

- Removing the age 18 lower limit on service taken into account for the purposes of qualification and payment calculation under the scheme;
- Repealing the provision under which the amount of payment due is tapered between the ages of 64 and 65, and
- Removing the upper age limit on entitlement.

39. In deciding on a suitable formula for redundancy payments, the RIA considers a number of options: (a) retaining the existing system, apart from the changes above and (b) using a single multiplier for all age groups. The impact on firms, employers and the Exchequer are summarised for the options in Table 4.¹⁶ Further details are available in the RIA on statutory redundancy payments.

40. Both consultations, *Age Matters* and the follow-up consultation *Coming of Age*, were based on an assumption that the current system of different multipliers for different age bands was discriminatory and would have to be removed. The Partial RIA on Statutory Redundancy Pay examined the costs and benefits of implementing a single multiplier (option b) as a possible means of removing the elements of age discrimination within the statutory redundancy payments scheme.

41. However further research and analysis, as well as responses to the *Coming of Age* consultation, have highlighted the fact that some age-related elements of the current system are objectively justifiable. Therefore the Government's preferred option is option a.

4. Summary of costs and benefits of changes to the formulae for statutory minimum redundancy payments compared with doing nothing

		Annual benefits (£m)	Annual Costs (£m)	Implementation Costs (£m)
Option (a): removing lower and upper age limits	Firms		£4.5m-£9.1m	
	Employees	£15m		
	Exchequer		£1.2m	£0.1m
Option (b): single multiplier and no lower or upper age limits. Multiplier = 1.1	Firms	£22.1-£44.2m		
	Employees		£50m	
	Exchequer	£6.0m		£0.1m

Unfair dismissal

42. The aim of changes to the legislation on unfair dismissal is to ensure that all workers, no matter their age, are treated fairly when they are dismissed. This should also result in increased security for those

¹⁵ The basic entitlement for statutory redundancy payments is as follows: half a week's pay for each year's service between the ages of 18 and 21, one week's pay for each year's service between 22 and 40, and one-and-a-half week's pay between 41 and 65, in all cases with weekly pay subject to a maximum of £280 and the number of years' service to a maximum of 20.

¹⁶ For the sake of clarity, the current weekly limit of £280 is used, and a single multiplier of 1.1 weeks per year of service for option (c).

workers currently not covered, and therefore an increase in their willingness to participate in the workforce.

43. Two aspects of the scheme were therefore considered: the age limit on the ability of an individual to claim for unfair dismissal and the calculation of the basic award, which mirrors the statutory redundancy payment formula (and therefore contains some discriminatory elements which are not considered to be objectively justified). The RIA on unfair dismissal considers several options:

- (a) Maintain the upper age limit;
- (b) Remove the upper age limit;
- (c) No change to the calculation of the basic award; and
- (d) Change in calculation of basic award formula based on a single multiplier.

44. The costs and benefits for firms, individuals and the Exchequer are outlined in Table 5.

5. Summary of costs and benefits of changes in unfair dismissal

	Benefits	Costs
Firms		
Option a - Keep upper age limit	None	None
Option b - Removing upper age limit	May encourage workers to stay in workforce	£2.4-2.8m each year
Option c - no change to calculation of awards	None	None
Option d - change calculation of awards	£1.0m	
Individuals		
Option a - Keep upper age limit	None	Employees aged 65 or older still cannot claim unfair dismissal
Option b - Removing upper age limit	Greater fairness and may encourage older workers to stay in workforce, although there is a risk that employers might be reluctant to keep on those aged 65 and over	None
Option c - no change to calculation of awards		Years of service at different ages treated differently
Option d - change calculation of awards		£1.0m
Exchequer		
Option b - removing upper age limit		£0.5m

45. We recommend options b and c as these options best meet the Government's policy objectives. The formula chosen for option c will mirror that chosen to calculate statutory redundancy payments.

Occupational pensions

46. The aim of these regulations is to ensure that employers are not discouraged from maintaining occupational pensions for their employees, in the context of age discrimination legislation. We will do

this by allowing employers, as far as possible, to maintain existing age-based rules.

47. The alternatives in implementing the legislation are:

- (a) Do nothing. This would in effect mean employers / scheme trustees relying on a general provision for aged-based policies to be objectively justified;
- (b) Provide that certain rules do not constitute unlawful age discrimination, leaving employers to objectively justify remaining age based-rules;
- (c) In addition to (b), provide that other rules, which are always objectively justified, are not unlawful. For the purposes of this paper we refer to this approach as exempting age rules.

48. Employers having to objectively justify all or many age based rules in occupational pension schemes (options a and b) could result in considerable costs (through deciding on whether each age-based rule was objectively justified) and uncertainty for employers, as the only way to test whether those rules complied with the age legislation would be through the Employment Tribunal system, and claims could arise many years into the future. There is considerable danger, therefore, that employers would be tempted to withdraw pension benefits or level down rather than go through this process. This would result in the Government not achieving its objective.

49. The Directive's provisions that allow for rules not to count as unlawful age discrimination, or to be objectively justified (and effectively exempted) will, in the context of age discrimination legislation, provide for the maximum certainty in the running of occupational pension schemes. The proposed approach is therefore option c.

50. The implementation costs to employers will come to about £51 million. There will some costs for employers and the Exchequer arising from Employment Tribunal claims. Employees should benefit from the maintained provision of their occupational pensions.

51. Some consultation responses noted that employers will face increased costs where they have to make pension contributions for workers who would currently be over retirement age and therefore not covered by occupational pension schemes. Due to uncertainties about how many older workers will continue to make pension contributions beyond their current retirement age we have not attempted to quantify this cost. Some employees will already have reached the maximum length of service for pension contributions before reaching retirement age, while others will choose to continue working while simultaneously drawing a pension (and thus not make further pension contributions).

Recruitment, training and promotion

52. In implementing the legislation, the Government will aim to improve opportunities and choice for individuals, and encourage labour market participation, whilst still allowing employers to manage their business effectively.

53. Decisions about recruitment, selection and promotion should normally be based on candidates' skills and abilities, but there might be exceptional cases when age requirements are justifiable.

54. The Government therefore proposes to provide for employers to be able to objectively justify age-based practices if appropriate and necessary. Failing to make such provision could result in employers engaging in practices that would result in reduced benefits for firms. Consultation has shown broad support for this approach.

55. Table 6 summarises the quantifiable costs and benefits of the proposed option.

6. Summary of costs and benefits of recruitment, training and promotion

	Benefits Annual	Costs Annual	Costs One-off
Employers			
Implementation (Awareness and Decision Making)			£65 m
Enforcement		£22 m	
Recruitment	£14-85m	£4.0-8.8m ^a	
Training	£51-420m	£44-370m	
Promotion	£14-180m		
Individuals			
Training	£5-42m		
Promotion	£27-140m		
Exchequer			
Enforcement		£6m	
Economy	Net annual benefit of £24-460m (average NPV)		
Notes: a. This cost is annual but gradually declines to about £2.5-6m by 2011.			

Pay and non-pay benefits

56. The aim is to ensure that that the provision of service-based pay and non-pay benefits to employees can continue without the imposition of unnecessary burdens. Such benefits motivate staff, reward loyalty, and recognize length of service. Many of the benefits employees receive will not be age discriminatory. However, some pay structures or benefits may result in direct or indirect age discrimination. Some pay structures potentially indirectly discriminatory because they are generally based on length of service or seniority rather than age. Consultation showed that the majority of employers and employees accept and welcome such benefits.

57. The options for implementation were:

- (a) Requiring employers to objectively justify such benefits; and
- (b) Providing that benefits which meet certain criteria are justified. Where benefits met those criteria employers would not need to objectively justify them

58. Option (b) enables firms to retain benefits which meet the specified criteria without further objective justification – thereby securing the continuing provision of a wide range of benefits that are widely

accepted and welcomed. If necessary, employers will be able to objectively justify other benefits under the general provisions allowing objective justification.

59. The implementation costs of the chosen option to business come to about £46 million. This will be a one-off cost which businesses are likely to incur either just before the legislation comes into effect or just after.

60. Where policies that employers feel they can no longer justify are removed, this may result in a small increase in fairness and equality. There may be some modest policy costs and benefits to employers, and employees where more equitable policies are put in the place of unjustifiable ones.

Vocational training

61. The definition of vocational training will follow the same approach as that adopted for the religion or belief and sexual orientation regulations, which prohibit discrimination by training providers. To reduce the burdens on FE and HE institutions in identifying which of their courses are vocational training within the meaning of the Directive, the implementing Regulations will cover all courses at FE and HE institutions. It should be noted that these Regulations do not cover schools.

62. It will be necessary for Universities and Colleges to remove or justify any age restrictions that remain in place when the age regulations come into force. Here, it is difficult to predict costs, but we anticipate that they would be minimal.

Macroeconomic implications

63. Key groups of beneficiaries from the legislation will be younger and older workers, although individuals of any age will be protected against age discrimination. The legislation will result in increased opportunities for affected individuals, largely through increased training, fairer promotion and recruitment practices, as well as a reduction in those retiring solely because they have reached their employers' normal retirement age. This will result in an increase in the labour supply, and a corresponding increase in growth.

64. Estimates of how much of an increase in GDP this will be is difficult to assess beforehand. The Department has considered using evidence from overseas and has modeled economic variables that might have an impact on the participation of different age groups.

65. Our initial assessment is that the impact of policies, excluding those on retirement ages, could result in an extra 15,000 to 29,000 employees in the workforce, resulting in an increase in GDP of between about £0.6 billion to £1.25 billion a year by 2016.

66. Assessing the impact of legislation relating to retirement ages has used a different methodology, by modeling the change in the number of individuals who will be retiring against their will as result of the legislation. Our proposed option is estimated to result in an increase the number of workers of between about 4,000 to 22,000, resulting in an increase in GDP of about £0.1 billion to £0.7 billion by 2016.

67. The total increase in the workforce could, therefore, be between 19,000 and 51,000, resulting in an increase in GDP of between about £0.7 billion to £2.0 billion by 2016. This is a plausible figure when compared with the estimate of the cost to the economy of low employment amongst older workers by the Cabinet Office of £16 billion each year. For further details of the analysis of the impact on the macroeconomy see Annex A.

Equity and fairness

68. There is evidence that discrimination affects, to varying degrees, both older and younger workers. Both groups of people may be excluded from promotion and training, or other terms and conditions of employment because of their age.¹⁷ Discrimination can also affect all economically active individuals – broadly speaking those who are in work and those that are looking for work - to the extent that job seekers are discouraged from applying for jobs at recruitment stage.¹⁸ Issues of equity and fairness that are specific to individual policy strands are discussed in the relevant RIAs.

Race equality Impact assessment

69. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firms impact test

70. Although the Age Positive Code of Practice has been in existence since 1999, the legislation will be new and will also require 'step changes' in attitudes. It will cover all firms and there is likely to be a significant effect on smaller firms. They will bear disproportionate implementation costs, which are expected to be relatively high, because of the complex nature of the subject. The cost per small firm is expected to be about £140. Small firms are also more likely to rely on informal methods, such as word of mouth and the use of informal contracts, and so may need to take more actions than larger firms to comply with the Directive. Very small firms (those employing fewer than 10 people) are also those that are more likely to employ workers over 65.

71. Small firms will be proportionately more likely to be taken to Employment Tribunal.

72. Like all companies, small firms will benefit from improvements in the functioning of the labour market. Consultation so far has led to a mixed reaction from small firms, with some not concerned while others

¹⁷ The Directive (article 6) provides that Member States may provide that differences of treatment on grounds of age shall not constitute discrimination if, within the context of national law, certain requirements are met. These are (1) they must be objectively and reasonably justified by a legitimate aim, including legitimate employment policy, labour market and vocational training objectives; and (2) the means of achieving that aim are appropriate and necessary.

¹⁸ In addition, those who are seeking or undertaking vocational training and who are not economically active could also be potentially affected, as well as those who receive pay but who are not economically active. However, we are uncertain at the moment the extent to which these groups are being discriminated against.

have raised business interests, which might need to justify some form of age discrimination. We have explored these issues further in a structured set of focus groups.

73. On the whole the impact on firms of all the legislation is likely to be slightly negative – estimates put the impact on small firms over a ten year period at somewhere between a cost of £210 for each firm to a gain of £85. Further details see the Small Firm Impact Test at Annex B.

Competition assessment

74. The legislation on age discrimination is likely to lead to an increase in participation rates, as well as training and promotion opportunities for older and young workers. This will enhance competition in the labour market, as age is no longer used as a criterion or filter in these key decisions. As a result, talent and ability will be better matched to recruitment and training decisions. Labour market competition will also increase from tapping a greater pool of applicants, increased training and improved promotion prospects.

75. Competition filter tests (see the individual RIAs) point to no sector where competition between firms will be adversely affected by this legislation.

Enforcement, sanctions and monitoring

76. Experience of the current discrimination jurisdictions in Great Britain suggests there could be a significant number of tribunal applications. Evidence of age discrimination in the United States also suggests there could be large numbers of cases, though comparisons with the US should be treated with caution. Based on our expectation for discrimination claims under the other jurisdictions, we assume an average of 8,000 Employment Tribunal claims per year. We do not attempt to estimate the main jurisdictions that applications will fall under, but there is likely to be a some falling under unfair dismissal because of the likely lifting of the age restriction in this area. The average cost of an ET application for an employer is on average around £4,900 and for the taxpayer £990.¹⁹ If we assume that in about 75 per cent of these tribunals the employer is not at fault then the cost for employers would be about £30m. The cost to the Exchequer costs of will be around £8m each year.

Implementation and delivery plan

Implementation period

77. Subject to parliament's approval the regulations will be in place by March 2006, at least six months before they come into force in October 2006.

78. Good practice guidance and detailed pensions guidance will be available around the same time to help employers prepare. In addition to that, we are holding a conference in April to widely publicise the legislation.

¹⁹ See "Findings from the 2003 survey of Employment Tribunal Applications" Employment Relations Research Series, 2004

Transitional Arrangements

79. Respondents stressed the importance of knowing what the transitional arrangements for the retirement and unfair dismissal provisions would be. Our intention is to produce the transitional provisions at the same time as the regulations are laid before Parliament. The provisions will aim to provide protection to employers.

Developing awareness

80. We have recently launched a 'capacity building' programme. The aim of the programme is to develop the capacity of intermediary organisations (NGOs/trade unions etc) to deliver advice and guidance to individuals on their new rights as a result of the regulations and to inform employers of their new obligations. We have specifically asked for applications that will provide a strategic capability to CEHR, the body with responsibility for age from 2007.

Common Commencement Date

81. Although some employer organisations suggested implementation should be delayed until 1 December 2006, the last date for implementing the Directive, we propose to keep to the 1 October implementation date, as (in line with Trade Union views) we consider that the benefits to employers of maintaining a common commencement date for employment (and other) regulation outweigh the benefit of an additional two months' preparation time for business and individuals.

Engaging with stakeholders

82. Our approach to developing the draft regulations has been through progressive consultations. *Towards Equality and Diversity* in 2001 aimed to explore what age-based practices employers had, why they had them, and if and why they needed to keep them. In 2003 *Age Matters* sought views on options for legislation.

83. Our aim has been to work collaboratively with stakeholders – business (large and small), Trade Unions, age interest groups, and managers. We have done this formally through the Age Advisory Group, and informally through continuing discussions with stakeholders.

84. Engaging stakeholders throughout the process enabled us to understand the potential practical problems faced by business and individuals in removing or justifying age-based practices.

85. We will continue to engage stakeholders formally through AAG and with others on a one-to-one basis or in particular groups leading up to legislation. We will also consult main stakeholders as we develop transitional provisions, which will be included as part of the final regulations laid before Parliament. Since guidance is crucial to successful implementation of age legislation, Acas – who are preparing guidance – are consulting stakeholders widely as it develops, in particular small business at whom guidance is specifically aimed.

Guidance

86. Many of the comments (including many of the comments from age lobby groups) related to what the guidance should include, and to the need for early guidance. We have passed these on to Acas who are

preparing the guidance and will be road testing it with stakeholders. They are consulting widely with stakeholders (small business in particular) as they develop and refine guidance further.

87. The *Coming of Age* consultation document contained the first explanation of the full draft regulations. Employers could use this to start thinking about what they needed to do – Chapter 2 of *Coming of Age* provided a checklist. That will help those with obligations under the regulations in their preparations, before full guidance is formally launched.

88. Good practice guidance, including separate guidance on occupational pensions, will be published as soon as possible after the Regulations are made, allowing employers at least six months to prepare for the legislation. At the same time the Department will publish an explanation of the law on the DTI website.

89. Guidance will be publicised through DWP's *Age Positive* campaign, as well the Acas website. The conference in April will be used as the platform for launching the guidance, and associated media activity will publicise its availability further.

90. We have also launched a 'capacity building' fund to provide grants, as we have done in relation to the sexual orientation and religion or belief regulations, to interim bodies to educate and train people to advise on the legislation.

Post-implementation review

91. The DTI and the Department of Work and Pensions have commissioned a series of baseline studies, which includes a survey of employers' awareness, perceptions and practices on age discrimination in employment and a study of the age dimension of employers' recruitment and promotion decisions. The first of these studies was carried out in 2005 before the legislation came into place. DTI anticipate that the first follow up surveys will be carried out between two to four years after the legislation has been implemented. DTI in 2005 also commissioned some case study research to look at employers' preparedness for the new legislation and the management and organizational implications. DTI will consider commissioning further case study research to look at the actual impact on management and business organisation. Further details of monitoring plans are given in the individual RIAs.

92. DTI's 2005 Fair Treatment at Work Pilot Survey will establish a baseline of employee perceptions and experience of age discrimination in the workplace, against which future progress can be gauged. The survey will include additional interviews with both older and young workers, to ensure a sufficient sample sizes for analysis. Provided the pilot is successful, it is intended to repeat this survey every two or three years.

93. Other, more specific, elements of proposed research, monitoring and evaluation are included in the six RIAs on the different age discrimination strands.

Summary and recommendations

94. In implementing the legislation, the Government will aim to improve opportunities and choice for individuals, and encourage labour market participation, whilst still allowing employers to manage their business effectively. Several options have been considered. The general option chosen has been to introduce legislation to outlaw age discrimination except where it can be objectively justified. The costs and benefits of the proposed options on each policy strand are outlined in Table 7 below.

7. Summary of quantifiable costs and benefits of age discrimination legislation

	Benefits Annual	Costs Annual	Costs One-off
Employers			
Total implementation costs for all policy strands (Awareness and decision making)			£219m
Total enforcement		£30m	
Retirement	£4.4-21m in first year; £4.4-21m in year 10	£0.5-2.5 in first year; £0.5-2.5 in year 10	
Statutory redundancy payment		£4.5m-£9.1m	
Unfair dismissal awards		£2.4m-£2.8m	
Recruitment	£14-85m	£4.0-8.8m falling to £2.5-6m by 2011	
Training	£51-420m	£44-370m	
Promotion	£14-180m		
Individuals			
Retirement	£12-67m in first year rising to £51-300m by year 10		
Statutory redundancy payments	£15m		
Training	£5-42m		
Promotion	£27-140m		
Exchequer			
Enforcement		£8m	
Retirement	£8.0-52m in first year rising to £42-240m by year 10		
Statutory redundancy payments		£1.2m	£0.1m
Unfair dismissal awards		£0.5m	
General	Improvements in the macroeconomy will mean higher tax and national insurance receipts.		
Macroeconomy	Total macroeconomic benefit could be about £0.7-2.0bn by 2016.		

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

**Gerry Sutcliffe
Parliamentary Under-Secretary of State
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Impact on the macroeconomy

1. Measures to reduce discrimination should broadly result in better matching of individuals to jobs. This could arise because individuals are no longer discriminated against (because of their age) when selected for promotion and training. It will also result in fairer criteria for selecting candidates for jobs and for redundancy, and in deciding when people should retire. This should encourage people to stay on in the labour force and may lead to increases in productivity.²⁰
2. Some may believe that increasing employment rates for some means reducing employment rates for others. This stems from a belief that there are only a certain number of jobs in the economy. This is commonly referred to as the ‘lump of labour fallacy’ and is not generally supported by empirical evidence.²¹
3. There may also be a belief that an increase in the labour supply will depress wages. While this may be true in the short run, it is unlikely to be sustained as the economy expands in response to this increase in available workers.
4. Increases in productivity have been considered in the individual RIAs. The impact on the labour force due to fewer individuals feeling that they have to retire solely because they reach the retirement age has been considered in the retirement age RIA. The following considers the impact of other policies on the labour supply.
5. Previous work on the lower employment rates of workers of certain age groups has looked at factors that are wider than just discrimination. For example the Cabinet Office report on older workers estimated that low employment amongst older people reduced GDP by around £16 billion.²² This is not solely due to discrimination, but it is useful in gauging an upper limit to any impact that legislation will have on older workers.
6. As part of our consultation process the Department invited academics and specialists in Government to consider the best way of modelling the impact of discrimination legislation. The conclusions were that assessing the impact of the legislation would be a problem before the event²³, but if we were to do so we should use, where possible, a range of methodologies. This would include looking at international evidence, building our own model of what impacts on the employment rate of different aged individuals based on the theories of labour supply and demand,

²⁰ There is widespread academic evidence to support this assumption. For instance in S. Lissenburgh and D. Smeaton (2003) *Employment transitions of older workers: The role of flexible employment in maintaining labour market participation and promoting job quality* the authors concluded that age remains the most significant factor in explaining the likelihood of ‘exiting’ the labour market for both men and women even when controlling for other factors. Some studies also find direct evidence of age discrimination in employment (see Casey B. and Wood S. (1994) *Great Britain: firm policy, state policy and the employment of older workers* and Hayward B., Smith and Davies G. (1997) *Evaluation of the campaign for older workers* The Stationary Office, London.

²¹ This is at the level of the economy. At the level of the firm, there may be a fixed amount of labour, at least in the short-term to medium term.

²² See Cabinet Office (2000) *Winning the generation game - improving opportunities for people aged 50-65 in work and community activity*. Performance and Innovation Unit Report.

²³ Partly because there are no reliable indicators for discrimination, and even if there were it would be hard to say what impact legislation would have on this, and partly because other changes, such as those relating to pensions, could easily swamp the impact of legislation.

and any evidence of the impact of other equality strands such as the Sex Discrimination Act and the Race Relations Act.

7. So far we have found little useful work on the impact of existing GB laws on employment rates. Good international evidence mainly relates to the US. The results show an increase in employment rates of those aged 60 and over of around six percentage points resulting from changes to legislation on age discrimination.²⁴ This is a large effect and there are some institutional factors that limit the usefulness of comparisons with the US – not least because it only covers direct discrimination. Even if we assumed a more conservative three percentage-point increase in employment rates for those aged 60 to 70 years, this would result in an increase in GDP of the order of £6.4 billion by 2016. This seems high, especially in the light of the initial results of modelling work (see paragraphs below).²⁵

8. The modeling work looked at range of factors that have the potential for impacting on employment rates of different aged workers, including discrimination.

9. First, we looked at variables that could affect the demand for, and the supply of, older workers. The demand for older workers was modelled as a function of the wage ‘premium’ associated with those over 49, the qualifications of those aged over 49, capacity in the economy, and the industrial mix. The supply of older workers was, likewise, modelled as a function of the wage premium associated with those over 49, the health of those over 49, the benefits available to those aged over 49, and the availability of flexible working arrangements in the economy. Both models also included a measure of perceived discrimination against older workers. There is no reliable, regular measure of discrimination against older workers, so we proxied discrimination using a series from the LFS: those aged over 49 not looking for work because they believed there were no jobs available.²⁶

10. Later, we studied the demand for, and the supply of, younger workers. The demand for younger workers was modelled as a function of the wage premium associated with those aged 16-24, the qualifications of those aged 16-24, capacity in the economy, and the industrial mix. The supply of younger workers was modelled as a function of the wage ‘premium’ associated with those aged 16-24, the qualifications of those aged 16-24, the number of dependents, 16-24 year olds involved in government training schemes, and the availability of flexible working arrangements. Discrimination was proxied using another LFS series: those aged 16-24 not looking for work because they believed there were no jobs available.

11. Throughout, data used covers the period 1994-2003, primarily from the Labour Force Survey²⁷ (LFS), but also the Pensioners’ Incomes Series²⁸, and the Government Actuary’s Department.

²⁴ Most of this effect has come from individuals staying in jobs later rather than higher rates of hiring of individuals. See Neumark D. and Stock W. (1999) *Age discrimination Laws and Labour Market Efficiency* Journal of Political Economy, Vol. 107 (5) pp. 1081-1110.

²⁵ See Meadows P. *Retirement ages in the UK: a review of the literature* Employment Relations Research Series 18, Department of Trade and Industry.

²⁶ A large proportion of this group may not be looking for reasons other than age discrimination, and we have taken this into account when assessing the impact of a reduction in age discrimination (as approximated by this variable) on total employment.

²⁷ The Labour Force Survey is a UK quarterly survey of individuals.

²⁸ The Pensioners’ Incomes Series 2002/03, produced by the Department for Work and Pensions, includes annual incomes data for recently retired pensioners, based on fiscal years at FY2002/03 prices.

12. Concerning the demand for older workers, the regression results suggests that a 1% improvement in our proxy for discrimination will lead to a 0.039% increase in the demand for older workers.²⁹ There is, however, a strong possibility that causality can work both ways here, with a decrease in our proxy for discrimination arising from an increase in the numbers of older workers in employment. We have, therefore, assumed that just 5-10% of those not looking for work because they believe there are no jobs available are as a direct result of age discrimination.³⁰

13. Using this assumption, age discrimination legislation is therefore likely to increase the demand for older workers by between 15,000 and 29,000 by 2016. This, in turn, will result in an increase in GDP of between £0.6 billion to £1.25 billion a year by 2016³¹. This assessment should be treated with caution, given the uncertainties described above. We do not therefore proportion the benefits to individuals, firms and the Exchequer. We do, however, intend to develop this analysis as a possible basis for trying to estimate the impact of the legislation after it has come into effect.³²

14. Concerning the demand for younger workers, the regression results suggest that the demand for 16-24 year olds will not be significantly affected by an improvement in our proxy for discrimination.³³

15. In assessing the impact of legislation on retirement ages a different methodology was used. This used an assessment of the change in the number of individuals that will be retiring against their will as result of the legislation. Our proposed option is estimated to result in an increase in the number of workers of between about 4,000 and 22,000 resulting in an increase in GDP of about £0.1 billion to £0.7 billion by 2016.

16. The total increase in the workforce could, therefore, be between 19,000 and 51,000 - resulting in an increase in GDP of between £0.7 billion and £2 billion by 2016. This is a plausible figure when compared with the Cabinet Office's estimate of the cost to the economy of low employment amongst older workers, referred to above: £16 billion each year.

²⁹ The model points to a larger increase in the supply of older workers. We have assumed that this increase in supply is unlikely to be taken up in full by employers.

³⁰ It is of interest to note that this indicator has declined remarkably over the period in question, from around 128,000 people at the end of 1993 to around 40,000 at the end of 2002. As a percentage of the unemployed or inactive aged over 49, it has fallen from 1% to 0.3% over the same period. Unfortunately we do not have any substantiating evidence that age discrimination has also declined during the period. This points to caution in the assumptions that we should have on the impact of discrimination in this area.

³¹ In line with Treasury advice and the methodology on the retirement ages, we have assumed the proportional increase in GDP is the same as the proportional increase in wages that results from the proportional increase in labour. This assessment compares with illustrative calculations used in the RIA published in July 2003 - of an increase of between £2 billion to £5 billion based on an increase in the probability of staying in employment of two per cent.

³² This would be very much a long-term project and will take place alongside other monitoring and evaluation work.

³³ Nor is the supply of older workers likely to increase significantly.

Small Firms Impact Test

1. The Small Firm Impact Assessment draws on evidence from:
 - A Research Study commissioned by the Small Business Service (SBS) on the impact on small businesses of equal opportunities legislation. This consisted of three focus groups around the country, with different sizes of small firms, which took place in March 2002. Questions included some on age discrimination.
 - A Research Study commissioned by the SBS on the impact of age discrimination legislation, with a focus on retirement ages. This consisted of three focus groups in Manchester run by MORI in March 2003.
 - Two separate focus groups (with a small business and 6 organisations representing small businesses) in August and December 2002.
 - Email feedback from a member of a small business forum.
 - The Workplace Employment Relations Survey 1998.
 - SBS statistics on the number of small firms.
 - Statistics from the Labour Force Survey.
 - The Evaluation of the Code of Practice on Age Diversity in Employment prepared for the Department of Work and Pensions in September 2001. This looked at practices on age discrimination across different firm size.
 - Responses to the *Age Matters* consultation in 2003.
 - Responses to the *Coming of Age* consultation in 2005

Policy costs

2. Although smaller firms are currently less likely to employ older workers³⁴, very small firms as a whole do have a large proportion of workers over 65 and they may need to take more actions than larger firms to comply with the Directive. Analysis of Workplace Employment Relations Survey 1998 shows that small firms are more likely to rely on informal methods such as word of mouth and use of informal contracts. Just under 40 per cent of establishments with between 10 and 24 employees have no equal opportunities policy on age, compared to 58 per cent of establishments with more than 500 employees. This also came out of the SBS case studies, with employers emphasizing how much they rely on informal dialogue with employees. These practices make them particularly susceptible to claims and could mean they are proportionally more likely to be taken to an Employment Tribunal.³⁵

³⁴ 19% of establishments with 10-24 workers have no workers over 50, compared to just 1% of those with 500+ workers. Of course, the legislation will not just cover older workers.

³⁵ 41% of claims to Employment Tribunals involve firms with less than 50 employees (Source: Survey of Employment Tribunal Applications 2003) and yet small firms employ only about 27% of employees (Source: Small Business Service)

3. Future demographic changes will be an important driver here as research shows that SMEs have low awareness of potential changes in the next 10 years.³⁶ Indeed, generally the SBS research has shown that retirement may not be something that many small businesses think about or plan for.

4. Furthermore, there is some evidence that small firms rely more on discriminatory methods than larger firms. 25 per cent of establishments with 10-24 employees use age as a recruitment factor compared to just 9 per cent of establishments with 500 or more employees. This finding also came up in the SBS research with some employers saying that they do discriminate at the recruitment stage on the basis of age. Reasons given were image and an ability to relate to customers.

5. Smaller employers also saw problems with having older workers. Some thought that they would find it harder to master new technology and others thought that they might not have the stamina to do longer hours. Problems around getting “new blood” into the company were also mentioned.

6. However, other firms (including our email response, see paragraph 1, bullet 4) were more relaxed, saying that they either relied on merit and performance for their employment decision or that it is hard to predict how older workers will perform. Some could see the benefit of a later retirement age in terms of less costly pensions. There was, however, a general desire for the legislation to be such that they are in control of when workers in their firms retire.

7. So although small employers are less likely to have an older worker, the prevalence of less formal procedures and the probable existence of more discriminatory practices make those that do have older workers more vulnerable to being taken to an Employment Tribunal. Furthermore, we assume that eventually most small firms will be affected, either through the recruitment process, or because they will at some stage have an older worker.

Implementation costs

8. Small firms find it harder to come to terms with new regulations than medium and larger companies. Many small employers (those with fewer than fifty employees) will have neither dedicated HR arms or formal systems in place. They also say that they do not know where to look.

9. We have discussed the implementation costs of different policy strands in the relevant RIAs. On the whole, given the size of their workforce, small firms bear a disproportionate administrative burden. The exception is for occupational pensions, where small firms are much less likely to be providing occupational pensions compared with larger firms. Small firms will be expected to spend between about five hours reading and understanding the guidance on age. Those that have an occupational pension scheme may also have to spend an additional day considering whether their age-based rules are consistent with the new legislation and whether some rules need justifying or removing. We have identified no implementation costs with reference to legislation on redundancy payments and unfair dismissal (see relevant RIAs for details). Table 1 gives a breakdown of the implementation costs associated with each strand of the legislation as well as the total cost.

³⁶ Promoting Age Diversity in Employment with Small and Medium Sized Employers see http://www.dwp.gov.uk/publications/dwp/2001/nsnr/annex_c.asp

1. Implementation costs for small firms

	Cost per firm (£)	Costs for all firms (£m)
Retirement ³⁷	50	58
Redundancy payments	0	0
Unfair dismissal	0	0
Training, promotion and recruitment	50	58
Pay and non-pay benefits	25	29
Occupational pensions ³⁸	18	21
Total	143	166

10. Even if small employers currently do not employ older workers or younger workers, future demographic changes may change this and so the full five hours may be a gradual process spread over several years for small firms. We do not model the path of awareness costs.

Total impact

11. The total impact on small firms includes implementation costs and policy costs. If we exclude statutory redundancy pay and unfair dismissal awards, for which the final formula has not yet been proposed, the total average impact on small firms will be about between a cost of about £24 million each year to a benefit of about £10 million each year.³⁹ In other words, the impact of the legislation is on balance likely to be slightly negative (A loss of about £210 to a gain of about £85 per small firm over ten years). The details are in Table 2.

2. Total impact of legislation on small firms (average yearly impact)

	Average yearly impact (£m)
Retirement ⁴⁰	+£3.1m to +£38m
Recruitment, training and promotion	-£0.8m to +£30m
Total implementation costs	-£16.5m
Total cost of tribunals	-£7.1 to 7.8m
Total	-£24m to +£10m

Note: The average yearly impact is the net present value of the costs and benefits over the first ten years divided by ten and discounted at 3.5%

³⁷ This assumes that an option of a default retirement age of 65, allowing employers to objectively justify their own retirement age if they wish and with a duty to consider, is adopted as recommended.

³⁸ This is the cost per firm including those who do not have occupational pension schemes. The average cost for just those with an occupational pension is about £340.

³⁹ This is the net present value of all costs and benefits over the first ten years after implementation, divided by the number of years (ten). The Treasury rate of 3.5% has been used to discount future costs and benefits. If redundancy payments and unfair dismissal awards are included the net impact would be a cost of £35m to a benefit of £19m, depending on the option chosen.

⁴⁰ This assumes that an option of a default retirement age of 65, allowing employers to objectively justify their own retirement age if they wish and with a duty to consider, is adopted as recommended.

Retirement ages

November 2005

<http://www.dti.gov.uk/er>

Purpose and intended effect of measure

Objective

1. The overall aim of the legislation is to promote greater choice for older workers about when they retire, without creating an unnecessary burden on business that may have an undue negative impact on productivity and employment growth. This will contribute towards a Government target of increasing the employment rate of those over 50 and will provide one part of the response to the effects of an ageing population.

Background

2. In 2006 the Government will bring legislation into force under the European Employment Directive outlawing age discrimination in employment and vocational training. Employers' mandatory retirement ages are one form of direct age discrimination that will fall under the legislation. They will be unlawful unless objectively justified. This regulatory impact assessment (RIA) discusses the costs and benefits of a range of options in respect of employers' mandatory retirement ages.

3. Legislation on retirement ages is being considered in a context where average retirement ages have been declining over the longer term. In 1950 the average retirement age for men in the UK was about 67 years. In 2001 it was about 63 years.⁴¹ Furthermore a majority of the UK workforce retire before they reach the normal retirement age in their employment. This is at a time when life expectancy has been rising.⁴² Retirement is something that most workers look forward to and hence the proportion of those who are still in employment after 65 is low.⁴³

4. Thus the number of workers that will be affected by a decision on legislation on retirement age is likely to be small in proportion to the size of the overall workforce. One would therefore expect the impact to be modest as well, relative to the size of the economy. International evidence supports this view (except in some detailed occupational sectors).

⁴¹ For women it was 64 years in 1950 and 61 years in 2001. 1950 source: Blöndel and Scarpetta (1998) *The Retirement Decision in OECD Countries*, OECD Economics Department Working Papers 202; 2001. Source: European Commission (2003) *Employment in Europe 2003 Recent Trends and Prospects*.

⁴² In 1961 the life expectancy of a 60 year old man was 15 years. By 2000-02 in Great Britain it was 20 years. Source: Government Actuaries Department Life Tables See <http://www.gad.gov.uk/>.

⁴³ See Meadows, P (2003) "Retirement ages in the UK: a review of the literature on key issues" DTI Research Series no. 18 see <http://www.dti.gov.uk/er/emar/errs18.pdf>. Also the findings of the Joseph Rowntree Foundation on The Role of Flexible Employment for Older Workers, see <http://www.jrf.org.uk/knowledge/findings/socialpolicy/343.asp>

5. According to a recent study⁴⁴, those that currently choose to postpone retirement and continue working beyond the normal retirement age in their job tend to be women aged 60 to 65; those who are self-employed; those with intrinsically interesting jobs; and those who have a financial reason for continuing to work. For further discussion of the numbers who are retiring because of employers' retirement ages, see paragraphs 21 to 26.

Rationale for government intervention

6. Although rates of participation in the labour force have recently been increasing for both older men and older women, they remain substantially below that of other age groups, as shown in the Table 1.

1. Economic activity rates by age and sex

Age	Men	Women
18-24	78.7%	69.7%
25-34	92.0%	75.2%
35-49	91.6%	77.9%
50-64(M); 50-59(W)	75.0%	69.1%
65+(M); 60+(W)	8.8%	9.8%

Source: Labour Force Survey estimates for Autumn 2004

7. The evidence suggests that some individuals, albeit a relatively small proportion of all those retiring, are being forced to retire against their will by their employer.⁴⁵ Some workers may be therefore being forced to retire when they are still capable and willing to do a good job. The scale of the impact on labour participation is illustrated in paragraph 73.

8. This could be because employers are negatively stereotyping older workers as incompetent, or as having deteriorating competence. In fact, there is no evidence that workers' productivity does generally decline with age⁴⁶, at least not before the age of 70.

9. Economists have various explanations as to why employers might discriminate. One is that employers may not be pure profit maximisers and may be less inclined to recruit certain workers because of their prejudices. Other explanations rely on the difficulty that risk-averse employers have of discerning some types of workers' productivity, or on employers taking account of discrimination from other workers, unions and consumers. A simple explanation is that some employers may just be misperceiving their workers' productivity. Added to these there may be a more pervasive view throughout society that older workers should 'make way' for younger workers to give them better job opportunities.

10. The risk for the economy of people being forced to retire against their will is that their productive potential is being lost. This represents a cost to employers, and the workers concerned will be negatively affected by being forced into their less-

⁴⁴ See Meadows, P *ibid*.

⁴⁵ See Meadows, P *ibid*: "Involuntary retirement at normal retirement age is not common." DWP Research Report 200 *Factors affecting the labour market participation of older workers*, 2003 finds that 60 per cent of employees face an employer's fixed retirement age, and around 20 per cent of those facing a fixed retirement age retire at that age. This would not necessarily mean that the retirement was involuntary. However, given the same report found that 18 per cent of those retiring early did so because they were made redundant/dismissed/had no choice, it seems reasonable to conclude that some of the retirements at employers' fixed retirement ages are involuntary, if not very common.

⁴⁶ Apart from in particular jobs.

favoured outcome of retirement. This loss of productive potential has to be set in the context shown in Table 1 above, where older workers' participation is already comparatively low, and the negative effect of changing demographics on the dependency ratio of the working to non-working populations. This effect has implications for the affordability of welfare and pension obligations.

Consultation

11. The Department has taken a progressively consultative approach on how to implement age discrimination legislation in Great Britain. The first formal consultation in 2001⁴⁷ covered all the new equality strands. On age it sought to find out what age-based practices were used by employers, why they used them, whether they wanted to keep them and why. At the end of 2002 the Department launched a second consultation⁴⁸ that focused mainly on strands other than age, as well as the general approach to discrimination legislation. In 2003 the Department launched its third consultation⁴⁹, which asked for views on proposals for outlawing age discrimination in employment and vocational training, including options for retirement ages. A final consultation on the draft regulations was held in mid 2005.⁵⁰

12. As well as informal consultation, the Department has had a strategy of continuing engagement with main stakeholders both informally, and formally, with the Age Advisory Group that is chaired by the Minister. We have sought views on policy options, as well as drawing on stakeholders' expertise to inform ourselves better about employment practices.

13. In *Age Matters*, we asked whether we should set a national default retirement age. The response was divided, with 52 per cent in favour of a default retirement age and 43 per cent against. In addition to the two written consultations, *Towards Equality and Diversity* and *Age Matters*, we held a series of meetings with representatives of employers, trade unions and age equality organisations in 2004 to discuss the issue of retirement ages. These meetings confirmed the conclusion from *Age Matters* that opinions were and would remain divided on this issue.

14. As regards the level of a possible default retirement age, the response was more one-sided: only 24 per cent were in favour of 70 as the default retirement age; 65 per cent were against.

15. Following the final consultation, we have clarified some of the drafting of the 'duty to consider' procedure but have not tightened up the procedure as some unions had sought (e.g. by requiring employers to give reasons) as this would undermine the Government's justification of the default retirement age. However, in light of consultation responses we have changed two of the notice periods, so that employees must make a request to continue working beyond the retirement age, at least three months before retirement date rather than six weeks as originally proposed; and employers must give at least a month's notice of retirement if the dismissal is not to be automatically unfair as opposed to the two weeks notice in the draft regulations. Neither of these changes are changes to policy. They simply reflect respondents concerns that the notification dates in the draft regulations would be unworkable.

16. A number of respondents criticised the provision enabling employers to discriminate against applicants over 65 in recruitment. This is a necessary adjunct to

⁴⁷ *Towards Equality and Diversity: Implementing the Employment and Race Directive.*

⁴⁸ *Equality and Diversity: The way ahead.*

⁴⁹ *Equality and Diversity: Age matters.*

⁵⁰ *Equality and Diversity: Coming of Age.*

the default retirement age, and we will make it clear that it will be reviewed at the same time, in 2011.

Options

17. The options being considered in this Regulatory Impact Assessment are:
 - a. No national default retirement age⁵¹ (DRA) and employers not able to set their own retirement ages;
 - b. No national DRA, but allowing employers to set their own retirement ages, which they would potentially have to justify at Employment Tribunal, hence employer-justified retirement ages (EJRAs);
 - c. No national DRA, allowing employers to set an EJRA, and also giving employees a new right to request to work beyond their employer's retirement age (if they have one)⁵²;
 - d. A national DRA of 65 and allowing employers to set an EJRA, and also giving employees a right to request to work beyond their employers' retirement age (if they have one) or 65 (if the employer chooses to make use of the DRA).
18. Failing to implement the Directive (i.e., doing nothing) would leave the UK non-compliant with the European Directive. Option d is the closest to legislation to maintain the status quo.

Costs and benefits

19. In analysing costs and benefits we need to look at the impact on employers, on workers⁵³ and on the macro-economy and the Exchequer. We need to make assumptions about the reaction of workers and employers to the legislation and about the associated costs and benefits. We also need to make assumptions about the behaviour of individuals and firms in the absence of legislation (the do-nothing approach).⁵⁴

Sectors and groups affected

20. The legislation applying to retirement ages will affect employers and workers.⁵⁵

⁵¹ A national default retirement age will allow employers either to set a retirement age within their firm at or above the level of the default retirement age, or to retire employees in direct reliance on the default retirement age. Where employers want to retire employees who are younger than the default retirement age, the Directive will only allow this if it is objectively justified.

⁵² The right to request ensures that individuals are not penalised by asking to continue to work. It also confers a duty on the employers to consider requests seriously, by holding a meeting with the individual and, if relevant, giving reasons why they do not want the individual to continue working for them. These reasons would not have to be defended at an Employment Tribunal.

⁵³ We are assuming that the legislation (with the exception of the right to request working past EJRA/DRA) does not just cover employees but also other classes of workers such as agency workers, home workers, etc.

⁵⁴ In estimating the numbers of older workers participating in the workforce we have used the Government Actuary's Department population projections and employment rate projections from the Office of National Statistics.

⁵⁵ The age discrimination legislation will cover some categories of worker not covered by the definition of an employee, although the right to request working past an EJRA or DRA would only apply to employees.

21. All employers employing older workers will be directly affected, and even those who do not currently employ older workers will have to make sure they are compliant with the legislation.

22. Depending on the option, the direct effect on workers will be to allow many who are currently being asked to retire, but who still want and are still capable of doing a good job, to stay at work longer. A recent survey⁵⁶ found that over half of those approaching retirement (59 per cent) had been working for employers who had a fixed retirement age. Men were more likely to have had a fixed retirement age than women (69 per cent compared with 52 per cent). For about three-quarters of men this was at the state pension age, while for women it was 58 per cent.

23. However, only a small fraction of these will be retiring solely because they have reached the normal retirement age in their place of work. The report on the survey found that "there is no evidence that employers' fixed retirement ages exert a widespread influence on decisions to retire before state pension age. However, there is evidence that employers' fixed retirement ages may prevent some people from continuing to work beyond state pension age". Even though women tend to retire earlier, they seem less likely to be doing so involuntarily.⁵⁷

2. Assumptions of percentages of workers who retire only because they reach their employer's fixed retirement age

Age	Men	Women
60	1-3%	2-4%
61-64	0-0.5%	0-0.5%
65	3-7%	1.5-2.5%
66-75	2-5 falling to 0-0.5%	1-2 falling to 0%

Source: DTI assumptions based on available evidence

24. Table 2 outlines our main assumptions on the proportions who are currently retiring only because they have reached their employers' normal retirement age. It takes into account the evidence above, as well as evidence from the 1994 Retirement Survey.⁵⁸ It should be noted that some of this evidence appears to be contradictory and so these assumptions are highly uncertain and are for the purposes of this impact assessment only. Please see Annex A for further details of the basis for these assumptions.

25. A right to make a request to an employer to work beyond the EJRA or the national DRA would apply to all employees approaching their EJRA or the national DRA. Of these, it is assumed that it will be potentially of use to those employees who are being forced to retire against their will. The assumptions on the numbers affected for **options c and d** are outlined in Annex A.

Assumptions

26. The main assumptions used in this cost benefit analysis are summarized in Annex A.

⁵⁶ See Humphreys, A., Costigan, P., Pickering, K., Stratford, N. and Barnes, M. (2003) *Factors affecting the labour market participation of older workers*. Department of Work and Pensions Research Report 2003.

⁵⁷ "The timing of retirement is determined only by the fixed age in their job for around one in ten men and one in 100 women". Meadows, P *ibid*

⁵⁸ As reported by Meadows, P.

27. Under **option a** employers will only be able to dismiss workers on fair grounds such as incompetence or misconduct. This may prompt many of them to review the characteristics and expectations of their staff. Some may want to review their performance measurement systems, which may not be sophisticated enough to distinguish marginal underperformance.

28. Under **options b, c and d** companies will be able to adopt an EJRA. If they do so, they may be challenged to justify this at an Employment Tribunal. They may instead choose to rely on their performance systems to identify and act on declining performance. As with **option a**, these systems may require some review.

29. Many companies currently have a retirement policy, although the proportions vary by company size.⁵⁹ Where a retirement policy exists many workers can choose to retire after their company's normal retirement age.⁶⁰ However, current practice takes place in the context of workers not having the ability to claim for unfair dismissal at or after the employer's normal retirement age or, if there is none, after state pension age (SPA). Those companies that do not have retirement policies or whose retirement policies are flexible (upwards) can currently afford to be relaxed.

30. Under **options b, c and d** the numbers of employers who decide to have their own EJRA will depend on:

- a. *Each option* – No DRA may mean more employers would consider having their own EJRA.
- b. *The flexibility of their existing retirement policy* - Many employers, especially smaller companies, allow all their workers to stay on beyond the company normal retirement age if they wish.⁶¹ Thus these employers may decide that there would be limited benefits in adopting an EJRA that would run the risk of challenge at an Employment Tribunal.
- c. *The presence of workers whose performance diminishes with age* - There are arguably a number of classes of workers, such as deep-sea divers, who run a health and safety risk if they continue to work after a certain age. This might tempt employers to adopt an EJRA for part of their workforce.
- d. *The effectiveness of performance and appraisal systems* - Many employers have formal appraisal systems for non-managerial staff.⁶² However, some may be more effective than others. This will in part depend on the nature of the work, with poor performance being easier to establish in some cases than in others. Any strengthening of performance and appraisal systems will probably need to apply to the whole of the workforce irrespective of age, in order to avoid accusations of age discrimination. Some employers

⁵⁹ The Evaluation of the Code of Practice on Age Diversity in Employment (prepared for the Department for Work and Pensions in 2001) showed that of the companies that had an employment or recruitment policy, 57 per cent of small firms, 62 per cent of medium sized firms and 70 per cent of large firms had one that covered retirement. However, it should also be noted that the evaluation found that 45 per cent of small firms, 26 per cent of medium sized firms and 11 per cent of large firms had no written or verbal employment or recruitment policy at all.

⁶⁰ Disney, R, Grundy, E and Johnson, P (1997) "The Dynamics of Retirement" DSS Research Report No 62.

⁶¹ The Evaluation of the Code of Practice on Age Diversity in Employment found that on average over the three waves of the Code of Practice, 39 per cent of employers let all their employees work past the company retirement age if they wished to do so.

⁶² The Workplace Employee Relations Survey 1998 found that 62 per cent of employers had a regular appraisal system.

may consider that the bureaucratic costs would outweigh the benefits such that they would prefer to set up their own EJRA and to run the risk of being taken to a tribunal.

- e. *The presence of certain types of workers* - Some workers like to work beyond the current normal retirement age because they enjoy their work.⁶³ Women may be more likely to want to work beyond their current normal retirement age, because they tend to have accrued less pension entitlement, mainly because of career breaks.
- f. *The ability that they have in recruiting younger workers* -Employers may find it increasingly hard to recruit younger⁶⁴ workers as the proportions begin to fall after 2005 due to an ageing population (shortly before the new regulations become effective).⁶⁵ Some employers may therefore opt not to set an EJRA, thus encouraging their older workers to think about the possibility of retiring later to make up for this deficit.
- g. *The cost and uncertainty of being taken to an Employment Tribunal* - Justifying objective criteria for an EJRA could be costly and have an uncertain outcome. There are likely to be a few high profile cases in the early years of implementation, whose outcome will have an impact on the decisions of other employers.⁶⁶

31. Assessing how many firms will set an EJRA under **options b, c and d** is therefore difficult. It is likely, however, that certain public sector employers (such as the civil service and the police) may want to set an EJRA for some or all of their workers because of concerns over health and safety or work performance (although the latter may be difficult to justify, given the evidence does not seem to support the proposition that productivity declines with age, all else equal).

32. Table 3 sets out our assumptions regarding the proportion of workers that will be covered by an EJRA as a proportion of those that are covered by a fixed retirement age today. These assumptions are for illustrative purposes only and given that predicting the future in this way is highly speculative the range of estimates is large.

3. Assumptions on workers that will be covered by an employer-justified retirement age that is below the state default retirement age

Option	As a percentage of those that are covered by a fixed retirement age today
Option a	0
Options b and c	25-50 at age 65; 0 at age 60
Option d	25-50 at age 60

Productivity of workers

33. The evidence on the productivity of older workers shows that they are no less productive than younger workers, except in a limited range of jobs. This is because

⁶³ See Meadows, P *ibid.*

⁶⁴ Those aged up to 49.

⁶⁵ See Dixon, S “Implications of Population Ageing for the Labour Market” Labour Market Trends – February 2003 pp 67 to 76.

⁶⁶ Cases which go to the Employment Appeal Tribunal or to a higher court will set a precedent for cases at Employment Tribunals.

their better experience, inter-personal skills and motivation offset their loss of speed, strength and memory. However, little is known about the productivity of workers over 70, as so few of them work.⁶⁷

34. The assumptions about the numbers affected by right to request continuing to work after the EJRA/DRA are set out in Annex A.

Benefits to firms

35. If some workers stay on at work longer than they would otherwise have done, this will lead to lower turnover, which will require a lower recruitment effort, (this will be especially true in those cases where the workers that stay on are those with special skills). For each worker this recruitment effort will be deferred until they eventually decide to retire. In each year there will be those who will be staying on from previous years, plus a new cohort who will be benefiting from the legislation; thus there will be savings on recruitment in the second year and subsequent years as well. Assuming that average cost of recruitment is about £4,200 per vacancy⁶⁸, illustrative calculations based on the same assumptions are outlined in Table 4.

4. Benefits to firms of lower staff turnover

	Year 1	Year 10	NPV over ten years*
Option a (no DRA/EJRA)	£14-36m	£13-32m	£110-280m
Option b (EJRA/ no DRA)	£10-31m	£8.4-27m	£75-240m
Option c (EJRA/no DRA/R2R)	£10-33m	£9-29m	£80-250m
Option d (DRA 65/EJRA/R2R)	£4.4-21m	£3.5-18m	£31-160m

* The net present value of benefits from year one to year ten inclusive, discounted at 3.5 per cent

36. There will be a benefit for employers in training those older workers who stay on (through better performance of workers, not compensated for in terms of increased wages), however we do not attempt to quantify this.

Benefits to individuals

37. To varying degrees, under all options, some of the older workers who want to continue working beyond their present normal retirement age will be able to do so. They will benefit from more earnings and the opportunity to save more for when they do decide to retire. There are also likely to be non-financial benefits that arise from workers being given a greater choice in their retirement age.

38. As those older workers stay on, other things being equal, younger workers will not be taken on to replace them. At the level of the firm therefore, for some firms, there will be a transfer of earnings from those workers to older workers, with possibly no great net effect. This is not the same thing as the macroeconomic effects which we expect to be positive and which we discuss later.

⁶⁷ See Meadows, P *ibid.*

⁶⁸ Source: CIPD surveys.

39. The gain to older workers will be their extra earnings, after tax and net of benefits,⁶⁹ as a result of being able to work longer. Illustrative estimates of these benefits for each option are shown in Table 5.

5. Benefits to individuals through higher earnings from staying in work*			
	Year 1	Year 10	NPV over ten years**
Option a (no DRA/EJRA)	£44-120m	£230-610m	£1,300-3,500m
Option b (EJRA/ no DRA)	£29-100m	£140-490m	£830-2,900m
Option c (EJRA/no DRA/R2R)	£31-110m	£150-540m	£900-3,200m
Option d (DRA 65/EJRA/R2R)	£12-67m	£51-300m	£320-1,900m

*net of tax and lost benefits * **The net present value of benefits from year one to year ten inclusive, discounted at 3.5 per cent

40. There is also a possibility that those who continue to work will be eligible for promotion, but given the limited number of years left in the workforce, we assume that the impact of this will be minimal.

41. Some of those staying on may also be eligible for training. This will lead to increases in productivity that could be reflected in higher wages.

Implementation costs to firms

42. The new regulations on retirement ages will need to be read and understood by employers. They then need to decide what to do as a result of the legislation. Under **options b, c and d** they may decide to have an EJRA and to justify this objectively if required. This is a complex and new area for employers and so this may take longer than most regulations. All our estimates are on the basis that employers will be reading the guidance on the whole of the age discrimination legislation at the same time and so the figures below represent marginal times and are in addition to those estimated for the other components.

43. Understanding the legislation

44. We assume that for small firms only one person in the firm will read the guidance, if at all⁷⁰, and that they will be less likely to do so if the firm does not have older workers. There is also a preference for using advice over the phone and face to face rather than through printed information or websites. It is therefore unlikely that all small firms will decide to become familiar with the legislation at one time, as smaller employers tend to read the legislation as and when they need to. Further advice may be sought from providers such as Acas.

45. We assume that all medium and large firms seek to understand the legislation either once it is laid in Parliament or shortly after it is brought into force in 2006. In larger firms those responsible for human resources may also be required to report the changes in legislation to senior staff and to produce their own guidance.

⁶⁹ Some who are now able to continue working might have been claiming benefits, which they would lose. Evidence from the Family Resources Survey suggests that this could be around 10-20 per cent of the group affected. We assume that they lose on average £90 per week, which is the average IB/SDA/JSA/Income Related Benefits to the family for 60-65 year olds not in work and receiving these benefits.

⁷⁰ Evidence from Blackburn, R and Hart, M (2002) "Small Firms' Awareness and Knowledge of Individual Employment Rights" DTI, Employment Relations Research Series No 14 showed that most companies seek to understand employment legislation on a needs basis.

46. As option a does not allow employers to justify their EJRA, the costs of reading and understanding the legislation are likely to be lower than, say, **option b**. **Options c and d** are likely to be more expensive, since these options contain an extra dimension to understand: the right for employees to request (R2R) continuing to work past the EJRA or DRA.

47. Tables 6, 7 and 8 below show that the total costs to firms of understanding the guidance will be about £31 million for **option a**, £53 million for **options b** and £61 million for **options c and d**. It should be stressed that these are average estimates and that the costs are likely to vary considerably from firm to firm.

6. Costs to employers of understanding the legislation under option a (no DRA/EJRA)

	Occupation of those reading and understanding guidance	Average hourly cost ⁷¹	Average time taken to understand legislation	Cost per firm	Number of firms	Total cost
Small firms	Manager/administrator	£25	1 hour ⁷²	£25	1,155,595	£28.9m
Medium and large firms	Personnel manager	£28	2 hours ⁷³	£56	35,885	£2.0m
All firms						£31m

Sources: ONS Annual Survey of Hours and Earnings 2004 and Small Business Service statistics for 2003. A small firm is defined as having 1 to 49 employees.

7. Costs to employers of understanding the legislation under options b (DRA/no EJRA)

	Occupation of those reading and understanding guidance	Average hourly cost ⁷⁴	Average time taken to understand legislation	Cost per firm	Number of firms	Total cost
Small firms	Manager/administrator	£25	1.75 hours ⁷⁵	£43.8	1,155,595	£50.6m
Medium and large firms	Personnel manager	£28	2.5 hours ⁷⁶	£70	35,885	£2.5m
All firms						£53m

Sources: ONS Annual Survey of Hours and Earnings 2004 and Small Business Service statistics for 2003. A small firm is defined as having 1 to 49 employees

⁷¹ This is taken as the average hourly wages (from the Annual Survey of Hours and Earnings) plus 30 per cent, which is the estimate of non-wage labour costs.

⁷² The assumption is that it takes half an hour to read the guidance and half an hour to follow-up with questions to Acas.

⁷³ This assumes that in medium and large firms employers spend three quarters of an hour reading the guidance, half an hour seeking clarification and three quarters of an hour disseminating and explaining guidance to others.

⁷⁴ This is taken as the average hourly wage (from the New Earnings Survey) plus 30 per cent, which is the estimate of non-wage labour costs.

⁷⁵ The assumption is that it takes three quarters of an hour to read the guidance and an hour to follow-up with questions to Acas.

⁷⁶ This assumes that in medium and large firms employers spend one hour reading the guidance, half an hour seeking clarification and one hour disseminating and explaining guidance to others.

8. Costs to employers of understanding the legislation under options c and d

	Occupation of those reading and understanding guidance	Average hourly cost ⁷⁷	Average time taken to understand legislation	Cost per firm	Number of firms	Total cost
Small firms	Manager/administrator	£25	2 hours ⁷⁸	£50	1,155,595	£58m
Medium and large firms	Personnel manager	£28	3 hours ⁷⁹	£84	35,885	£3.0m
All firms						£61m

Sources: ONS Annual Survey of Hours and Earnings 2004 and Small Business Service statistics for 2003. A small firm is defined as having 1 to 49 employees

Deciding what to do

48. For all options there will be a decision to be made by employers about any changes that need to be made to present performance and pay systems (if any) and for **options b, c and d** about whether to adopt an EJRA. The cost of deciding what retirement policy to adopt will involve looking at the company's current retirement policy and deciding what changes, if any, to make in the light of the new legislation.

49. We assume that for small firms a decision would have been reached while the manager/owner was reading and understanding the legislation. But for medium and larger firms this is likely to involve more discussions, at a board meeting perhaps, and advice from lawyers (either inside or outside the company). We assume that decisions on pay and performance systems would take a similar amount of time, if indeed discussion were needed. We argue that pay systems are unlikely to be reviewed under **option d** as this option involves preserving a default endpoint to employment. We also argue that under **option d** there is unlikely to be much discussion about performance systems.

⁷⁷ This is taken as the average hourly wage (from the New Earnings Survey) plus 30 per cent, which is the estimate of non-wage labour costs.

⁷⁸ The assumption is that it takes an hour to read the guidance and an hour to follow-up with questions to Acas.

⁷⁹ This assumes that in medium and large firms employers spend one hour reading the guidance, one hour seeking clarification and one hour disseminating and explaining guidance to others.

9. Total costs of making decisions for all options for medium and large firms

	Option a	Options b and c	Option d
Cost of discussion at board meeting ⁸⁰ (length of meeting)	£1,050 (2.5 hrs)	£1,260 (3 hrs)	£210 (0.5 hours)
Cost of legal advice ⁸¹		£33	£33
Total cost per business	£1,050	£1,293	£243
Total cost for all medium and large firms ⁸²	£38m	£46m	£8.7m

50. Table 10 gives an estimate of the average costs of all options for medium and large firms. Again there may be considerable variation in costs on a firm-by-firm basis. See Annex A for further details of assumptions of the time taken under each option. The costs of deciding what to do are assumed to be the same between **options b and c**. **Options c and d** do involve an extra factor in the decision (whether the R2R makes an EJRA more risky), but we argue it should not make the decision significantly more costly.

10. Total implementation costs for all options

	Option			
	a	b	c	d
Reading and understanding the guidance	£31m	£53m	£61m	£61m
Deciding what to do	£38m	£46m	£46m	£8.7m
Total implementation	£69m	£99m	£107m	£70m

51. Concerns were raised during the *Coming of Age* consultation that the implementation costs for smaller employers had been underestimated. However, whereas larger employers are assumed to seek to understand the legislation at once, smaller businesses tend to read the legislation on a “need to know” basis. The estimated cost of implementation presented here is an average cost across all smaller businesses. Furthermore, DTI and Acas will make detailed guidance on the legislation available for employers. It is envisaged that this will significantly reduce the need to seek specialist legal advice.

Policy costs for employers

52. The policy costs to employers will depend on their reaction to the legislation. There may be the cost of strengthening their performance systems. Even then they may still be more at risk of being taken to an Employment Tribunal should they need to dismiss or downgrade older workers due to poor performance. For employers that adopt EJRA this risk will be greater, as they also risk being challenged to justify it.

53. For employers who improve their performance and appraisal systems, there is likely to be an offsetting benefit in terms of a likely improvement in the performance

⁸⁰ Assumes that 6 executive board members present, all at hourly rate of pay of directors and chief executives of major organisations at a cost of about £70 per hour each. A half-hour discussion would cost £210 and a one hour discussion would cost £420.

⁸¹ The hourly pay of an in-house solicitor is £25.34 (3 digit SOC90 code 242, source ASHE 2002), so the hourly cost is about £33. We assume that legal advice is not required for **option a**.

⁸² This is reached by multiplying the cost per business by the number of medium and large firms (30,990).

of the whole of the workforce and the company. How much this offsets the cost of implementation will vary from employer to employer. However, under **options b, c and d** it is likely that for certain firms the net costs will reach a certain limit, where it will pay for the employer to adopt an EJRA. Logically this net cost will be equivalent to the cost of going to tribunal plus an amount to compensate for the uncertainty in the outcome. For **option a** employers would not be able to adopt an EJRA, but there is still likely to be an upper limit to net costs, as once they reach a certain limit they may prefer to risk being taken to an Employment Tribunal for unfair dismissal.

54. An illustration of possible extra costs of running a more thorough appraisal/competence system suggests that five to ten minutes extra⁸³ assessing everyone employed where appraisal systems are already in place would cost in the order of £18 to £36 million each year.⁸⁴ These could be partially or totally offset by gains in productivity, particularly if they take place in conjunction with other management best practice changes. We do not attempt to quantify this.

55. Some firms without appraisal systems may put them in place as a result of the legislation. As we do not have any evidence on what proportion of firms might do this just because age legislation comes into force, we do not attempt to quantify this cost.

56. These types of costs are most likely to be felt under **option a** and least likely under **options d**, since **option a** involves the biggest change to the status quo as regards retirement ages, so we argue it will require the biggest changes to appraisal systems.

57. We assume that the net cost to employers of employing more older workers, rather than younger workers, is likely to be neutral.⁸⁵

58. At the firm level and typically for smaller firms there are a limited number of senior jobs. If any of these are taken up by a worker staying on beyond the current normal retirement age, some firms may find it hard to retain and encourage younger workers who would be looking to replace them. At the level of the economy, job blocking is less likely to be a problem as there will also be a decrease in the proportion of 16 to 49 year olds who will be looking to take on these senior posts.

59. At the level of the firm, this is more likely to be a cost under **options a, b and c** rather than under **option d** where there is a default retirement age of 65. We do not attempt to quantify this.

60. Pay systems may include pay enhancements related to years of service, which are meant to reward workers for loyalty and for the gradual accumulation of firm-specific skills. They are usually predicated on an endpoint. Under **options a and b**, where the employer does not introduce an EJRA, the end point might be hard to

⁸³ This is at the lower end of estimated costs that we have been given by consultees, as it does not include any compensating efficiency gains.

⁸⁴ SBS statistics suggest that just over 17 million people work in medium or large firms in Great Britain. Assuming average hourly earnings of £12.19 from the Annual Survey of Hours and Earnings 2004, a factor of 1.3 to take into account non-wage costs and 79 per cent of firms have appraisal systems in place (WERS 98), this suggests the following calculation: $17,100,000 \times 79\% \times 1.3 \times £12.19 \times [1/12 \text{ to } 1/6] = £18 \text{ million to } £36 \text{ million}$ to two significant figures.

⁸⁵ Hourly earnings for older workers over 60 are lower than workers aged between 30 and 59 across the main occupational groups. This could be because of a number of reasons, for instance lower skills or a lower presence in the types of jobs that pay more (like new economy jobs or high paying jobs in the financial sector), or discrimination. However, if we make the assumption that workers are paid their marginal product (what they are worth), then there should be no net effect as employers would have to recruit marginally fewer younger workers.

estimate as it may vary from worker to worker. This may require some adjustment to pay systems. We are not sure to what extent this will be relevant to employers and so we do not attempt to quantify the net costs, although we have quantified the time taken to make a decision (see above).

61. There will also be costs to employers from defending Employment Tribunal cases. The average cost to an employer of defending an Employment Tribunal (ET) discrimination case is around £4,750.⁸⁶ Age cases are likely to be significantly more complex (e.g., considering justifying objective criteria for age discrimination) than typical ET applications, or even existing discrimination cases. If there are 1,600 cases related to retirement (see paragraphs 69 to 71 below), and employers win (and are, therefore, compliant with the legislation - the costs of non-compliance are not included) in 75 per cent of cases⁸⁷, then costs to employers for general retirement-related ET cases would come to around £5.7 million per year. The cases related to right to request are costed separately below.

Costs to employers of the right to request working past the EJRA or DRA

62. Under **options d and c** employers would incur costs when they receive requests from employees to continue working beyond the EJRA or DRA. The numbers of requests received are worked out according to the assumptions set out in Annex A. The employer would be under an obligation to take such requests seriously, following basic minimum procedural standards. Where requests are not accepted, there is provision for an appeal stage and, ultimately, recourse to an external dispute resolution mechanism, which could be an ET.

63. The employer would be obliged to hold a meeting to discuss the request with the employee, at which s/he will have the right to be accompanied (not costed because of a lack of evidence on the use of the right to be accompanied). It is assumed that each meeting requires half a day of management time and half a day of employee time. 'Deadweight' requests - those that would have happened anyway, probably at lower cost - are assumed to amount to five per cent of all requests and to cost an arbitrary £50 more than they would have done otherwise.⁸⁸ An employee would also have a right to an internal appeal if their request was unsuccessful. It is assumed that people do not have, or at least do not use, such an opportunity at the moment, so there is no 'deadweight' effect at the appeal stage. The appeal is assumed to require one day's management time and one day's employee time.

64. It is assumed, (for derivation of this assumption see Annex A) that 35-70 per cent of requests are successful either at the first meeting or on appeal. It is further assumed that 50 per cent of those employees who are unsuccessful in the first meeting decide to exercise their right to an internal appeal, that 80 per cent of these are also

⁸⁶ Estimate based on the Survey of Employment Tribunal Applications 2003.

⁸⁷ This is the proportion of Employment Tribunal claims that were 'successful' for employers in 2003/04. Acas-conciliated settlements and 'disposed of otherwise' are excluded. We take success for the employer as the claim being withdrawn, or dismissed at a hearing, and failure as the claimant winning at the tribunal hearing. Source: Employment Tribunal Service annual report and accounts 2003/04, and DTI calculations.

⁸⁸ These assumptions match those used in the Regulatory Impact Assessment of the duty of employers to seriously consider requests for flexible working from the parents of young and/or disabled children, 2002, available at: <http://www.dti.gov.uk/er/fworkingRIA.pdf>.

unsuccessful in their appeal, and finally that of those losing an appeal, 12 to 16 per cent⁸⁹ decide to take the matter to an ET.

65. According to the Annual Survey of Hours and Earnings Survey 2004 the hourly wage of a manager/senior official time is £19.24, that of a personnel manager is £21.58 and that of the average employee is £12.19. The first of these is used for management costs in small firms, and the second for management costs in medium and large firms. These figures were increased by 30 per cent to take account of non-wage costs and used to estimate the aggregate costs of first meeting and appeal meetings in the table below. These assumptions imply a first meeting cost of around £170, and an appeal meeting cost of around £340.

66. The costs of an ET application is taken at £4,900.⁹⁰ Table 11 shows the costs to firms under options c and d.

11. First-year costs to employers of the right to request working after the EJRA or DRA		
	Option c	Options d
First meetings	£58,000-71,000	£150,000-340,000
Appeal meetings	£120,000-370,000	£310,000-1,800,000
Employment Tribunals	£17,000-90,000	£46,000-430,000
Total	£190,000-530,000	£510,000-2,500,000

67. Given that cost or other disruption to the business could be a valid ground for refusing a request (as long as the reason is not age-discriminatory), it is assumed that any costs incurred by businesses that grant these requests will be negligible.

Costs for workers

68. Some workers' performance (at least as perceived by their employer) may start to diminish as they get older, leaving them at risk of an undignified exit from the labour market, under all options. This risk is greater under **option a** where there is neither an allowance for an employer-specific retirement age nor for a default retirement age. Conversely the risk is lower under **option d**. We do not attempt to cost this, as we are unsure of how many workers this is going to impact upon and what the cost to each worker would be. On average, across all older workers, the evidence⁹¹ suggests that performance does not decline with increasing age, at least up to age 70, but this does not prohibit the possibility that the performance of some workers declines.

Impact on the number of Employment Tribunals

69. The number of ET applications is likely to rise as a result of the legislation. This is in line with findings in the United States. However, it is hard to say to what extent it will be different under different policy options. Under **option a**, employers may be taken to an ET if they dismiss older workers because of their age or if they dismiss them because of poor performance - poor performance may still be a valid

⁸⁹ Based on the Legal Services Research Centre's Periodic Survey 2001 and statistics from the Employment Tribunal Service, it is estimated that 12 to 16 per cent of all employment-related disputes lead to an Employment Tribunal application. See footnote 4 in the Regulatory Impact Assessment on Statutory Dispute Resolution procedures, 2004, available at: http://www.dti.gov.uk/er/emar/dispute_resolution_ria.pdf

⁹⁰ The estimated average cost of a discrimination application to employers based on the Survey of Employment Tribunal Applications 2003 is £4,750.

⁹¹ See Meadows, P, *ibid*.

12. Mid-range estimates of labour supply increase under different options			
	Year 1	Year 5	Year 10
Option a (no DRA/EJRA)	6,000	22,000	30,000
Option b (EJRA/ no DRA)	4,800	18,000	23,000
Option c (EJRA/no DRA/R2R)	5,100	19,000	25,000
Option d (DRA 65/EJRA/R2R)	3,000	11,000	14,000

reason for dismissal, but an employer would have to show they were not being age-discriminatory in applying performance criteria. Under **options b, c and d**, an employer could dismiss/retire a worker at the EJRA or DRA without fear of ET. Under **option d** there could be challenges to employers who adopt EJRA's below the state default of 65.

70. The impact of the right to request on ET applications has been quantified (see Table 11). As a result of the right to request working beyond the EJRA or DRA, in the first year we expect around 5 to 19 Employment Tribunal applications under **option c**, and 13 to 88 under **option d**. 88 applications would represent just 0.07 per cent of all ET applications.

71. Basing estimates on the number of Employment Tribunal applications in respect of sex, race, and disability discrimination we estimate that there will be an average of 8,000 ET applications per year resulting from the age strand of the Directive⁹², of which 20 per cent might relate to retirement issues. This takes into account the fact that we expect a fall in applications following the implementation of the Employment Act 2002. It is hard to say how many tribunal cases there would be under different options.

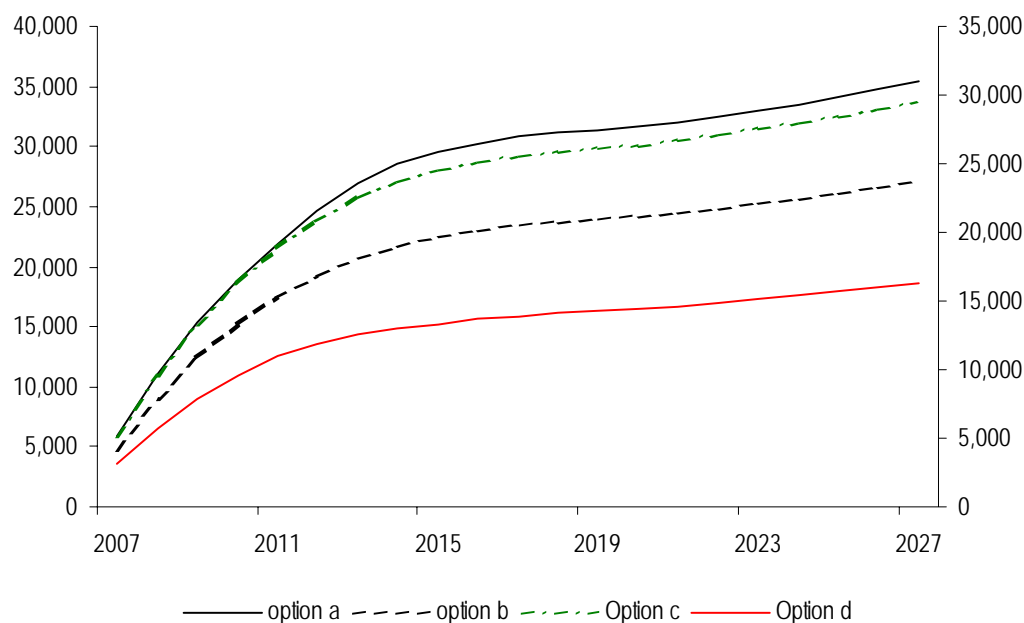
Macroeconomic effects

72. The legislation will have an impact on the labour supply that will affect the macroeconomy. The following indicates what the contribution of changes to retirement age legislation might be. We made some estimates of possible impacts, based on certain assumptions laid out in Tables 1 and 2. These are for illustrative purposes only.

73. Table 12 and the chart below illustrate the order of magnitude of these expected increases. Extrapolating these trends, the increases in labour supply do not flatten right out and fall, but the rate of change of the increases falls to a steady, small rate. As a percentage of the total labour force, an increase of 30,000 in year 10, as in **option a**, would equate to 0.1 per cent of the UK workforce; 14,000 as in **option d**, would equate to just 0.05 per cent. Even of the UK workforce over 50, these increases represent just 0.4 per cent and 0.2 per cent, respectively. The analysis calculates the effects on men and women separately, but the chart below gives the sum of estimated male and female labour supply increases.

⁹² For derivation, see Annex B of the Regulatory Impact Assessment on Age Discrimination Legislation, 2003, available at: http://www.dti.gov.uk/er/equality/agediscrim_RIA.pdf.

2. Labour market affect of different options (mid-range estimates)



Source: illustrative calculations.

74. We have made estimates of the impact on GDP based on these changes to the workforce by using some simple assumptions:

- The economy adjusts smoothly and wages at all ages are the same as they are today.
- The contribution of increased wages of those 60 and over is their increased labour supply multiplied by their average wages (£9,008 per year for women and £18,648 for men).
- The percentage rise in GDP is the same as the percentage rise in aggregate wages.
- The estimated increase in GDP is shown in Table 13 for each option.

13. Estimates of increases in GDP resulting from increase in labour supply

	Year 1	Year 10	NPV over ten years
Option a (no DRA/EJRA)	£100-270m	£530-1,400m	£3,100-8,000m
Option b (EJRA/ no DRA)	£67-220m	£320-1,100m	£1,900-6,500m
Option c (EJRA/no DRA/R2R)	£71-240m	£350-1,200m	£2,100-7,100m
Option d (DRA 65/EJRA/R2R)	£27-150m	£120-680m	£740-4,200m

75. Contributing to these increases in GDP are an increase in profits as well as an increase in incomes and taxes.⁹³ Estimates of increases in profits are shown in Table 14. These count as benefits to employers (before tax) but unlike other factors which we have included, it is possible they may not represent a change in profit margins, nor a change in total factor productivity.⁹⁴ However, if an increase in labour resulted in a better use of capital or resulted in increasing returns to scale⁹⁵, employers would benefit from some proportion of these changes through a change in profit margins and an increase in total factor productivity.

14. Estimates of increases in profits resulting from increase in labour supply

	Year 1	Year 10	NPV over ten years
Option a (no DRA/EJRA)	£22-58m	£120-300m	£680-1,700m
Option b (EJRA/ no DRA)	£15-49m	£70-240m	£420-1,400m
Option c (EJRA/no DRA/R2R)	£16-53m	£76-260m	£450-1,600m
Option d (DRA 65/EJRA/R2R)	£6-33m	£26-150m	£160-910m

76. With an increase in the size of the employment pool, employers would also gain from better job matching and hence higher productivity, particularly if the pool of skilled workers increases. Even though most workers who work beyond retirement age do so in the jobs that they had before they reached retirement age, all options would increase the size of the labour pool that employers can recruit from. There will be more younger workers to choose from when recruiting. We do not attempt to put a value on this impact.

77. Working for longer means running down retirement savings later, which would have a positive impact on the overall stock of savings. However, knowing that there is no longer a normal retirement age, or one that is higher than previously, may act as a disincentive to savings, as workers would have more flexibility. The net impact is therefore uncertain.⁹⁶

Exchequer effects

78. Increased output will improve public finances as those older workers who stay at work will either pay more taxes or receive fewer benefits. We assume that tax revenues increase by the same proportion as GDP. Estimates of the increase in tax revenues are shown in Table 15.

⁹³ These are pre-tax profits, which are defined as revenue from sales minus non-tax costs. Non-tax costs include wage costs, non-wage labour costs including non-pay benefits such as pensions, capital costs and intermediate goods and services' costs. We have not made any estimates of the impact on profits after tax.

⁹⁴ This assumes that for each unit of increased labour there is a corresponding increase in capital and that there are constant returns to scale.

⁹⁵ Increasing returns to scale means that larger scale (of a firm, industry or whole economy) implies greater efficiency. Under increasing returns to scale, if all inputs are increased by 10 per cent, then output increases by more than 10 per cent.

⁹⁶ Pam Meadows concludes that the impact on savings of lifting retirement ages is likely to be positive, although she outlines the uncertainties in arriving at such a conclusion.

15. Estimates of increases in tax revenues resulting from increase in labour supply

	Year 1	Year 10	NPV over ten years
Option a (no DRA/EJRA)	£35-93m	£190-490m	£1,100-2,800m
Option b (EJRA/ no DRA)	£22-78m	£110-390m	£670-2,300m
Option c (EJRA/no DRA/R2R)	£24-84m	£120-430m	£730-2,500m
Option d (DRA 65/EJRA/R2R)	£8-52m	£40-240m	£250-1,500m

79. There will also be costs to the taxpayer from an increased number of ET applications. It is estimated that it costs on average £910 to process each application.⁹⁷ If there are 1,600 applications a year, plus varying numbers of applications associated with the right to request depending on the option chosen (see *Impact on the number of Employment Tribunals* above), then the cost of applications to the Exchequer would come to around £1.5 million in the first year under all options. The additional applications arising from the right to request are likely to be very few.

Conclusions, risks and sensitivity analysis

80. So far we have concluded that the introduction of the legislation under any of the options is likely to have a positive impact and in some instances we have not been able to quantify the difference between the options. We have, however, identified that under **option d**, the net impact on employers in terms of the impact on productivity is most favourable, whilst under **options b and c** the impact is of a similar order of magnitude. For **option a**, the net impact is more uncertain than for **option d**.

81. It is also clear that benefits to individuals, employees, employers (including non-productivity effects), the Exchequer and GDP tend to dwarf costs and benefits to employers due to productivity effects, with **option a** showing higher benefits than the other options.

82. However there is much that we do not know about the present expectations of workers and the future behaviour of employers and workers and the associated costs and benefits. The following outlines the main risks to our conclusions.

83. The numbers that want to work longer may increase. This will increase the macroeconomic impact and the benefit to older workers but may put additional pressure on some firms who will find it difficult and expensive to accommodate this.

84. A retirement age of 65 could mean higher employment rates up to 64, but it may also result in lower employment rates of those 65 and over (as happened in the US⁹⁸).

85. Under all options there would have to be changes to unfair dismissal legislation, to give employees and some non-employee workers the right to claim for unfair dismissal at age 65 and above. Retirement at the DRA or an EJRA will still be a fair reason for dismissal. Employers may not want to encourage the continued participation of a few older workers, since their legal risks will be higher if they do not have a uniform policy. This could lead to the unintended consequence of a reduction in how many workers are allowed to continue working. This risk would be reduced by a right to request working beyond the EJRA or DRA.

⁹⁷ Estimate based on the Employment Tribunal Service Annual Report 2003/04 and figures provided by Acas.

⁹⁸ See *Age Discrimination in the USA*, Adams, S.J, 2001.

86. Little is known about the performance of those over 70. If this declines quite quickly, it could put extra burdens on some employers, particularly under **option a**. At present, however, relatively few people work past the age of 70.

87. Little evidence is available from other countries of likely overall impact. To our knowledge, no other major country has outlawed both direct and indirect discrimination on the basis of age.

88. The reaction of employers is unknown, but we have assumed that they will be able to make an informed assessment of which course of action is best for them in the light of their new obligations under age discrimination legislation. This may not be the case, as a normal retirement age of between 60 and 65 is well entrenched in Great Britain, and employers may be overwhelmed by the scale of the changes they need to consider and implement in the face of the new legislation. They are, therefore, at risk of making incorrect and costly decisions. This will be more so for **options b and c**.

89. It may take some time for the behaviour of employees and employers to change, thus the benefits arising from the changes in the labour supply and the reduction in turnover costs may take some time to be felt.

90. The legislation may have the unintended effect of discouraging the employment of older workers if employers are not sure how long they will have to employ them and what they will have to do to dismiss them if they turn out to be poor performers. This is more of a risk under **options a, b and c**.

91. There is a potential risk that an employer who grants a request by an employee to work beyond the EJRA would undermine his/her defence for the EJRA if challenged to justify it at a subsequent Employment Tribunal. This risk would seem fairly low if only a few requests are granted, which implies the risk is potentially larger for larger firms. If a successful request would undermine the EJRA, then employers will be much less likely to grant requests. Employers would not face the same disincentive to granting requests to work beyond the national DRA. Another effect of this risk is that employers might be less likely to adopt EJRA when there is a right to request.

92. A lower success rate for requests to work beyond EJRA would mean fewer people staying in the labour market, and smaller net benefits to the economy. Fewer employers adopting EJRA would mean more people staying in the labour market and larger net benefits to the economy. There is clearly a trade-off here: one effect would offset the other, although to what extent we cannot be sure. In any case, we can still be confident that a right to request would have significant net benefits, because of the likely effect on the number of employers adopting EJRA and the fact that the right to request working past the DRA would be unaffected by this risk.

93. There are probably more risks to our estimate of costs and benefits to employers associated with **options a, b and c** than with **option d**. Given the degree of uncertainty a sensitivity analysis has been carried out below.

94. Our analysis rests on a number of key assumptions, specifically our estimates of the numbers who are retiring against their will and the numbers of employers who adopt an EJRA under different options, the numbers of people who will make a request under different options and how many are successful, and also our other assumptions about behaviour as outlined above.

95. For **option d** to be equivalent to **options a, b or c** we would have to assume that under **option d** virtually no employees retire against their will at 65 or over. This does not seem to be consistent with the behaviour of employers or the desires of employees today. Alternatively, we would have to assume that under **options a, b**

and c employers are sufficiently concerned about not being able to dismiss older workers that this substantially affects their willingness to employ older workers. This may be a concern initially, but it would act against the other parts of the legislation (on recruitment for instance) and may not be sustainable in the longer term because of changes in the age profile of the workforce.

96. It is possible that it may take some time for the behaviour of employees and employers to change. This could result in **option d** looking the most favourable in the short-term, even though it is not in the longer term.

97. For **option b** to be equivalent to **option a**, one would have to assume that virtually no employers decide to justify EJRA's and that there are minimal implementation costs associated with this decision.⁹⁹ Again we think this is not consistent with employers' behaviour today. Alternatively, one would have again to assume that under **option b** employers recruit fewer older workers.

98. For **option c** to be equivalent to **option b** there would have to be either a negligible number of requests to continue working, or a zero success rate for requests. The latter does not seem plausible, but the former may be. There has been significant take up of the right of parents of young and/or disabled children to request flexible working, which suggests people are willing to make such requests and the evidence suggests that people are being forced to retire against their will. Add to this the fact that when people are approaching retirement they probably have less to lose, and it seems likely that there will be a significant number of requests.

99. Our sensitivity analysis suggests that in terms of benefits to the economy that arise because of changes to the labour supply, it is unlikely that **option d** is as favourable as the other options, although it may be in the short term. It is also very likely that in the long-term **option a** is the most favourable option.

Equity and fairness

100. Under all the options considered, some workers, who would be forced to retire against their will if the status quo continued, will be able to continue working. Whilst the legislative changes being considered would only impact directly on a relatively small number of people (those forced into retirement), the changes might also give other workers more choice in their retirement options by encouraging employers to re-examine their retirement policies.

101. There is a risk under those options that allow EJRA's that some individuals who would have been allowed to continue working past their normal retirement age will not be allowed to because the employer would be at risk of undermining her/his whole EJRA policy.

102. Those workers whose performance declines, or is perceived by their employers to decline, will be at risk of an undignified exit from the workforce. That is, instead of retiring at their normal retirement age with a 'pat on the back', in order to get rid of them their employer will be forced to tell them their performance is no longer up to requirements. The extent of this effect will be greatest under **option a**, and least under **option d**.

103. More men will benefit from changes to retirement age legislation than women, because a higher proportion of men are still working at age 60 and over than of women.

⁹⁹ We have assumed that under **option b** that medium and large employers spend some time in reaching a decision on this issue.

Race equality impact assessment

104. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firms impact test

105. Small firms make up around 97 per cent of all firms with employees, and they will have to make sure they are compliant with the legislation. This means that small firms will bear a disproportionate (relative to employment levels) share of the implementation costs of the legislation. The policy costs of the legislation will be more related to levels of employment, because they relate to issues surrounding the retirement of workers, so the more workers a company has, the more costs it will face. Thus, small firms will face only around a third of the total policy costs of the legislation.

106. There will also be benefits to small firms from the legislation. These benefits include savings on recruitment, improvements in productivity and increased aggregate profits.

107. Annex B details the results of consultation and focus groups with small firms.

Competition

108. All the options considered for retirement ages are expected to lead to an increase in participation rates for older workers. This will enhance competition in the labour market as age is used to a lesser extent as a criterion in employer retirement decisions. Older workers who wish to stay in the labour market, to a differing extent under different options, will be more likely to be able to do so and will not be forced out due to considerations unrelated to their ability to do the job.

109. The competition filter was applied. The results appear in Annex F. Almost all sectors of the economy will be affected, since virtually all sectors of the economy employ workers approaching retirement age. Those firms who employ more workers approaching retirement age will be more affected than those who employ fewer workers approaching retirement age. Notwithstanding, we do not feel that the legislation is likely to affect the number or size of firms. None of the changes in legislation considered here should impose higher costs on new entrants relative to existing firms. Overall, we have identified no sectors where competition between firms may be adversely affected by these different legislative options.

Enforcement, sanctions and monitoring

110. Employers who are not compliant with the legislation may be taken to Employment Tribunal by their workers. The section *Impact on the number of Employment Tribunals* above details how many more applications to Employment Tribunals we expect under the different options. The costs to employers and the Exchequer of these applications are then considered in the *Policy costs for employers* and *Exchequer effects* sections.

111. Sanctions may be taken against employers who are not compliant with the legislation in the form of awards at Employment Tribunal. The management and employee time costs and legal costs of Employment Tribunals will be a further deterrent to non-compliance.

Post-implementation review

112. The DTI has already commissioned a baseline survey to assess the pre-legislative state of affairs regarding employers' awareness, perceptions and practices on age-related issues including retirement, alongside some case study research. The DTI intends to carry out a follow up survey to assess the impact of legislation and will consider commissioning further case study work to assess the impact of legislation on firms. DTI will also explore, with the ONS and DWP, the prospects for collating better statistical data on employee retirement intentions and behaviour.

113. The DTI will also monitor Employment Tribunal applications through application statistics and the Surveys of Employment Tribunal Applications.

114. There will be a formal review of the legislation after 5 years. Annex D gives a summary of the aims of the review and the information that it will use to come to a conclusion.

Summary and recommendation

115. The net benefits to the economy because of the legislation are the sum of the effects of the increase of the labour supply on GDP and the productivity effects on employers.

116. Table 16 summarises and disaggregates the quantified net costs and benefits to the economy into those for individuals, firms and the Exchequer. The table in Annex E gives a further breakdown of these costs and benefits, and also lists those costs and benefits which we have not been able to quantify.

Table 16: Summary of quantified net costs and benefits (£m)					
		Option			
		a	b	c	d
Employers (due to changes in total factor productivity)	Yr 1	Cost £75-79m	Cost £110m	Cost £120m	Cost £57-72m
	Average annual NPV**	Cost of £32m to benefit of £0.46m	Cost of £6.8-32m	Cost of £6.4-39m	Cost of £9.4m to benefit of £1.5m
Individuals	Yr 1	Benefit £44-120m	Benefit £29-100m	Benefit £31-110m	Benefit £12-67m
	Average annual NPV**	Benefit £130-350m	Benefit £83-290m	Benefit £90-320m	Benefit £32-190m
Exchequer	Yr 1	Benefit £35-93m	Benefit £22-78m	Benefit £24-84m	Benefit £8-52m
	Average annual NPV**	Benefit £110-280m	Benefit £67-230m	Benefit £73-250m	Benefit £25-150m
Economy (due to changes in the labour supply)	Yr 1	Benefit £100-270m	Benefit £67-220m	Benefit £71-240m	Benefit £27-150m
	Annual average NPV**	Benefit £310-800m	Benefit £190-650m	Benefit £210-710m	Benefit £74-420m
Total	Yr 1	Benefit £21-190m	Cost £48m to benefit of £110m	Cost £50m to benefit £120m	Cost £46m to benefit £91m
	Annual average NPV**	Benefit £280-790m	Benefit £150-640m	Benefit £170-700m	Benefit £63-420m

** Annual average NPV = the net present value of the costs and benefits from year 1 to year 10, discounted at the Treasury rate of 3.5 per cent and divided by ten.

117. The Government has concluded that legislation implementing the age strand of the European Employment Directive should set a default retirement age (DRA) of 65. Employers would be free to objectively justify setting their own retirement age (EJRA) below 65, and employees would have a right to request working over the DRA or their employers EJRA (if appropriate).

118. This approach aims to promote greater choice for older workers without an unnecessary burden on business – many of whom have traditionally relied on retirement ages as an important means of human resource planning – and the broader economic advantages of not imposing a DRA.

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

Gerry Sutcliffe

Parliamentary Under-Secretary of State

(Minister for Employment Relations and Consumer Affairs)

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Main assumptions

The following annex outlines the main assumptions that we have made while estimating the costs and benefits of the impact of age legislation on retirement ages.

Potential numbers affected

The assumptions on the number of workers affected by legislation on retirement ages are based on, and attempt to be consistent with, the following evidence:

- An assessment of the numbers of those employed if the legislation is not introduced. This has been derived by using the Government Actuary Department's population projections and employment rate projections from the Office of National Statistics.
- The findings in a recent research report¹⁰⁰ that 59 per cent of employees had a fixed retirement age at their place of work.

The conclusions from the same research that 'there is no evidence that employers' fixed retirement ages exert a widespread influence on decisions to retire before state pension age. However, there is evidence that employers' fixed retirement ages may prevent some people from continuing to work beyond state pension age'.

For those that faced a fixed retirement age, the distribution of normal retirement ages is shown in the table below:

1. Employers' fixed retirement ages (FRA)

Fixed retirement age (FRA)	Proportion of men in a workplace with a FRA at that age	Proportion of women in a workplace with a FRA at that age
55	2.0%	1.1%
60	11.3%	31.0%
61	-	-
62	1.3%	-
63	0.7%	0.5%
64	0.7%	-
65	49.9%	19.3%
65+	1.3%	0.5%

Source: Table 5.5, page 67 in Department for Work and Pensions Research Report 200, *Factors affecting the labour market participation of older workers*, Alan Humphrey et al, 2003.

Not all people reaching their employers' fixed retirement age retire at that age. According to the same research referred to above, 19 per cent of all those with a fixed retirement age retired at that retirement age. Moreover, not all people who retire at the same age as their fixed retirement age will be doing so against their will - perhaps 50 per cent do so. The table below estimates the proportions of those retiring at each age who are doing so against their will because of a fixed retirement age, using the evidence referred to from DWP Research Report 200 and assuming a 50-50 split on the voluntary-involuntary nature of the retirement.

¹⁰⁰ See Humphreys A., Costigan P., Pickering K., Stratford N. and Barnes M. (2003) *Factors affecting the labour market participation of older workers*, Department of Work and Pensions Research Report 200.

2. Proportions of people retiring forced to do so by a fixed retirement age, based on DWP research

Fixed retirement age (FRA)	Proportion of men retiring involuntarily due to a FRA	Proportion of women retiring involuntarily due to a FRA
55	0.2%	0.1%
60	1.1%	2.9%
61	0.0%	0.0%
62	0.1%	0.0%
63	0.1%	0.0%
64	0.1%	0.0%
65	5.0%	1.8%
65+	0.1%	0.0%

Source: Tables 5.5 and 5.6 on pages 67 and 68 in Department for Work and Pensions Research Report 200, *Factors affecting the labour market participation of older workers*, Alan Humphrey et al, 2003.

Other evidence

We also need to be aware of the somewhat contradictory evidence arising from research based on the 1994 Retirement Survey which found that involuntary retirement at normal retirement age is not common and is more likely to be found in those who are obliged to retire at 60 rather than at 65.¹⁰¹

The 1994 Retirement survey suggested that the majority of fixed retirement ages are at state pension age. It also suggested that for 10.3 per cent of male retirements before state pension age, the main reason was a fixed retirement age, but that this was the case for just 0.7 per cent of female early retirements. The latter fits with the later survey evidence above - that there are very few fixed retirement ages before 60 for women.

3. Assumptions of percentages of workers who retire only because they reach their employer's fixed retirement age

Age	Men	Women
60	1-3%	2-4%
61-64	0-0.5%	0-0.5%
65	3-7%	1.5-2.5%
66	2-5%	1-2%
67	1-3%	0.5-1.5%
68	0-1%	0-1%
69	0-0.5%	0-0.5%
70+	0-0.5%	0%

Source: DTI assumptions based on available evidence

The assumptions above were designed to be consistent with the above evidence, but are nevertheless highly uncertain.

Table 4 sets out our assumptions for the proportion of workers that will be covered by an EJRA as a proportion of those that are covered by a fixed retirement age today. These assumptions are for illustrative purposes and given that predicting the future in this way is highly speculative, the range of estimates is large.

¹⁰¹ DTI Employment Relation Research Series 18, *Retirement ages in the UK: a review of the literature*, Pamela Meadows, 2003.

4. Assumptions on workers that will be covered by a employer-justified retirement age that is below the state default age

Option	As a percentage of those that are covered by a fixed retirement age today
Option a	0
Options b and c	25-50 at age 65; 0 at age 60
Option d	25-50 at age 60

Tables 3 and 4 enable us to estimate the impact on the numbers of extra workers who will be able to work for different options. This gives us figures for the reduction in vacancies and the increase in GDP (including the impact on wages, profits and taxes).

Right to request beyond an EJRA or the DRA

All employees reaching their EJRA or the DRA would be able to make a request to continue working, but it is assumed that only those being forced to retire against their will (as estimated in Tables 3 and 4 above) are likely to make a request.

It may be that women may be more likely to request postponing retirement, because women in general, due to career breaks and so on, have not accumulated as much pension entitlement as men. However, without evidence on which sex is more likely to submit requests, both sexes are treated identically. A discussion of the evidence is in the footnote below.¹⁰² 40 per cent to 60 per cent of those being forced to retire because of EJRA's or a DRA are assumed to submit a request. A wide range has been taken to reflect the level of uncertainty.

Requests to postpone retirement when faced by an EJRA/DRA may well not have such a high success rate, since where there is an EJRA, the employer already has a policy about when people should retire in the form of the EJRA. We have therefore decided to take a broad range from 35 per cent to 70 per cent, reflecting the evidence¹⁰³ that the acceptance rate may be high and the intuition that it may be much lower.

¹⁰² In April 2003, a new right came in to force for parents with children under six or disabled children under eighteen to be able to request to switch to flexible working arrangements, a request which employers would have a statutory duty to consider seriously. Unfortunately, evidence on what the change in requests for flexible working has been as a result of this legislation is not very robust. The DTI Flexible Working Survey found that 24 per cent of employees with children under six had made a request in the six to ten months since the legislation came in to force, but we do not know how many in this group applied before April 2003.

The second Work Life Balance survey, carried out in February-March 2003, found that 12 per cent of male parents and 29 per cent of female parents had made a request for flexible working in the last two years. The equivalent figures from the Flexible Working Survey are 11 per cent and 27 per cent, but the time period is lower - just the six to ten months since April 2003. If we assume the requests are evenly distributed over the respective time periods, then since the legislation came into force, yearly requests have gone from 6 per cent to 16.5 per cent for men, and 14.5 per cent to 40.5 per cent for women, but that assumption is probably flawed, and this applied to all parents, only a subset of whom were actually affected by the statutory right.

¹⁰³ The second Work Life Balance employees survey found that 77 per cent of employees' requests for flexible working were successful, whilst the employers' survey found that 28 per cent of employers would automatically grant such a request, whilst for 52 per cent of employers it would be conditional on the case. If half of conditional cases were granted, then employers probably granted about 28 per cent plus 26 per cent = 64 per cent of requests. The flexible working survey, meanwhile, found that 77

5. Assumptions on employees making requests to continue working past their EJRA or the DRA

Option	Those still forced to retire as percentage of those forced under the status quo		
	60-64	65-69	70+
a	0%	0%	0%
b	0%	25-50%	25-50%
d without R2R	25-50%	100%	100%

Option	Request rate	Success rate	Those still forced to retire as percentage of those forced under the status quo		
			60-64	65-69	70+
c	40-60%	35-70%	0%	14.5-43%	14.5-43%
d with R2R	40-60%	35-70%	14.5-43%	58-86%	58-86%

Source: DTI estimates. Option h will be as for option g for the first five years, then as option e thereafter.

The estimates in the above table of the proportions of people still being forced to retire, fed through into estimated costs and benefits for the right to request continuing to work when the EJRA or DRA is reached.

The benefits also depend on the type of request received. The policy would include a right to request continuing work, but switching to flexible working arrangements. Of possible flexible working arrangements, part-time working and job share seem the most significant for workers over 60 (the only age range where significant numbers of workers are forced to retire against their will).

It is assumed that 6 per cent of requests are to switch to part-time employment and 1 per cent of requests are to switch to job share.¹⁰⁴

Implementation costs

We assume that:

- For small firms only one person in the firm will read the guidance, if at all¹⁰⁵ and that this takes one hour for **option a** and two-and-a-half hours for **options b, c and d**;
- In medium and large sized firms this will involve more time (two hours for **option a** and three hours for **options b, c and d**); and

per cent of employees' requests for flexible working were wholly granted and 9 per cent were partially granted.

¹⁰⁴ The DWP Evaluation of the Code of Practice on Age Diversity in Employment found that, on average, over the three waves of the Code of Practice, 67 per cent of over 50s currently working would only consider part-time employment after they retire. According to the Labour Force Survey Spring 2003, 61 per cent of 59 to 64 year old workers work part-time. The difference between these two statistics can be interpreted as some measure of the percentage of older workers who would like to switch from full-time to part-time employment - i.e., about 6 per cent. The Labour Force Survey Spring 2003 suggests that just 0.45 per cent of working 60-64 year olds have a job share arrangement (this 0.45 per cent cannot be relied upon due to a small sample size, but it is evidence that job share arrangements are rare in this age group). Demand for job share arrangements may be much higher than this. Hence we assume 1 per cent of requests may be for a job share.

¹⁰⁵ Evidence from R.Blackburn and M.Hart (2002) "Small Firms' Awareness and Knowledge of Individual Employment Rights" DTI, Employment Relations Research Series No 14 showed that most companies seek to understand employment legislation on a needs basis.

- The cost of making decisions on EJRA's, performance systems and pay systems involves the time of a board of directors (see Table 6), and, for EJRA's advice from a lawyer (one hour).

6. Length of board meeting for medium and large firms in hours				
	Option a	Option b	Option c	Option d
EJRAs	0.5	1	1	0.5
Appraisal systems	1	1	1	0
Pay systems	1	1	1	0
All topics	2.5	3	3	0.5

Policy costs

It is assumed that:

- Adjustment to existing appraisal systems will mean an additional 5 to 10 minutes of all employees' time per year. Note this is at the lower end of estimates that we have been given through informal consultations. It also does not include any positive productivity effects;
- The net savings for having to recruit fewer staff is £4,200 per vacancy. This estimate comes from the average of the last three Chartered Institute of Personnel and Development surveys; and
- Older workers' productivity does not decline with age.

Small Firms Impact Test

Table 1 below gives details of the costs and benefits of different options to small firms.

1. Summary of costs and benefits to small firms of different options over ten years				
	Option a	Option b	Option c	Option d
Productivity effect	£0 to -£86m	-£330m to -£120m	-£37m to -£120m	-£26m to -£55m
Effect on aggregate profits	+£180-470m	+£110-380m	+£120-420m	+£44-240m
Sum of productivity and profits	+£95m to +£470m	-£5m to +£350m	-£2.5m to +£380m	-£12 to £220m

Source: DTI estimates of costs and benefits in net present value terms over ten years. Numbers may not add due to rounding. All numbers are quoted to two significant figures.

A research study was commissioned by the Small Business Service into the impact of age discrimination with a focus on retirement ages. This consisted of three focus groups in Manchester run by MORI in March 2003.

Other more general focus groups on age discrimination were held in August and December 2002.

Although smaller firms are currently less likely to employ older workers¹⁰⁶, very small firms as a whole do have a very large proportion of workers over 65 and they may need to take more actions to comply with the legislation.

Future demographic changes will be an important driver here as research shows that SMEs have low awareness of potential changes in the next 10 years.¹⁰⁷ Indeed, generally the SBS research has shown that retirement may not be something that many small businesses think about or plan for. Many will not have had to deal with retirement before.

Smaller employers also saw problems with having older workers. Some thought that they would find it harder to master new technology and others thought that they might not have the stamina to do longer hours. Problems around getting 'new blood' into the company were also mentioned.

However, other small firms were more relaxed, saying that they either relied on merit and performance for their employment decision or that it is hard to predict how older workers would perform. Some could see the benefit of a later retirement age in terms of less costly pensions. There was, however, a general desire for the legislation to be such that they are in control of when workers in their firms retire.

So, although small employers are less likely to have older workers, the prevalence of less formal procedures and the probable existence of more discriminatory practices make those that do have older workers more vulnerable to being taken to an Employment Tribunal. Furthermore, we assume that eventually almost all small firms will be affected, either through the recruitment process, or because they will at some stage have older workers.

¹⁰⁶ 19 per cent of establishments with 10-24 workers have no workers over 50, compared to just 1 per cent of those with 500+ workers. The legislation will not just cover older workers.

¹⁰⁷ Promoting Age Diversity in Employment with Small and Medium Sized Employers see http://www.dwp.gov.uk/publications/dwp/2001/nsnr/annex_c.asp

Implementation costs

Small firms find it harder to come to terms with new regulations than medium and large companies. Many small employers (those with less than fifty employees) will have neither dedicated HR arms or formal systems in place.

There are about 1.19 million businesses in Great Britain, of which about 1.16 million are small employers and around 36,000 are medium to large employers. The total cost for small businesses of reading and understanding the guidance and making decisions is between about £25 and £50 per business or between £29 million and £58 million for all small businesses, depending on the option chosen. These costs are included in the above table of costs and benefits to small firms.

Government agencies and departments consulted

Better Regulation Task Force

Cabinet Office

Department for Constitutional Affairs (DCA)

Department for Environment, Food and Rural Affairs (DEFRA)

Department for Work and Pensions (DWP)

Department of Health (DoH)

Employment Tribunal Service (ETS)

Health & Safety Executive (HSE)

HM Customs & Excise

HM Prison Service

HM Treasury

National Assembly for Wales – Equality of Opportunity Committee

Office for Standards in Education (OFSTED)

Office of the First Minister and Deputy First Minister (Northern Ireland)

Scottish Executive

Small Business Service (SBS)

Monitoring and review: Default Retirement Age

Background

Following extensive consultation in 2003 and 2004, the Government has concluded that legislation should:

- Set a default retirement age of 65, but also create a right for employees to request working beyond a compulsory retirement age, which employers will have a duty to consider;
- Ensure close monitoring of the retirement age provisions so that evidence is available for a formal review of age discrimination five years from implementation; and
- Allow employers to objectively justify earlier retirement ages if they can show it is appropriate and necessary.

Objectives of the review

The default retirement age is being introduced because many businesses say they need it for reasons of workforce planning, and because not having a default retirement age could have adverse effects on pensions and other employment benefits.

Therefore, in 2011, our decision on whether to keep or abolish the default retirement age will focus mainly on two factors:

- **Whether the default retirement age remains appropriate and necessary to facilitate workforce planning and to avoid adverse effects on pensions and other employment benefits.**
- Other objectives of social policy.

The impact of the regulations on key stakeholders

Before deciding on what information to collect for the review, it is important to consider the likely impact (including unintended consequences) that the regulations will have on businesses, individuals and other stakeholders, taking into account that the environment may change (for instance the value of pensions may increase). Table 1 below describes a possible set of impacts and behavioural changes.

1. Possible reaction to retirement age legislation (including unintended consequences)

	Default age for specified period
Employers	<ul style="list-style-type: none">• Those who currently have a retirement age below 65 may need to raise their retirement age unless they can justify not doing so.• Employers without a normal retirement age may decide to introduce one.• Employers will need to consider how they deal with requests to work beyond the normal retirement age.• There may be incentives for employers to invest in extra training, although with a DRA so close to current normal retirement ages there may be little incentive to do so.• There may be a pre-legislative effect with employers making older workers redundant while they still can and changing the terms of their pension schemes.
Individuals	<ul style="list-style-type: none">• Employers may become confused by the changes to legislation.• Clarity about the retirement age may result in changes to savings behaviour.• With the DRA set at 65 this may limit options to work longer and save more.• With the right to request working beyond a normal retirement age, individuals may consider doing so for the first time (assuming that they are aware of this right).• Behaviour will also depend on occupational pension ages. If these are increased (see above) some workers will have to work longer.• Individuals' reasons for retiring may change, and the regulations may have little impact.
Unions	<ul style="list-style-type: none">• Unions may welcome the legislative changes or they may do deals with employers which would slow change.

Monitoring

The areas to be examined will include:

- **Information relevant to workforce planning:** such as changes in employers' use of age in workforce planning - both in businesses that have retirement ages and those that do not;
- **Information relevant to pensions:** such as trends in life expectancy, individual savings patterns and financial planning, and any changes to occupational pensions (what the changes are, why they have occurred, and any conclusions we can draw as regards the effect removing the default retirement age might have on pensions);
- **Information relevant to other employment benefits:** such as any changes to employment benefits (what the changes are, why they have occurred, and any conclusions we can draw as regards the effect removing the default retirement age might have on employment benefits); and
- **Other relevant information:** such as changes in people's expectations of retirement ages, changes by employers to their retirement ages (and the reasons for doing so), changes in participation rates in the labour market of those over 65

compared with other age groups (and the effect of the new duty to consider on this), changes in the numbers of requests to work beyond normal retirement age as well as in the percentages of accepted requests, and changes in patterns of work for older workers (including part-time work and other forms of flexible working).

We will use both independent information sources and informal discussions with our main stakeholders to monitor the developments in these areas between now and 2011.

Independent sources

This will involve the use of surveys (both quantitative and qualitative) and official databases. Some examples of the surveys we will use are the Labour Force Survey (LFS), the survey of Factors Affecting the Labour Market Participation of Older Workers (FALMPOW), the DTI/ DWP Survey of Employer Practices and the Employers' Pension Provision Survey (EPPS).

More detail on the list of surveys and the information we expect to get from them are in Table 2.

A baseline exercise of information that relies largely on official statistics has already been published.¹⁰⁸ Other surveys sponsored by DTI and DWP, that will also provide a baseline, have already been published or are in the field. These surveys are intended to be repeated, as appropriate in time for the review.

¹⁰⁸ See Urwin P. (2003) *Age matters: a review of existing survey evidence* Employment Relations Research Series No. 24, Department of Trade and Industry URN 03/1623

2. List of sources of independent sources of information

Sources of information	What source will show
Government sponsored surveys	
<ul style="list-style-type: none"> English Longitudinal Survey of Ageing (ELSA) Factors affecting the labour market participation of older workers (FALMPOW) (qualitative and quantitative) British Social Attitudes Survey (BSAS) Survey of individual awareness of ER legislation (IAERL) DTI/DWP Survey of employer practices (SEP) (qualitative and quantitative) Small Firms' Awareness study (SFAS) Worklife balance survey Employers' Pension Provision Survey (EPPS) Government Actuaries surveys (GAD) Survey of Employment Tribunal Applications (SETA) 	<ul style="list-style-type: none"> employers normal retirement ages (FALMPOW 2002; SEP 2004) labour market status of older workers by age (ELSA/FALMPOW) factors (including employer retirement ages) that affect LM participation (FALMPOW/ELSA) availability of options for flexible retirement (SEP;FALMPOW) number of hours worked per week (ELSA) perceptions about the incidence of discrimination (BSAS) changes in occupational pensions (EPPS; GAD) changes in other policies such as performance or competence appraisal, training, promotion, selection (SEP 2004) awareness of retirement age policy (SFAS; IAERL) employment tribunal applications by broad jurisdiction and age (SETA)
Official statistics	
<ul style="list-style-type: none"> Labour Force Survey New Earnings Survey (NES or ASHE) 	<ul style="list-style-type: none"> Employment rate of older workers; labour market status of older workers; hours worked by age; earnings by age; training by age; incidence of redundancy by age
Surveys sponsored by other organisations	
<ul style="list-style-type: none"> Chartered Institute of Personnel Directors Association of pension funds CROW 	<ul style="list-style-type: none"> occupational pension provision possibly changes in employers practices (CIPD, etc.)
Administrative databases	
<ul style="list-style-type: none"> Benefit recipients data (from DWP) Employment Tribunal Service (ETS) Occupational Pension Regulatory Authority (OPRA) 	<ul style="list-style-type: none"> numbers of claimants/other benefits by age number of tribunal applications, including unfair dismissals, redundancy and discrimination (will not be able to distinguish age of applicant) number of pension schemes by type and size of membership
Informal monitoring sources	
<ul style="list-style-type: none"> Feedback from a wide range of stakeholders (e.g., CBI, TUC, EEF, CIPD, Age networks (employers and individuals) etc.) using one to one meetings/focus groups etc. 	<ul style="list-style-type: none"> Reaction of employers and individuals; difficulties; unforeseen benefits/costs; potentially all that the above can show.

Informal contacts with stakeholders

The main organisations with an interest in the Age Regulations are representatives of employers, employees and age equality organisations. These include Age Concern, British Chambers of Commerce, the Confederation of British Industry (CBI), the Chartered Institute of Personnel and Development (CIPD), the Chartered Management Institute, Employers Forum on Age, Help the Aged, Third Age Employment Network and Trades Union Congress (TUC).

We have developed our policy on age discrimination (including retirement ages) in consultation with these stakeholders, and we will continue to stay in close contact with them. If their views alter over time, this could indicate whether the cultural change that we want has come about, which in turn will influence the decision on whether it is necessary and appropriate to keep the default retirement age. In addition, stakeholders may be able to give anecdotal feedback on the impact of the legislation "in the real world". To offset any risk that this information is biased, it will be important to talk to a wide range of stakeholders and to make sure that similar information (where relevant) is sought. Finally, they may be able to provide us with additional data from any surveys or monitoring activities that they carry out.

Timing

We will collect information from the outset as described above. We will carry out a formal review five years after the Age Regulations come into force to decide whether we will abolish the default retirement age. If so, we will give those affected (mainly employers) time to prepare before the removal of the default retirement age would become effective. Whilst information will become available in the period leading up to the decision in 2011, it would be sensible not to come to any conclusions before then.

Annex E

Summary of costs and benefits - options a to d

		Option a	Option b	Option c	Option d
Individuals	Costs	Prospect of an undignified exit from the labour market if performance declines greatly	Same as a.	Prospect of an undignified exit from the labour market if performance declines greatly	Same as e but less so
	Benefits	Some older workers who want to continue working beyond the present normal retirement age will be able to do so. This will allow them to earn more and to save more for retirement if they so choose. Illustrative calculations show extra earnings net of tax and lost benefits equal to £44-120m in yr 1 rising to £230-610m in yr 10. NPV¹⁰⁹ £1,300-3,500m over 10 years. Even those not retiring later may benefit from greater choice in when to retire.	As a, with extra net earnings of £29-100m in yr 1 rising to £140-490m in yr 10. NPV £830-2,900m over ten years	As a with extra earnings net of tax and lost benefits equal to £31-110m in yr 1 rising to £150-540m in yr 10. NPV £900-3,200m over 10 years.	As a, with extra net earnings of £12-67m in yr1 rising to £51-300m in yr 10. NPV £320-1,900m over ten years
			As a. but less so	As a. but less so	As a. but less so
Exchequer		Increased labour supply will increase tax revenues and decrease welfare payment, leading to net exchequer benefits of £35-93m in yr 1 rising to £190-490m in yr 10. NPV £1,100-2,800m over ten years.	Increased labour supply will increase tax revenues resulting in net exchequer benefits of £22-78m in yr 1 rising to £110-390m in yr 10. NPV of £670-2,300m over ten years.	Increased labour supply will increase tax revenues and decrease welfare payment, leading to net benefits of £24-84m in yr 1 rising to £120-430m in yr 10. NPV £730-2,500m over ten years.	Increased labour supply will increase tax revenues resulting in exchequer benefits of £8-52m in yr 1 rising to £40-240m in yr 10. NPV of £250-1,500m over ten years.
The economy	Benefits	Increase in labour supply (about 0.1% of the labour force) leading to increased GDP of about £100-270m in yr 1 rising to £530-1,400m in yr 10. NPV of £3,100-8,000m over ten years. Better job matching may lead to small increases in productivity Net effect of saving unclear	Increase in labour supply (about 0.08% of labour force) leading to increased GDP of about £67-220m in yr 1 rising to £320-1,100m in yr 10. NPV of £1,900-6,500m over ten years. As a but smaller effect Net effect on saving unclear	Increase in labour supply (about 0.09% of the labour force) leading to increased GDP of about £71-240m in yr 1 rising to £350-1,200m in yr 10. NPV of £2,100-7,100m over ten years. As a but smaller effect Net effect on saving unclear	Increase in labour supply (about 0.05% of labour force) leading to increased GDP of about £27-150m in yr 1 rising to £120-680m in yr 10. NPV of £740-4,200m over ten years. As a but smaller effect Net effect on saving unclear

¹⁰⁹ Net present value is a standard tool used in economic appraisals to value future returns. To adjust for the fact future returns are generally considered to be worth less than those today, we use a discount rate of 3.5 per cent, which means that the calculated costs and benefits are reduced by 3.5 per cent for each year beyond the first year, that they occur.

		Option a	Option b	Option c	Option d
Firms	One-off costs	Implementation costs of £69m Introduction of new appraisal systems: may be necessary for some firms Some firms may have to adjust their pay systems where they have pay enhancement based on expected endpoint.	Implementation costs of £99m Introduction of new appraisal systems: may be necessary for some firms Some firms may have to adjust their pay systems where they have pay enhancement based on expected endpoint.	Implementation costs of £107m Introduction of new appraisal systems: may be necessary for some firms Some firms may have to adjust their pay systems where they have pay enhancement based on expected endpoint.	Implementation costs of £70m Introduction of new appraisal systems: may be necessary for some firms
	Recurring costs	In some firms it may be harder to retain and encourage younger workers looking to replace older workers. Adjustment of appraisal systems: upper end of £18-36m each year npv £150-310m over ten year period.	As a but smaller effect Adjustment of appraisal systems : upper end of £18-36m each year, npv £150-310m over ten year period.	As with a. but smaller effects . Adjustment of appraisal systems: upper end of £17-37m each year, npv £150-310m over ten year period. Handling requests to continue working past the EJRA or DRA – including Employment Tribunals: £0.2-0.5m each year, npv £2.0-5.6m over ten years	Handling requests: £0.5-2.5m each year, npv £4.9-25m over ten years
	Benefits	Savings on recruitment costs: first year £14-36m, npv over 10 years £110-280m. Small increase in size of labour pool will mean better job matching. Increase in productivity because of better appraisal systems. Better performance from more motivated and perhaps more trained older workers Increase in profits due to increase in size of the labour supply. Illustrative calculations show net benefit of around £22-58m in yr 1 rising to £120-300m in yr ten. NPV £680-1,700m over ten years.	Savings on recruitment costs: first year around £10-31m, npv over ten years £75-240m. As a but smaller effect As a but smaller effect As a but smaller effect Increase in profits due to increase in size of the labour supply. Illustrative calculations show net benefit of around £15-49m in yr 1 rising to £70-240m in yr ten. NPV £420-1,400m over ten years.	Savings on recruitment: first-year around £10-33m, npv over 10 years £80-250m. As a. but smaller effect As a. but smaller effect As a. but smaller effect. Illustrative calculations show net benefit of around £16-53m in yr 1 rising to £76-260m in yr ten. NPV £450-1,600m over ten years.	Savings on recruitment: first-year around £4.4-21m per year, npv over ten year £31-160m. As a. but smaller effect As a. but smaller effect Illustrative calculations show net benefit of around £6-33m in yr 1 rising to £26-150m in yr ten. NPV £160-910m over ten years.
	Net quantified impact on firms	Net benefit of around £310-1,700m over ten years.	Net cost of around £16m to net benefit of around £1,300m over ten years.	Net benefit of around £24-1,400 over ten years.	Net benefit of around £17-880m over ten years.
	Net quantified impact on firms due to changes in total factor productivity.	Net cost of around £320m to net benefit of around £46m over ten years. More likely to be towards the latter.	Net cost of about £68-320m over ten years. More likely to be towards the latter.	Net cost of around £64-390m over ten years. More likely to be towards the latter.	Net cost of about £94m to net benefit of around £15m over ten years. More likely to be towards the former.

Competition Filter

Competition Filter	
Question	Answer
1. In the market(s) affected by the new regulation, does any firm have more than 10% market share?	No
2. In the market(s) affected by the new regulation, does any firm have more than 20% market share?	No
3. In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	No
4. Would the costs of the regulation affect some firms substantially more than others?	No
5. Is the regulation likely to affect the market structure, changing the number or size of firms?	No
6. Would the regulation lead to higher set-up costs for new or potential firms that existing firms do not have to meet?	No
7. Would the regulation lead to higher ongoing costs for new or potential firms that existing firms do not have to meet?	No
8. Is the sector characterised by rapid technological change?	Not relevant
9. Would the regulation restrict the ability of firms to choose the price, quality, range or location of their products?	No

Statutory redundancy pay

March 2006

<http://www.dti.gov.uk/er>

Purpose and intended effect

Objective

1. The objective of changing the legislation on statutory redundancy payments is to reduce age discrimination in the workplace, in a way that is consistent with the overall social policy aims of the statutory redundancy scheme.

Rationale for government intervention

2. In 2006 the Government will bring legislation into force under the European Employment Directive¹¹⁰ outlawing age discrimination in employment and vocational training. Compliance with the EU Employment Directive may have implications for the structure and operation of the statutory redundancy scheme.

3. The current legislation entitles redundant employees of different ages to different multiples of their years of service in calculating their statutory redundancy payments. Table 1 shows how entitlement is calculated under the existing system.

1. Weeks earned for each year of service, by age group

Age	Entitlement	Weeks earned per year of service in this age band
Under 18	No	0
18-21	Yes	0.5
22-40	Yes	1.0
41-64	Yes	1.5
65 and over	No	0

To qualify for statutory redundancy payments, employees have to have completed two years' continuous service. For each complete year of continuous service between the ages of 18 and 21, employees receive half a week's pay. For each complete year of continuous service between the ages of 22 and 40, employees receive one week's pay. For each complete year of continuous service between the ages of 41 and 65 employees receive 1½ weeks' pay. However, if employees are over 64, the total

¹¹⁰ Council Directive 2000/78/EC of 27 November 2000 establishing a general framework for equal treatment in employment and occupation:
http://europa.eu.int/comm/employment_social/fundamental_rights/pdf/legisln/2000_78_en.pdf

amount of the payment received is reduced. There is a cap of twenty years on reckonable service.

4. This amounts to treating people differently on account of their age. Unless it can be objectively justified, this would amount to unlawful discrimination.

5. The Government considers that those aspects of direct age discrimination in statutory redundancy payments that cannot be objectively justified in terms of the aims of the scheme should be removed.

Consultation

Within Government

6. These proposals have been developed in consultation with various interested Government departments including the Department for Work and Pensions and HM Treasury.

Public Consultation

7. The Department of Trade and Industry has consulted both formally and informally, on changes to the statutory redundancy payments scheme. In the formal consultation in 2003, it asked a number of questions about the age-based elements of the scheme, as well as the retention of length of service as a factor in the payment calculation and the retention of the 20-year limit. The responses broadly showed support for removing the age-based elements of the scheme and support for the retention of using length of service as a factor and for the 20-year limit. However, informal consultation has subsequently shown some concern from business about removing the limit of 65 years, which was not asked about in the formal consultation.¹¹¹

8. Responses to the 2005 consultation document 'Coming of Age'¹¹² on this issue can be divided into two broad categories. A number of trade unions argued that the present age-banded system should be replaced by a single multiplier, and that this should be set at the level of 1.5 to ensure that no workers would be worse off.

9. However a number of employers' organisations called for the Government to retain the present age-banded system, on the grounds that this would ensure no workers were worse-off and avoid disruption to employers' existing contractual schemes. They also argued that if a single multiplier were preferred, this should be set at a level designed to ensure an outcome that was cost-neutral for employers.

10. The Government has held a series of meetings in recent months with key stakeholders to discuss the way forward on the redundancy scheme, against the background of 'Coming of Age'.

11. In the course of those meetings the Government became concerned that a system using a single multiplier might not meet our overall policy aims. We have therefore carefully examined the rationale for the current scheme, and come to the conclusion that this provides the best fit with our aims¹¹³.

¹¹¹ For details of the formal consultation in 2003, called *Equality and Diversity: Age matters*, and the results of the consultation see <http://www.dti.gov.uk/er/archive.htm>. Key results of the 2003 consultation with respect to statutory redundancies are given Chapter 7.

¹¹² *Equality and Diversity: Coming of Age*, Consultation on the draft Employment Equality (Age) Regulations 2006, July 2005, URN 05/1171

¹¹³ The Government has considered carefully the economic evidence surrounding the current age structure of the statutory redundancy payments scheme. In doing so it has assessed the relative risks of

12. The Directive provides for the possibility of Member States providing for different treatment on the grounds of age, where this difference of treatment is objectively and reasonably justified by a legitimate aim, including employment policy¹¹⁴. We have looked at this question very closely and we are confident that retaining the age bands is permitted by the Directive.

Options

13. The statutory redundancy payments scheme, introduced in 1965, currently has a number of aspects that may be judged to discriminate directly on grounds of age. Where these cannot be justified, they ought to be removed. There are however other aspects of the scheme, that could be said to have an indirect disparate impact on different age groups, but that the Government proposes to retain and to justify objectively for the following reasons.

- The two year qualifying period of continuous service: An employee with less than that length of service cannot be said to have demonstrated sufficient commitment to justify payment¹¹⁵;
- The use of length of service as a factor in the payment calculation: This is an obvious proxy for degree of dedication and commitment;
- The use of weekly pay at the time of dismissal (subject to the statutory upper limit) as a factor in the payment calculation: This reflects the position the employee has reached in the employer's business and is the most (and arguably only) administratively convenient figure to use – particularly given that many employers do not keep long-term records that could be used, for instance, to work out a career average rate of pay; and
- The 20 year cap on length of service taken into account in the payment calculation: Its removal would expose employers to the risk of excessive financial burdens in the event of a redundancy situation – which could lead them to have to make even more redundancies or even drive them into insolvency.
- Under certain policy options (discussed below), redundancy pay would continue to vary according to employees' length of service in different age bands in order to meet the Government's social policy aims.
- Although the removal of age discrimination in employment is the key objective of the Directive, consideration also needs to be given to the distributional impact of changes in the labour market across different age groups. Thus adequate protection may be needed for the more vulnerable groups.

14. In order to achieve its objectives in reducing the extent of age discrimination in the workplace and in complying with European law requirements, the Government considered the following principal options:

redundancy by age and has examined the respective wider labour market and social characteristics of the groups involved and the factors underlying their opportunities for re-employment.

¹¹⁴ Council Directive 2000/78/EC, Article 6

¹¹⁵ In a survey of employers in 2000/01, 75 per cent thought that the two-year length of service requirement was about right; 13 per cent thought it was too long and 10 per cent thought it was too short. Source: IFF Research Ltd (unpublished) *Employers' Redundancy Practices* – copies available on request.

Option A:

The statutory redundancy payments system is broadly retained in its current form but with the following modifications:

- Remove the age 18 lower limit on service taken into account for the purposes of qualification and payment calculation under the scheme;
- Remove the upper age limit on entitlement, thereby giving employees aged 65 and over the right to statutory redundancy payments for the first time;
- Repeal the provision under which the amount of payment due is tapered by one twelfth for each month elapsed between the ages of 64 and 65; and
- Revoke the Redundancy Payments Pensions Regulations 1965 SI 1965/1932. Under these Regulations, employers may offset pensions or lump sums that are paid immediately on redundancy or within a short time after and that meet specified conditions, including the condition that the Secretary of State is satisfied as to certain matters. According to the amount of the pension or lump sum payable, the statutory redundancy payment due may be either reduced or extinguished completely. There has been little or no use of these provisions (one case in the last ten years).

Option B:

15. A single weekly multiplier across all age bands is used to determine statutory redundancy payments, in addition to the modifications outlined under option (a).

Preferred option

16. Many of the issues were previously discussed in *Age Matters* and the follow-up consultation *Coming of Age*. Both consultations were based on an assumption that the current system of different multipliers for different age bands was discriminatory and would have to be removed. The Partial RIA¹¹⁶ examined the costs and benefits of implementing a single multiplier (option b) as a possible means of removing the elements of age discrimination within the statutory redundancy payments scheme.

17. However further research and analysis, as well as responses to the consultation, have highlighted the fact that some age-related elements of the current system are objectively justifiable¹¹⁷. Therefore the Government's preferred option is option a. For consistency with the Partial RIA costs and benefits will be presented in this RIA for both options.

Costs and benefits

Business sectors affected

18. Table 2 shows the distribution of redundancies by industrial sector and compares this to the distribution of all employees. It is clear that in 2001 proportionally more employees were made redundant in manufacturing. However, the distribution of redundancies by sector is likely to vary from year to year, depending on business conditions.

¹¹⁶ Partial Regulatory Impact Assessment: Statutory Redundancy Payments, DTI, July 2005.

¹¹⁷ See paragraphs 11 and 12 above.

2. Distribution of redundancies and employees by industry

	Redundancies (%) (2000/01)	Employees Spring 2001
Manufacturing	46	18
Mining, construction, utilities and agriculture	4	7
Wholesale and retail	18	15
Financial and business services	18	15
Transport and communications	*	7
Public administration	*	8

Source: IFF Research Ltd *Employers' Redundancy Practices and Labour Force Survey* *sample size too small

Employees

19. Table 3 below shows estimates of statutory redundancy payments due to employees per year, if they are made redundant, under each policy option. The figures are based on the numbers of employees who said that they had been made redundant 18 over a one-year period and who had at least two years of service. To estimate statutory payments, we have used information on when employees started work with their employer and their weekly earnings. Estimates have been disaggregated by age, so that some adjustment can be made to take into account the different characteristics of those being made redundant compared with all employees.

3. Estimates of statutory redundancy payments to employees

	£280 limit	£300 limit	£310 limit	£320 limit
Existing system	1030m			
Option (a): removing lower and upper age limits	1045m	1100m	1120m	1145m
Option (b): single multiplier and no lower or upper age limits				
1 week	890m	940m	960m	980m
1.1 weeks	980m	1030m	1050m	1070m
1.5 weeks	1340m	1410m	1440m	1470m

The table gives estimates for the existing system, based on a statutory limit of £280¹¹⁹ for a week's pay.¹²⁰ The table also gives estimates of - options (a) and (b) with different statutory limits. Options (a) and (b) both include removing the upper age limit, which is estimated to cost £2.4 - £3.6 million depending on the multiplier applied to older workers.

20. The following effects are observed under all of the options:

- Employees below the age of 20 with two years of service will have the right to redundancy payments for the first time. (According to the Labour Force Survey, however, this would affect a negligible number of people).

¹¹⁸ Source: Labour Force Survey, from Summer 2003 to Spring 2004

¹¹⁹ The weekly limit increased to £290/week in February 2006 but we have used £280 in this document to ensure consistency with previous versions of this RIA.

¹²⁰ The minimum payment is currently calculated as follows: half a week's pay for each year of service between the ages of 18 and 21, one week's pay for each year of service between 22 and 40, and one-and-a-half week's pay between 41 and 65, in all cases with weekly pay subject to a maximum of £280 and the number of years of service to a maximum of 20.

- Employees aged 64 will no longer see their entitlement reduced by a twelfth every month till they are 65.
- Employers aged 65 and above will have the right to statutory redundancy payments for the first time. If it is decided to have a default retirement age and/or to allow firms to set their own mandatory retirement ages (that they will have to justify), then some employers might make use of the DRA/EJRA provisions to retire their staff instead of making them redundant to avoid paying redundancy pay. According to the Labour Force Survey, a negligible number of people say they are made redundant at age 65 and over. This is likely to benefit between about 1,700 and 7,700 employees.¹²¹

21. The impact of option (b), a single multiplier for all age groups, depends on the multiplier chosen. For any multiplier below 1.5, employees aged between 42 and 63 would see their entitlement fall, since their entitlement for service at ages 42 and over would be reduced. Conversely, for any multiplier above 1.0, employees up to the age of 41 would see their entitlement rise.

Impact on employers

22. Any changes to statutory redundancy payments could have an impact on employers, depending on their circumstances:

- Those who pay the statutory minimum will in theory have to pay a different amount to their employees, depending on the policy option pursued
- This might not be the case for those who are unable to make redundancy payments either in part or in full because of insolvency. In which case the Exchequer may have to pay part or all of the payments due.
- Those who currently pay over the new statutory minimum will not be directly affected, but may increase their payment anyway.

23. Evidence suggests that a substantial number of employers (maybe around half) pay above the statutory minimum.¹²²

24. Normally, statutory redundancy payments are paid by employers direct to redundant employees. However, if employers fail to do so¹²³ the Insolvency Service (IS) pays employees from the National Insurance Fund on employers' behalf. In 2003/04, the IS spent about £120 million on statutory redundancy payments. This is about 12 per cent of our estimate of the total amount due to employees under the existing system of around £1030 million.¹²⁴

¹²¹ The numbers benefiting depends on whether the redundancy rate for those aged 65 and over is the same as it is today (about 0.5 per cent) or the same as other age groups (about 2.4 per cent). With the legislative change it is likely that the redundancy rate could rise towards the latter.

¹²² The current mean statutory minimum redundancy payment (based on the Labour Force Survey) is estimated at about £2,200. The Family Resources Survey 2002-03, suggests a median actual redundancy payment of £5,000, based on a sample size of 452. A report by IFF Research Ltd. for the Department of Trade and Industry in 2001 found that 48% of employers made some improvement to the statutory entitlement for at least one employee made redundant. Of these, 77% offered an improvement to all employees, and 23% to just some of their employees. The sample size was 1,085. The 2002 Survey on redundancy by the CIPD found that 72% of employers paid redundancy compensation above the statutory minimum. The CIPD report was based on a sample size of 563, but was heavily biased towards larger firms, which according to the IFF report, are more likely to pay redundancy pay above the statutory minimum.

¹²³ For instance, due to insolvency or financial difficulty.

¹²⁴ Note that this has changed from 13 per cent in the partial RIA (July 2005), due to updated policy costs.

25. Based on this information and what we know about the proportion of employers who pay over the statutory minimum, employers will probably have to bear between 44 and 88 per cent of the changes to the scheme. It is important to note that the total policy costs presented above in Table 3 are *maximum* total policy costs, as some employers may currently pay above the statutory minimum and therefore not be affected.

26. Table 4 shows how much this will cost or benefit employers for different options each year. This was calculated as 44 to 88 per cent of the total policy cost for each option. A positive sign indicates that employers stand to gain and a negative sign indicates that they will lose, compared to the existing scheme.

	Low (44 per cent)			High (88 per cent)		
	£280 limit	£300 limit	£320 limit	£280 limit	£300 limit	£320 limit
Option (a): removing lower and upper age limits	-4.5m	-27.0m	-48.0m	-9.1m	-53.9m	-96.0m
Option (b): single multiplier and no lower or upper age limits						
1 week	+61.4m	+42.2m	+24.1m	+122.8m	+84.4m	+48.2m
1.1 weeks	+22.1m	+0.9m	-19.0m	+44.2m	+1.9m	-37.9m
1.5 weeks	-135.3m	-164.1m	-191.2m	-270.5m	-328.2m	-382.4m

27. Most employers, even those who have a redundancy agreement, may not incur any additional costs in becoming aware of the legislation, as they would probably do so on an ‘as needs’ basis, whatever the formula.

28. Some employers have automated payroll systems that include paying statutory minimum redundancy payments, which would need changing. We do not have any information on the extent of these systems, nor what the cost would be of updating these systems.

29. Employers and unions have also highlighted to us that there may be extra costs in negotiating agreements over the statutory minimum under option (b), due to lack of familiarity of the new system. We do not have any evidence on the extent of contractual redundancy agreements that set out how much above the statutory minimum employers would pay.¹²⁵ It is likely, however, that some employers and unions or staff representative who have contractual arrangements in place or who have established some precedent for what is an acceptable improvement on the statutory minimum, would have to renegotiate them in the light of the new formula. We do not attempt to quantify this.

Exchequer

30. The Insolvency Service pays employees where employers are insolvent or otherwise unable to pay statutory redundancy pay. In addition, the statutory limit is also applied to other payments such as unpaid wages, notice pay and outstanding holiday pay. Each of these has costs to the Exchequer, as shown in the table below. A positive sign indicates that the Exchequer stands to gain and a negative sign indicates that it will lose, compared to the existing scheme.

¹²⁵ Although informal consultation with employers have shown us that they do exist and case studies suggest that this is not unusual. For evidence of the latter see IDS Studies Plus Personnel policy and practice (2001) *Managing redundancy* Income Data Services Ltd.

5. Impact on Exchequer of various options compared to doing nothing

	£280 limit	£300 limit	£310 limit	£320 limit
Option (a): removing lower and upper age limits	-1.2m	-7.4m	-10.3m	-13.1m
Option (b): single multiplier and no lower or upper age limits				
1 week	+16.8m	+11.5m	+9.0m	+6.6m
1.1 weeks	+6.0m	+0.3m	-2.5m	-5.2m
1.5 weeks	-36.9m	-44.8m	-48.5m	-52.2m

These Exchequer costs are calculated as 12 per cent of the total policy cost of each option (see explanation in paragraph 25 above).

31. The computer system used to process these payments will need to be reprogrammed in light of the changes in the scheme. It is estimated that this will cost up to £100,000. This is an implementation cost.

Economy

32. Changes to statutory redundancy payments are essentially changes to transfers between different sectors of the economy (individuals, firms and the Exchequer). Therefore there will be no direct impact on the economy, with the exception of implementation costs. There may, however, be indirect effects, in so far as the policy aids the transition of different groups back into work, or promotes a sense of security and commitment while employed. Given that the changes to the scheme are relatively marginal, and that many employers already pay above the statutory minimum, we do not expect the changes to have a significant effect on the economy.

Equity and fairness

33. Equity and fairness of any policy option needs to be considered in the light of labour market circumstances affecting different age groups. Thus what counts as fair depends on the social policy objective under consideration. Revising the formula used to calculate statutory redundancy payments, so that it does not depend on age, would mean that workers were not discriminated against on the basis of age in this area. Options that increase the number of weeks pay per year of service that redundancy pay is based on would benefit all workers. However, although lower paid workers would see the same proportional increase as higher paid workers, their absolute increase would be lower. Options that increase the statutory limit would benefit those who earn over that limit.

Race equality impact assessment

34. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firms impact test

35. The legislation will impact on all firms. Small workplaces are much less likely to say that they have made redundancies in the last year.¹²⁶ It is likely that small employers will be less affected by any changes to the legislation.

¹²⁶ Source: Tables 32 and 17 of IFF Research (unpublished) *Employers' Redundancy Practices* Department of Trade and Industry. Of workplaces with 5-24 and 25-99 employees, 4 and 16 per cent,

Competition assessment

36. The legislation applies to all firms. We have applied the Competition Filter and have concluded that there will be negligible impact on competition (see Annex), although we note that manufacturing firms have the highest share of redundancies, as detailed in Table 2, meaning that this sector could be affected substantially more than others, depending on the policy option chosen.

Enforcement, sanctions and monitoring

37. Enforcement will be, as is currently the case, through the tribunal system.

Implementation and delivery plan

38. Subject to Parliament's approval the age regulations will be in place by spring 2006, at least six months before they come into force in October 2006. The level and timing of any new weekly limit to the statutory redundancy payment remains under discussion. A one-off order-making power to increase the limit by more than the current index-linked formula is included in the Work and Families Bill, which is presently before Parliament.

39. Acas are preparing guidance and will be road testing it with stakeholders. They are consulting widely with stakeholders (small business in particular) as they develop and refine guidance further. In addition to that, we are holding a conference in April 2006 to widely publicise the legislation.

Post-implementation review

40. Monitoring will be required to check on the impact of the new rules on employers and on employees. The DTI undertook a survey in 2000/01 which asked about employers' redundancy practices, looked at the demographics of employees who were made redundant and sought views of the statutory scheme. We envisage conducting a similar survey three to five years after the new regulations are produced.

41. Statistics will also be collected on an annual basis from the Insolvency Service to monitor the number of claims made where employers have been unable to pay the statutory minimum. The Department will also monitor on a quarterly basis the number of claims to Employment Tribunals that are related to redundancy payments.

42. The proposal to retain the current broad age-banded system (option a) will require the Government to monitor the labour market circumstances of different age groups regularly to ensure that the "objective justification" criteria are still met.

Summary and recommendation

43. This RIA considered two options to address the implications of the changes to the statutory redundancy payments scheme that may potentially be required as a result of implementation of the European Employment directive. The impact on firms, employers and the Exchequer of the preferred option of retaining the current age-banded system is summarised in Table 6 below.

respectively, said that they had made redundancies in the last 12 months, compared with 37 and 50 per cent for those with 100-499 and 500 and over employees, respectively.

6. Summary of costs and benefits of changes to the formulae for statutory minimum redundancy payments compared with doing nothing

		Annual benefits (£m)	Annual Costs (£m)	Implementation Costs (£m)
Option (a): removing lower and upper age limits, while retaining current age-banded system	Firms		£4.5m-£9.1m	
	Employees	£15m		
	Exchequer		£1.2m	£0.1m

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

**Gerry Sutcliffe
Parliamentary Under-Secretary of State (Minister for Employment Relations
and Consumer Affairs)**

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Competition Filter

Competition Filter	
Question	Answer
1. In the market(s) affected by the new regulation, does any firm have more than 10% market share?	No
2. In the market(s) affected by the new regulation, does any firm have more than 20% market share?	No
3. In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	No
4. Would the costs of the regulation affect some firms substantially more than others?	Yes
5. Is the regulation likely to affect the market structure, changing the number or size of firms?	No
6. Would the regulation lead to a higher set-up costs for new or potential firms that existing firms do not have to meet?	No
7. Would the regulation lead to higher ongoing costs for new or potential firms that existing firms do not have to meet?	No
8. Is the sector characterised by rapid technological change?	Not relevant
9. Would the regulation restrict the ability of firms to choose the price, quality, range or location of their products?	No

Unfair dismissal

March 2006

<http://www.dti.gov.uk/er>

Purpose and intended effect of measure

Objective

1. The aim of these regulations is to ensure that all workers, no matter their age, are treated fairly when they are dismissed. This should also result in increased security for those workers currently not covered, and therefore an increase in their willingness to participate in the workforce.

Background

2. Under the Employment Rights Act 1996 (the "**ERA**"), most employees who have one year's qualifying service with their employer have the right not to be unfairly dismissed. This means that:

- (i) The reason for dismissal must be one of the reasons set out in the legislation as being potentially fair (e.g., redundancy, capability, conduct, 'some other substantial reason'); and
- (ii) The employer must act fairly in the way he or she carries out the dismissal (e.g., did the reason justify dismissal in the particular circumstances? Did the employer carry out fair procedures?)

3. Employees who successfully claim unfair dismissal can be awarded financial compensation in the form of a basic award, calculated in the same way as a redundancy payment¹²⁷, and a compensatory award (which is not based on age criteria).

4. However, except in limited circumstances, such as specified health and safety dismissals (where the one-year qualifying period also does not apply), the right not to be unfairly dismissed does not currently apply to employees who have reached the normal retirement age for their job, or, if there is no normal retirement age, the age of 65.

¹²⁷ The formula for statutory redundancy payments is as follows: to qualify for statutory redundancy payments, employees have to have completed two years' continuous service. For each complete year of continuous service between the ages of 18 and 21, employees receive half a week's pay. For each complete year of continuous service between the ages of 22 and 40, employees receive one week's pay. For each complete year of continuous service between the ages of 41 and 65 employees will receive 1½ weeks' pay. However, if employees are over 64, the total amount of the payment received will be reduced. There is a cap of twenty years on reckonable service and on a week's pay (£290 as from February 2006. The previous limit of £280/week has been used in this RIA to ensure consistency with the RIA on the Statutory Redundancy Pay Scheme).

5. The basic unfair dismissal award is calculated in the same way as a statutory redundancy payment, on the principle that an employee who is dismissed unfairly should be entitled to at least as much compensation as one who has been fairly dismissed through no fault of his or her own. The Partial RIA on redundancy payments published in July 2005 recommended that we remove or justify the age-based criteria used in the calculation of redundancy pay. The method used to calculate the basic award for unfair dismissal would need to be consistent with the calculation of statutory minimum redundancy pay.

Rationale for government intervention

6. The Government has proposed having a Default Retirement Age (DRA) of 65 (at least until 2011). To achieve this, compulsorily retiring an employee at the DRA (or an employer-justified retirement age) must constitute neither age discrimination nor unfair dismissal.

7. However, the upper age limit on unfair dismissal goes well beyond this. It categorically withholds the possibility of legal recourse from employees at or above their normal retirement age (or, as the case may be, the age of 65) against a wide range of ways of unfair dismissal which are unrelated to retirement (for instance allegations of theft), including where the dismissal is carried out with an unfair procedure. This is not only unfair, but it could also act to discourage those older workers participating in the workplace.

8. In the Partial RIA it was stated that providing a different calculation for awards for unfair dismissal and redundancy would mean that elements of age discrimination would remain in the way awards were calculated and that this would be hard to justify.

Consultation

Within government

9. These proposals have been developed in consultation with various interested Departments including the Department for Work and Pensions, the Department for Education and Skills, HM Treasury, HM Revenue and Customs, Cabinet Office and the Small Business Service.

Public consultation

10. Our aim was to ensure that the default age was honoured, so that employers retiring individuals on or after the DRA (or an employer-justified retirement age) would be secure from challenge provided they followed the correct procedure and the dismissal was a planned retirement. Consultees (legal as well as employer bodies), argued persuasively that the ability for employees to claim that retirement was not the real reason for their dismissal, opened up far too much scope for challenge and would result in confusion and unnecessary tribunal cases. We have tightened up the provisions so that employers who have provided sufficient (at least 6 months) notice of retirement on the default or employer justified retirement age and who have followed the duty to consider procedure, will be protected from challenges on grounds of unfair dismissal.

11. We have also tightened up some of the drafting by removing language that would open up the possible number of retirement decisions to challenge in employment tribunals. The removal of such language should reduce the potential cost to employers, brought about by unnecessary claims.

12. The Government has held a series of meetings in recent months with key stakeholders to discuss the way forward on the Statutory Redundancy Pay scheme, against the background of *Coming of Age*. The outcome of these discussions and the subsequent decisions taken by Government would therefore have implications for the formula used to calculate basic awards for unfair dismissal.

13. In the course of those meetings the Government became concerned that a system using a single multiplier might not meet our overall policy aims. We have therefore carefully examined the rationale for the current scheme, and come to the conclusion that this provides the best fit with our aims¹²⁸.

14. This RIA has now been revised to reflect this approach and to ensure consistency with the formula used in the statutory redundancy payment scheme.

Options

15. This RIA will consider options for the upper age limit and for the calculation of awards for unfair dismissal.

(1) Upper age limit

16. Currently there is an upper age of the normal retirement age for their job, or, in the absence such an age, the age of 65 for those who are able to claim for unfair dismissal. The options are:

- (a) Maintain the upper age limit
- (b) Remove the upper age limit

17. Option a would still retain the exceptions to the age limit for specified reasons such as particular health and safety grounds, so older employees might attempt to argue that these were the reasons for their dismissal. However, it would fail to meet the objective of treating those fairly irrespective of their age in the case of a dismissal and would carry a high risk of challenge, since it would directly discriminate against older employees.

18. Other options, similar to option a, were also considered, which while maintaining the upper age limit for claims for unfair dismissal, allowed for claims to be made in the event of procedural irregularities related to the termination of employment. These options carry the same risks as option a, and are therefore not considered in this RIA.

19. Option b would result in people being treated the same irrespective of their age, as those over 65 would be able to claim should they think they had been treated unfairly, albeit at a cost to employers.

(2) Calculation of basic award

20. Currently, the basic award is calculated using the same formula for statutory redundancy payments. In the Partial RIA the options for calculating the basic award for unfair dismissal were:

- (c) No change to calculation
- (d) Change in calculation of formula based on a single multiplier

21. Option c ensures consistency with the existing formula for the statutory minimum compensation for redundancy.

22. The two consultations *Age Matters* and *Coming of Age* conducted in 2003 and 2005 respectively were based on the assumption that the current system of different

¹²⁸ See the RIA on Statutory Redundancy Payments Scheme for details.

multipliers for different age bands was discriminatory and would have to be removed. The previous RIA on Unfair Dismissal therefore presented an option for a change in the formula used based on the adoption of a single multiplier. As stated above, following consultation with stakeholders, the Government carefully examined the rationale for the current redundancy scheme and came to the conclusion that this provides the best fit with the Government's overall social policy aims.

23. Option c is therefore the Government's preferred option. Although a single multiplier option is no longer being proposed, option d below simply updates those costs and benefits presented in the partial RIA.

Costs and benefits

Business sectors affected

24. Table 1 gives a breakdown of unfair dismissal claims to Employment Tribunals by industrial sector, and compares this to the proportion of employees in that sector. It shows that the regulations are likely to impact proportionately more on manufacturing and less on other services/public administration compared with other industries. The manufacturing sector is also more likely to be affected by changes to the formula for redundancy payments. This is probably due to the structural changes to the economy seen in recent decades, resulting in a decline in manufacturing employment. To what extent this will continue in the future is uncertain.

1. Industrial breakdown of unfair dismissal claims

	Unfair dismissal claims (%)	All employees (%)
Agriculture/hunting/forestry and fishing	1	1
Manufacturing	28	15
Construction	6	6
Wholesale/retail	13	16
Hotels/restaurants	5	4
Transport/Communications/utilities	10	8
Finance	6	5
Other services/Public administration	29	44

Source: Survey of Employment Tribunal Applications 2003 (www.dti.gov.uk/er) and the Labour Force Survey (Spring 2003)

Assumptions

25. Detailed characteristics of those claiming for unfair dismissal are difficult to obtain due to sample sizes in the relevant survey. However their broad characteristics are not dissimilar to those who are made redundant.¹²⁹ We have, therefore, used the model established for working out the impact of changes in the formula for redundancy¹³⁰ to estimate the impact on awards for unfair dismissal.

26. There is also a lack of information on those being dismissed at 65 or at their employer's normal retirement age (again due to sample sizes). Even if we had this information it would not be possible to distinguish if an employee was being retired or dismissed, as currently the employer does not have to justify the decision and there is no recourse to the law that would enable this to be tested. Also unfair dismissal would only apply to a small proportion of all dismissals.

¹²⁹ They have a similar job tenure and age profile.

¹³⁰ See RIA on redundancy payments

27. We have instead used information on the number of tribunal claims and previous work on disputes to estimate the numbers affected. The RIA on dispute resolution procedures estimated that approximately 12-16 per cent of disputes would result in a claim to an Employment Tribunal. There were on average about 47,000 claims to Employment Tribunal, where unfair dismissal was the main jurisdiction, in the three years to 2003/04. This implies that there were about 300,000 to 390,000 disputes that related to unfair dismissal. The number of employees between 16 and 64 years in spring 2004 was about 23.3 million; the number of employees aged 65 and over was about 0.3 million. Assuming that employees aged 65 and over are proportionately as likely to have a dispute as those under 65, this means that there could be about 4,000 to 5,300 disputes that are related to unfair dismissal. This could result in about 640 extra tribunal applications each year.

Benefits to individuals and firms of changes to upper age limit

28. Option a - no change - would fail to meet the objective of treating those fairly irrespective of their age in the case of a dismissal and would carry a high risk of challenge since it would directly discriminate against older employees.

29. Option b would result in those aged 65 and over having the right for the first time to redress if they felt that they had been dismissed unfairly. This would result in greater fairness and may encourage more workers to stay in the workforce. However, there is a risk with this option that employers will be cautious about allowing individuals to remain in employment beyond the DRA, if they fear that they may be taken to an Employment Tribunal, should they need to dismiss them for fair reasons. We do not attempt to quantify this.

Benefits to individuals of changes in the formula for calculating awards

30. Option c - no change - would maintain the current system and result in years of service at different ages being treated differently.

31. Option d would mean bringing the compensation of those dismissed unfairly and would result in years of service at different ages being treated equally, including years of service at 65 and over. The change in compensation compared with option c, is outlined in Table 2.

Cost to firms of changes to upper age limit

32. Firms should already be aware of legislation on dismissal. They will need to note that this now applies to all employees, and how they should treat older employees when asking them to cease working for them. The cost of the latter will largely be incurred when seeking to understand the legislation on retirement ages and so we do not envisage implementation costs to firms arising from changes to this legislation alone. Implementation costs due to retirement age legislation are considered in the relevant RIA.

33. Firms will have to deal with dismissals for those employees aged 65 and over in the same way as for other employees. In the event of a dismissal they will be bound to follow the minimum statutory dispute resolution procedures.

34. The RIA on dispute resolution estimated that in about 24 per cent of cases the procedures are either exempt or individuals will decide not to take action. If this was also the case for disputes arising from dismissal of those aged 65 and over, this would

mean that employers would bear the cost of procedures arising from an extra 3,000 to 4,000 disputes.¹³¹

35. Previous estimates of the costs of a dispute arising from a disciplinary procedure were:

- Three to six hours of a manager's time at a cost of about £60 to £120¹³²
- Two to four hours of staff time at a cost of about £24 to £48¹³³

36. The total additional cost to all firms will therefore be about £0.3 million to £0.7 million each year.

37. There will also be the cost to firms of tribunals. This is estimated to cost about £2.1 million each year.¹³⁴

Cost to firms of changes to award formula

38. Firms do not need to become familiar with the legislation on the award formula; should they have to pay an award, they will be told by the Employment Tribunal how much this should be. However, they may want to become aware of the formula, should they think that an award against them is likely. We assume that this information would be sought on a case-by-case basis, and would be incurred even in the absence of a change in the formula. Therefore no extra costs should be involved.

39. Apart from years of service at different ages being treated equally, the formula can change in two other respects:

- The upper limit for the weekly wage used in calculating benefits
- The multiple of the number of years of service used in the calculation

40. Table 2 shows the impact each year on employers of option d (change the formula) compared with option c (do nothing). The estimates are based on the impact of changes in the formula for redundancy payments.

2. Extra cost of awards under single multiplier system compared to existing system. £millions

	£280 limit	£300 limit	£310 limit	£320 limit
1 week	-£2.8m	-£1.8m	-£1.4m	-£1.0m
1.1 weeks	-£1.0m	£0.0m	£0.4m	£0.8m
1.5 weeks	£6.2m	£7.6m	£8.2m	£8.8m

Source: DTI estimate

41. These changes should be viewed in the context of the costs of awards in 2002/03 of £20.7million.¹³⁵ So while small changes to the formula will not have

¹³¹ This assumes that employers do not already have procedures in place for dealing with dismissal of older workers.

¹³² The number of hours was estimated in the RIA on dispute resolution and the cost of those hours calculated by multiplying the median wages of managers (Source: Annual Survey of Hours and Earnings 2004) by a factor of 1.3 (to take into account non-wage costs) and then by the number of hours.

¹³³ Similarly, the number of hours was estimated in the RIA on dispute resolution and the cost of those hours calculated by multiplying the median wages of all employees (Source: Annual Survey of Hours and Earnings 2004) by a factor of 1.3 (to take into account non-wage costs) and then by the number of hours.

¹³⁴ This is calculated as the cost of a claim (about £3,300) times the number of claims (640). This does not include any costs of awards should the applicant be successful.

much impact, a big change (limit of £320 and one and a half weeks pay per year of service) would have a much greater impact on the cost of awards.

42. Changes to the Statutory Redundancy Scheme will remove the lower age limit of 18 for qualifying service for redundancy payments (and thus basic awards for unfair dismissal). This will mean that employees with at least one year's service before 18, who currently do not qualify for 'basic award' compensation in the case of unfair dismissal, will do so in future. In theory this could increase the numbers of Employment Tribunal applications, although in practice the effect is likely to be negligible, since compensation sums would remain low for young workers who have relatively few years of service¹³⁶. This effect is not included in the costs calculations in this RIA.

Costs to the Exchequer

43. An increase in the number of tribunal claims will cost the Exchequer about £0.5 million each year.¹³⁷

Implementation costs

44. As discussed above, it is unlikely that these regulations will result in extra implementation costs to employers.

Equity and fairness

45. The changes to the legislation will mean that workers of different ages are treated more fairly if they are dismissed. Those aged 65 and over, who are paid less than other age groups, will be able to claim for compensation for the first time.¹³⁸ Furthermore, years of service at ages 16 to 21 will be dealt with equally compared with years of service at other ages. This will tend to benefit younger workers, who are often those whose labour market attachment is lowest.

Race equality impact assessment

46. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firms impact test

47. The legislation will affect all firms. Taking into account the number of employees working in small firms, they are more likely to have a claim made against them at an Employment Tribunal than other firms.¹³⁹ However, we do not have any evidence that small firms are more likely to have disputes. Small firms as a whole are also not likely to employ more workers aged 65 and over. This is not true of very

¹³⁵ Source: Employment Tribunal Service Annual Report and Accounts 2003/04. See <http://www.ets.gov.uk/annualreport2004.pdf>

¹³⁶ For example: an 18 year old with 2 year's service would receive a maximum basic award of (2 years' service) * (0.5 weeks pay / year's service) * (£280 pay limit per week) = £280, under the current redundancy system but with the lower age limit removed.

¹³⁷ The cost to the Exchequer of each tribunal claim (about £990) times the number of claims (530)

¹³⁸ Median hourly earnings of those aged 65 and over are £9.25. This is lower than every other age group apart from 16 to 22 year olds. Source: Annual Earnings of Hourly Earnings

¹³⁹ In 2003, 37 percent of claims were against organisations with 1 to 49 employees (Source: Survey of Employment Tribunal Applications), whilst 27 per cent of employees worked for these sized firms.

small firms who are slightly more likely to employ workers aged over 65 – and workers aged 16 to 17 years old.¹⁴⁰

48. The above evidence suggests that small firms as a whole are more likely to be affected by the changes to the legislation. However many individual firms are initially unlikely to be affected at all, as about 40 per cent do not employ any workers aged over 60.¹⁴¹

Competition assessment

49. We have applied the Competition Filter (see Annex) and have concluded that there will be minimal competition effects.

Enforcement, sanctions and monitoring

50. Enforcement mechanisms will not change with regard to the law on unfair dismissal. Employees will continue to be able to take a claim to an Employment Tribunal, should they think that they have been unfairly dismissed. Sanctions will change, depending on the formula used, as described above.

Implementation and delivery plan

51. Subject to parliament's approval the regulations will be in place by spring 2006, at least six months before they come into force in October 2006.

52. Good practice guidance will be available around the same time to help employers prepare. In addition to that, we are holding a conference in April 2006 to publicise the legislation.

53. Further details on the commencement date, awareness raising measures and guidance for employers and employees are available in the Summary Age Discrimination RIA.

Post implementation review

54. The Department will monitor the number of unfair dismissal applications by tracking administrative databases as well as repeating its periodic survey of Employment Tribunal claims. Case studies that look at the impact of the age legislation in general, should also alert us to any unintended consequences. A formal separate review is not planned, but any evidence on the way these regulations are working will be fed into the review on retirement ages, which will take a broad view of how the regulations are impacting on the labour market participation of older workers.

Summary and recommendation

55. The impact of this legislation on firms, employers and the Exchequer are summarised for each of the options in Table 3 below. For the sake of clarity, only the current weekly limit of £280 and a multiplier of 1.1 are used for option (d).

¹⁴⁰ 2.9 per cent of employees in workplaces with 1-10 employees who do not belong to a larger organisation are 65 and over. This compares to 2.6 per cent of employees being 65 and over for all workplaces.

¹⁴¹ Source: Department of Work and Pensions (2001) *Evaluation of the Code of Practice on Age Diversity in Employment*

3. Summary of costs and benefits

	Benefits	Costs
Firms		
Option a - Keep upper age limit	None	None
Option b - Removing upper age limit	May encourage workers to stay in workforce	£2.4-2.8m each year
Option c - no change to calculation of awards	None	None
Option d - change calculation of awards	£1.0m	
Individuals		
Option a - Keep upper age limit	None	Employees aged 65 or older still cannot claim unfair dismissal
Option b - Removing upper age limit	Greater fairness and may encourage older workers to stay in workforce, although there is a risk that employers might be reluctant to keep on those 65 and over	None
Option c - no change to calculation of awards	None	None
Option d - change calculation of awards		£1.0m
Exchequer		
Option b - removing upper age limit		£0.5m

56. We recommend options b and c, as these options best meet the Government's policy objectives. The formula chosen for option c mirrors that used for the calculation for statutory redundancy payments.

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

**Gerry Sutcliffe
Parliamentary Under-Secretary of State
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Competition Filter

Competition Filter	
Question	Answer
1. In the market(s) affected by the new regulation, does any firm have more than 10% market share?	No
2. In the market(s) affected by the new regulation, does any firm have more than 20% market share?	No
3. In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	No
4. Would the costs of the regulation affect some firms substantially more than others?	No
5. Is the regulation likely to affect the market structure, changing the number or size of firms?	No
6. Would the regulation lead to higher set-up costs for new or potential firms that existing firms do not have to meet?	No
7. Would the regulation lead to higher ongoing costs for new or potential firms that existing firms do not have to meet?	No
8. Is the sector characterised by rapid technological change?	Not relevant
9. Would the regulation restrict the ability of firms to choose the price, quality, range or location of their products?	No

Occupational pensions

November 2005

<http://www.dti.gov.uk/er>

Purpose and intended effect of measure

Objective

1. Occupational pension schemes contain a great many age-based rules necessary for their effective operation and management. In the context of age discrimination legislation our aim is to ensure that employers are not discouraged from maintaining occupational pensions for their employees. We will do this by allowing employers and trustees, as far as possible, to maintain existing age-based rules.

Background

2. The European Employment Directive (Council Directive 2000/78/EC) covers occupational pension schemes¹⁴², and allows Member States to exempt certain aspects of occupational pensions from age legislation:

- **The fixing of ages for admission or entitlement to occupational pensions, including the fixing of different ages for employees or groups or categories of employees; and**
- **The use of age criteria in actuarial calculations.**

3. In addition, the Directive allows for provisions of occupational pensions to remain lawful if they are justified by a legitimate aim, such as a legitimate objective of employment policy.

Rationale for government intervention

4. In *Age Matters*, our previous consultation in 2003, we noted our intention to take advantage of the provisions in the Directive that allow occupational pension schemes to set ages for admission or entitlement to retirement benefits.

5. Employers who wish to maintain occupational pensions are already under many competing pressures and face some difficult decisions in how they run their pension schemes in the future. Since many rules in schemes are necessarily age-based, there is the potential for age legislation to jeopardise the provision of occupational pensions if employers or trustees decide to close or level down schemes rather than face legal challenges, even unsuccessful ones.

¹⁴² Personal pensions (i.e., pension plans other than those offered by the employer) are not covered, with the exception of any payments into such pensions by the employer. The Directive does not cover state pensions. The Age Regulations will not affect them.

6. The approach the Government has taken in respect of the default retirement age is underpinned in part by the aim of avoiding undermining the provision of occupational pensions.

7. If we did not address this in implementing legislation and provide as far as possible for rules to be exempt or objectively justified, employers might decide to close pension schemes rather than risk future legal challenges. The Government has identified many different age-based rules that are used by schemes, though there could be more that we are unaware of.

8. Examples of these rules are: minimum or maximum ages for admission to a pension scheme and setting the amount of pension by reference to years of service.

Consultation

9. The Department has taken a progressively consultative approach on how to implement age discrimination legislation in Great Britain. The first formal consultation in 2001¹⁴³ covered all the new equality strands. On age it sought to find out what age-based practices were used by employers, why they used them, whether they wanted to keep them and why. At the end of 2002 the Department launched a second consultation¹⁴⁴ that focused mainly on strands other than age, as well as the general approach to discrimination legislation. In 2003 the Department launched its third consultation¹⁴⁵, which asked for views on proposals for outlawing age discrimination in employment and vocational training, including options for retirement ages. A final consultation on the draft regulations was held in mid 2005.¹⁴⁶

10. As well as informal consultation, the Department has had a strategy of continuing engagement with main stakeholders both informally, and formally, with the Age Advisory Group that is chaired by the Minister. We have sought views on policy options, as well as drawing on stakeholders' expertise to inform ourselves better about employment practices.

11. Almost all respondents supported the Government's approach to occupational pensions. The regulations allow occupational pension schemes in general to work as they do now by effectively exempting most age-related rules and practices.

12. We had a large number of enquiries early on in the consultation from pensions lawyers anxious to advise their clients. A major concern was the uncertainty about whether personal pensions, including stakeholder pensions, were covered. As a result we have included an exemption for employer contributions to personal pension schemes, but otherwise such schemes will not be caught by the regulations.

13. In consultation with a range of clients (private sector law firms and interested Departments), it became apparent that the scope of various exemptions was too wide, entitling employers and trustees of pension schemes to continue rules which were indefensible under the Directive. The scope of such exemptions where we considered that a "blanket" exemption was not likely to satisfy the proportionality test under Article 6.1 have been narrowed. As a result, we have for example tightened up an exemption to allow different contribution rates to DC schemes for members of different ages, so long as the rates increase with the age of the members.

¹⁴³ Towards Equality and Diversity: Implementing the Employment and Race Directive.

¹⁴⁴ Equality and Diversity: The way ahead.

¹⁴⁵ Equality and Diversity: Age matters.

¹⁴⁶ Equality and Diversity: Coming of Age.

14. Other exemptions have been deleted because we concluded that the exemption dealt with a practice that did not constitute discrimination at all, and therefore did not need an exemption.

15. There are one or two age rules that we do not think can be given a blanket exemption under either Article 6.1 or 6.2 – for example setting an upper age limit on paying contributions to a scheme. Some employers will not necessarily welcome this. The overall objective, nevertheless, is to ensure that exemptions are provided in good faith and serve a purpose to continue to survive.

Options

16. The alternatives in implementing the legislation are:

- (a) Do nothing. This would in effect mean employers/scheme trustees relying on a general provision for aged-based policies to be objectively justified;
- (b) Provide that certain rules do not constitute unlawful age discrimination;
- (c) In addition to (b), provide that other rules, which are always objectively justified, are not unlawful. For the purposes of this paper we refer to this approach as exempting age rules.

17. Employers having to objectively justify all or many age-based rules in occupational pension schemes (options a and b), could result in considerable costs (through deciding on whether each age-based rule was objectively justified) and uncertainty for employers, as the only way to test if those rules complied with the age legislation would be through the Employment Tribunal system, and claims could arise many years into the future. There is considerable danger, therefore, that employers would be tempted to withdraw pension benefits rather than go through this process. This would result in the Government not achieving its objective.

18. The Directive's provisions that allow for rules not to count as unlawful age discrimination, or to be objectively justified (and effectively exempted) will, in the context of age discrimination legislation, provide for the maximum certainty in the running of occupational pension schemes. This is because employers will be left to look through and decide if they have any other rules that need consideration. It is only those other rules that employers would have to objectively justify or change. This will keep costs down compared with an alternative of making employers go through the process for all rules.

19. The proposed approach is, therefore, option c.

Costs and benefits

Business sectors affected

20. Table 1 gives a breakdown of the proportion of occupational schemes by industrial sector.¹⁴⁷ As most occupational pension schemes are concentrated in large firms, it is perhaps unsurprising to see a large proportion in both retail/distribution/hotels and catering and manufacturing.

¹⁴⁷ These figures relate only to the private sector.

1. Industrial breakdown of occupational schemes

	All (%)	Closed schemes ¹⁴⁸ (%)
Agriculture/hunting/forestry and fishing	*	*
Manufacturing	19	20
Construction	7	8
Retail/distribution/hotels and catering	47	49
Transport and Communications	1	2
Banking, finance and business services	13	12
Public administration, education and health	8	3
Other Services	5	7

Source: Employers Pension Provision Survey 2003 (www.dwp.gov.uk/asd)

Costs and benefits to individuals

21. The proposed approach avoids the disincentive effect that failing to secure age-based rules would have. About 52 per cent of employees are covered by occupational schemes. The average employer contribution is seven per cent of payroll costs. Clearly any reduction in benefits could result in a substantial loss to employees.¹⁴⁹

Implementation costs to firms

22. Employers will need to go through all their age-based rules and consider whether they are allowable (either because they are exempt from the regulations or because they are objectively justified) or whether they need to consider keeping them and justifying them objectively themselves.

23. This could require the input of actuaries and legal advisers, as well as senior Directors of firms and the trustees of pension funds.

24. Currently about seven per cent of employers provide occupational pensions for their employees. While few smaller enterprises offer these schemes, around 85 per cent of very large firms (with over 1000 employees) do so. Table 2 gives a breakdown of firms that have occupational pensions schemes. It should be noted that many firms do not provide occupational pensions for all their employees¹⁵⁰, and some employers run several schemes.¹⁵¹

¹⁴⁸ A closed scheme is a scheme that is closed to new beneficiaries or employees

¹⁴⁹ Source: Department for Work and Pensions *Employers' Pension Provision Survey 2003* Research Report No 207

¹⁵⁰ Only 21 per cent provide an occupational pension for 76 to 100 per cent of their employees (Source: *Employers' Pension Provision Survey 2003*)

¹⁵¹ 71 per cent of employers who provide a scheme only provide one (Source: *Employers' Pension Provision Survey 2003*)

2. Firms with occupational pension schemes

Number of employees	Per cent	Numbers
1-4	3	23,500
5-19	9	28,800
20-49	13	7,500
50-99	30	5,200
100-499	32	4,600
500-999	65	1,400
1000 and over	85	1,900
Total	6	72,800

Source: Employers' Pension Provision Survey 2003 and Small Business Service, SME Statistics 2003. Numbers may not add due to rounding

25. Companies would need some time to discuss the changes required to pension schemes, and would need to seek professional advice, maybe from the firms that run their pension schemes or from independent advisors. Either way this will come at a cost.

26. The following tables outline the assumptions about the time needed and the costs involved. Small firms (up to 49 employees) are likely to need less time than large firms. This is because there may be economies of scale in the advice given; those advising small firms may well be advising others with the same or similar rules.¹⁵² Table 3 outlines possible costs for small firms.

3. Cost of making a decision about changes to pension scheme for small firms

	Time (days)	Cost per day (£)	Total Cost (£)
Managers	1	190	190
Actuaries	0.25	350	90
Accountants	0.25	280	70
All			340

Sources for costs per day are the Annual Survey of Hourly Earnings 2004. We have multiplied these figures by 1.3 (for managers) and 2 (for actuaries and accountants) to take into account non-wage costs.

27. Larger firms are more likely to provide occupational pensions with bespoke rules. Each one will have to be looked at individually in detail before any decision can be made about what changes are needed. And a wider number of managers would be involved. Table 4 outlines possible costs for medium and large firms.

4. Cost of making a decision about changes to pension scheme for medium and large firms

	Time (days)	Cost per day (£)	Total Cost (£)
Corporate managers	3.5 ¹⁵³	200	690
Actuaries	2	350	690
Accountants	2	280	560
Employee representative	1	105	105
All			2,000

Sources for costs per day are the Annual Survey of Hourly Earnings 2004. We have multiplied these figures by 1.3 (for managers and employee representatives) and 2 (for actuaries and accountants) to take into account non-wage costs.

¹⁵² We have assumed that occupational pensions offered by small firms would be pooled with other small schemes and managed by the same administrator and set of trustees.

¹⁵³ This assumes that the managing director spends half a day, finance director 2 days and the personnel manager 1 day. This would include meeting time.

28. The total costs to all firms are shown in Table 5.

5. Cost of making a decision about changes to pension scheme for all firms

	Cost per firm (£)	Number of firms	Costs for all firms (£m)
Small firms	340	59,700	21
Medium and large firms	2,000	13,100	27
Total		72,800	47

Sources for costs per day are the Annual Survey of Hourly Earnings 2004. We have multiplied these figures by 1.3 (for managers and employee representatives) and 2 (for actuaries and accountants) to take into account non-wage costs.

29. Trustees who run occupational pension schemes will need to become aware of the changes and would need to consider their obligations. In August 2003 there were about 230,000 trustees of occupational pension schemes. If each trustee takes one hour in a meeting to consider their obligations, then this would cost about £3.6 million.¹⁵⁴

30. The total implementation costs are therefore about £51 million. These are likely to be incurred either shortly after or shortly before the legislation is implemented.

Policy costs to employers

31. The overall aim is to ensure that, as far as possible, the rules of occupational pensions remain unchanged. Where change does occur - because employers do not think that they can objectively justify existing rules - it is unclear whether this will result in a cost or benefit to employers.

32. Some consultation responses noted that employers would face increased costs where they have to make pension contributions for workers who would currently be over retirement age and therefore not covered by occupational pension schemes. Due to uncertainties about how many older workers will continue to make pension contributions beyond their current retirement age we have not attempted to quantify this cost. Some employees will already have reached the maximum length of service for pension contributions before reaching retirement age, while others will choose to continue working while simultaneously drawing a pension (and thus not make further pension contributions).

Costs to the Exchequer

33. The Exchequer may incur costs through an increase in Employment Tribunal cases. The average cost of a case to the Exchequer is estimated to be about £990. We do not attempt to quantify the impact of any increase due solely to this strand of the legislation. An overall figure for all the age discrimination legislation is calculated in the summary.

Equity and fairness

34. The aim of the legislation is to make unjustified age discrimination unlawful whilst retaining the provision of occupational pensions, through ensuring that existing rules are still lawful under age discrimination legislation, where the Directive allows this. Therefore, on the whole, we do not expect an impact on equity or fairness.

¹⁵⁴ The average wages of employees is about £12 per hour (Source: Annual Survey of Hours and Earnings 2004). The total cost for all trustees is therefore £12 x 1.3 (to take into account non-wage costs) x 230,000

Where there are changes, particularly if they involve removal of provisions that are not objectively justified, they might result in some increase in fairness.

Race equality impact assessment

35. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firm impact test

36. Small firms are less likely to provide an occupational pension scheme to their employees (see Table 2) and if they do they are likely to be able to take advantage of economies of scale (as explained earlier) in dealing with the new legislation.

Competition assessment

37. We have applied the Competition Filter (see Annex) and have concluded that these regulations are unlikely to have any impact on competition.

Enforcement, sanctions and monitoring

38. Employees will be able to make a claim to an Employment Tribunal where they feel that the rules of their occupational pension scheme are unlawful. We envisage that there will be claims of this nature. Some may be related to issues of the retirement age of the firm. The average cost to employers of a tribunal claim where discrimination is the main jurisdiction is about £4,400.¹⁵⁵ We have assessed the total cost of tribunal claims for all aspects of age discrimination in the summary RIA.

Implementation and delivery plan

39. Subject to parliament's approval the regulations will be in place by March 2006, at least six months before they come into force in October 2006.

40. Good practice guidance and detailed pensions guidance will be available around the same time to help employers prepare. In addition to that, we are holding a conference in April to widely publicise the legislation.

41. Further details on the commencement date, transitional arrangements, awareness raising measures and guidance for employers and employees are available in the Summary Age Discrimination RIA.

Post-implementation review

42. The Government will monitor surveys such as the Employers' Pension Provision Survey, to look at the extent of provision of occupational pensions. However, case studies are more likely to be able to assess the impact of the legislation.

Summary and recommendation

43. In implementing the legislation the Government's aim has been to combat unfair age discrimination and to encourage the continuing provision of occupational pensions schemes. To achieve this objective the Government proposes to provide that as many rules as possible are not unlawful under the Regulations. The effect will be that most age-related provisions in pensions schemes will remain lawful. So this will

¹⁵⁵ This is an estimate based on the results of the Survey of Employment Tribunal Applications 2003. This number represents the median cost. The mean cost is estimated to be about £4,900.

leave employers to look through and decide if they have any other rules that need consideration. It is only those other rules that employers would have to objectively justify or change. This will keep costs down compared with an alternative of making employers go through the process for all rules.

44. The implementation costs to employers will come to about £51 million. There will be some costs for employers and the Exchequer arising from Employment Tribunal claims. Employees should benefit from the maintained provision of their occupational pensions.

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

**Gerry Sutcliffe
Parliamentary Under-Secretary of State
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Competition Filter

Competition Filter	
Question	Answer
1. In the market(s) affected by the new regulation, does any firm have more than 10% market share?	No
2. In the market(s) affected by the new regulation, does any firm have more than 20% market share?	No
3. In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	No
4. Would the costs of the regulation affect some firms substantially more than others?	No
5. Is the regulation likely to affect the market structure, changing the number or size of firms?	No
6. Would the regulation lead to higher set-up costs for new or potential firms that existing firms do not have to meet?	No
7. Would the regulation lead to higher ongoing costs for new or potential firms that existing firms do not have to meet?	No
8. Is the sector characterised by rapid technological change?	Not relevant
9. Would the regulation restrict the ability of firms to choose the price, quality, range or location of their products?	No

Recruitment, training and promotion

November 2005

<http://www.dti.gov.uk/er>

Purpose and intended effect of measure

Objective

1. The aim of the legislation is to maximise the participation and economic (and social) contribution of groups that are currently subject to discriminatory practices in the labour market because of their age. At the same time the Government recognises that there are exceptional circumstances when some age-based practices are capable of being objectively justified, and the Directive allows this. In implementing the legislation, the Government will, therefore, aim to improve opportunities and choice for individuals, and encourage labour market participation, whilst still allowing employers to manage their business effectively.

Background

2. The legislation will cover all practices in employment and vocational training that amount to age discrimination, including recruitment, employment based training and promotion. This could potentially affect individuals of all ages but evidence suggests that those affected tend to be older workers (about 50 years or over) and young workers (up to about 25 years). Even when older workers are in the labour market they may be denied training and promotion opportunities. It is also aimed at benefiting job seekers who face discrimination entering the labour market. The legislation will, therefore, increase the participation of older and younger workers in the economy, while at the same time enabling employers to draw on a wider pool of workers.

3. This Regulatory Impact Assessment considers the impact of the regulations on recruitment, training and promotion. It also considers the impact of allowing employers to objectively justify some age-based practices in these areas. A more general discussion of objective justification is included in the summary RIA of all the strands of age discrimination legislation.

Rationale for government intervention

4. Discrimination results in poorer quality matches in labour markets, which leads to lower national output¹⁵⁶. The evaluation of the Code of Practice and other studies find

¹⁵⁶ Mankiw (1997) defines discrimination as 'the offering of different opportunities to similar individuals who differ by colour of skin, ethnicity, gender, age or other characteristics.' For an introduction to the economics of discrimination in labour markets, including a discussion of the theory

direct evidence of age discrimination in employment¹⁵⁷. Older workers may find it difficult to re-enter the labour market after a period of absence because of negative stereotypes, even though they are still productive. Young workers may also find it difficult to enter the labour market for the first time. The risk that exists currently is that these people are not participating fully in the workforce and so human resources are wasted. Age discrimination is consistent with the lower employment rates for younger and older workers (see Table 1), as well as the higher incidence of inactivity and long-term unemployment for the latter group. These patterns persist over the economic cycle. However, they are not just due to discrimination.

1. Economic activity rates by age and sex

Age	Men	Women
18-24	78.7%	69.7%
25-34	92.0%	75.2%
35-49	91.6%	77.9%
50-64(M); 50-59(W)	75.0%	69.1%
65+(M); 60+(W)	8.8%	9.8%

Source: Labour Force Survey estimates for Autumn 2004

5. Other discriminatory practices in recruitment, training or promotion could reduce productivity because of the resulting ineffective matching of talent, aptitude and abilities to these advancement opportunities. Employers will also have a smaller pool of workers to draw on and will either not be making the most of the existing potential skills base of the workforce or will be losing valuable skills.

Consultation

Within government

6. These proposals have been developed in consultation with various interested Departments including the Department for Work and Pensions, the Department for Education and Skills, HM Treasury, HM Revenue and Customs, Cabinet Office and the Small Business Service.

Public consultation

7. The draft regulations contained a non-exhaustive list of examples of legitimate aims which could justify discrimination. These were copied from the Directive and were intended to give employers and tribunals a helpful pointer. However, they were widely felt to be unhelpful. Some consultees (mainly unions) were disappointed that we were not proposing to provide an exhaustive list, while others (mainly age interest groups) felt it was inappropriate to provide such a list in the Regulations at all. In the light of these responses we have moved the list from the Regulations into guidance.

of discrimination, its impact on the economy and why it can persist in a competitive market, see chapter 14 of 'Economics of Work and Pay' (1996), Filer, R, Hamermesh, D, and Rees, A.

¹⁵⁷“Code of practice on Age Diversity in Employment and Age Diversity in Employment Guidance and Case Studies (DfEE 1999)”. Casey, B and Wood, S (1994), “Great Britain: firm policy, state policy and the employment of older workers.” Hayward, B, Taylor, S, Smith and Davies G (1997), “Evaluation of the campaign for older workers”, London, The stationary Office.

Options

8. The following options were considered:

- a. Implement the Directive by outlawing discrimination on the basis of age, without providing for employers, exceptionally, to objectively justify age-based practices in recruitment, training and promotion.
- b. Implement the Directive by outlawing discrimination on the basis of age, and allow employers to objectively justify age discrimination in certain circumstances in recruitment, selection and promotion.

9. Implementing the Directive and not providing for employers to be able to objectively justify essential age-based practices if necessary in certain circumstances, risks forcing decisions that are clearly not economically efficient. For instance, the Directive itself recognises that circumstances might justify the fixing of a maximum age for recruitment based on the need for a reasonable period of employment before retirement. The risk is, therefore, that employers would incur the same costs as for option b, whilst realising lower benefits. It may also result in more subtle forms of discrimination that are not so easily detected.

10. Implementing the Directive and allowing employers to objectively justify age discrimination in certain circumstances, will mean that employers may sometimes treat workers differently on the basis of age. We are of the view that because of the requirement to justify this objectively, if challenged, only essential practices will be retained where they are appropriate and necessary. Instances of age discrimination will, therefore, be reduced. Consultation with employer organisations shows broad support for this approach, although some have pointed to the potential for more uncertainty in determining what is lawful. The DTI recognises the important role that guidance will have in helping employers to understand the process of objective justification, and in helping employees to understand their rights.

11. Given that option a is highly likely to result in lower net benefits than option b, the costs and benefits section that follows considers the latter only.

Costs and benefits

Business sectors affected

12. Table 2 shows the distribution of different aged workers by industrial sector. Those sectors that employ a higher proportion of older or younger workers will be disproportionately affected by the legislation. Those sectors that employ proportionately more young workers are: distribution, hotels and restaurants, and other services. The spread of older employees appears quite evenly distributed.

2. Percentage of employees of different age groups by industry sector

	16-24 years	50 years and over	16-24 and 50 years and over
Agriculture and fishing	18	22	39
Energy and Water	10	26	36
Manufacturing	10	26	36
Construction	17	25	42
Distribution, hotels and restaurants	32	20	51
Transport and Communication	11	24	35
Banking, finance and insurance	14	19	33
Public administration, education and health	8	28	36
Other services	24	25	49
All	16	24	40

Source: National Statistics (www.statistics.gov.uk) Labour Force Survey Spring 2004

Assumptions

13. We assume only people in work could have faced age discrimination in terms of promotion and training practices, whereas a wider group of individuals could face age discrimination in terms of recruitment. In this RIA we focus mainly on those who are economically active.

14. Although there are no age limits in the proposed regulations, to assess the potential extent of age discrimination in the workplace and the coverage of legislation we consider two specific age groups in Great Britain: those aged **16-24**, and those aged **50 and above**. Table 3 shows the number of economically active people and the number of employees in these two age groups.

3. Numbers of economically active and employees

Age	Economically active (thousands)	Employees (thousands)
16-24	4,723	3,763
50 and over	7,786	5,830
16-24 and 50 and over	12,509	9,593
All	29,821	24,215

Source: National Statistics (www.statistics.gov.uk) Labour Force Survey Spring 2004

15. Assessing how discrimination has affected individuals is difficult. Information on employers' policies gives us an idea of the potential for individuals being adversely affected. If some employers have recruitment policies that explicitly take age into account this could, potentially, result in some age groups not being successful in job applications. It is hard to say to what extent this would apply for two reasons. First, the job applicant may have other qualities that are more important to the employers and, second, there may be a difference between policy and practice within an organisation.¹⁵⁸ On the other hand, individuals' perceptions can be just as

¹⁵⁸ This was something that was pointed out in Evaluation of Code of Practice.

misleading. An individual may not be aware that they are being discriminated against and if they do suspect that this is the case, they cannot be sure, nor can they assess, how much it has affected them.

16. In the sections that follow we make assumptions about the extent of discrimination based on surveys of both employers and individuals to come up with a range of possible effects.

Awareness costs to business of the legislation

17. Compared to other recent legislation which deals with equality at work and which has been introduced as a result of the Directive (for instance in relation to religion, sexual orientation, disability), there are additional considerations for companies getting to grips with the age legislation. In particular:

- What would otherwise be direct age discrimination can in some cases be ‘objectively justified’;
- It may reflect many ingrained day-to-day practices, through conscious prejudice or the unintended by-products of actions; and
- It is not covered by existing legislation;

18. We assume that a manager in every small business spends an average of one hour reading and understanding the implications of the legislation, rising to two hours for medium and large firms.

19. The Directive allows for direct age discrimination to be objectively justified. Businesses will, therefore, need to consider the extent to which they make use, if at all, of the objective justifications. These awareness costs will also be incurred by those who decide to take a completely non-ageist approach. We assume that, for smaller firms, it takes a shorter number of hours to become familiar with the legislation, as fewer in the organisation would be involved in this process.

20. We assume Acas¹⁵⁹ will take on a dissemination role, though large firms may also need more specialised legal advice to understand what is and what is not permissible under the Directive. Because of the complex and new issues involved, further consideration could take a further one hour for small firms (giving a total of **two hours**).¹⁶⁰ Medium to large employers may also need to produce and disseminate guidance for personnel departments and this could take anything up to five hours (giving a total of **seven hours**). These figures are likely to vary considerably from firm to firm depending on the structure of the organisation and current practice.

21. The corresponding costs to business of the time taken in becoming aware of the legislation and further consideration are outlined in Table 5.

¹⁵⁹ Advisory, Conciliation and Arbitration Service.

¹⁶⁰ A one hour average for further consideration for small firms to consider the implications of the legislation is lower than the estimated five hours for medium and large firms. However, very small firms (those, say, with one to nine employees) may find it considerably quicker to consider practices that are largely based on informal agreements, even if these need to be revised. Firms with one to nine employees make up a significant majority (86 per cent) of all small firms in the UK (Source: Small Business Service).

5. Cost to employers of understanding the legislation concerning training, promotion and recruitment

Period	Occupation of those reading and understanding the guidance	Average hourly cost	Average time taken to understand legislation	Cost per firm	Number of firms	Total costs
Small firms	Manager/administrator	£25	2 hours	£50	1,160,000	£58m
Medium and large firms	Personnel manager	£28	7 hours	£196	35,900	£7m
All firms						£65m

Sources: Annual Survey of Hours and Earning 2004 and Small Business Service statistics for 2004. A small firm is defined as one having 1 to 49 employees.

Benefits to business in changes in recruitment practice

22. The main benefits to employers will be an increased pool of potential applicants from a greater supply of older and younger individuals previously subject to discrimination - as well as increased mobility of these individuals. Although this pool *already* exists, it will be *untapped* to the extent that some companies simply ignore applications from these workers or these individuals may decide not to apply for vacancies (and, for example, choose to be inactive rather than actively looking for work). In both cases it is because of perceptions or subtle forms of age discrimination or stereotypes in the recruitment process.

23. The Evaluation of the Code of Practice reported that between 13 and 26 per cent of employers had some form of age consideration in either their job advertisements or in their selection process.¹⁶¹ On the other hand between 12 and 16 per cent of older workers said that they had experienced discrimination either in getting a new job or in obtaining a job interview. We therefore assume that between 12 and 26 per cent of instances (where employers are trying to fill vacancies) result in some form of discrimination on the basis of age that will affect individuals aged 50 and individuals aged 16 to 24.

24. Around 2.3 million to 3.0 million job vacancies may be advertised in the GB each year.¹⁶² The 2003 DFES Employers Skill Survey estimated 'hard to fill vacancies' were around 40% of all unfilled vacancies. Therefore in about 110,000 to 310,000 of hard to fill vacancies employers had used some form of age consideration.¹⁶³ Costs to the employers of recruiting staff are around £2,500 per head (not including training).¹⁶⁴

25. If 12 to 26 per cent of older and younger workers are being discriminated against, this represents 5 to 11 per cent of the economically active (those employed and unemployed) who are looking for a job. The legislation, therefore, has the potential to increase the pool of potential applicants by this percentage, resulting in an equivalent

¹⁶¹ 26% if the 13% in the job advertisement and the 13% in the selection process are not overlapping.

¹⁶² The 2004 CIPD Recruitment Retention and Turnover Survey found that labour turnover was 16.1 per cent (or 3.9 million employees). If 75 per cent of vacancies are advertised, this is equivalent to about 3 million advertised vacancies. Evidence from the Labour Force Survey shows that employee tenure is on average 7.5 years. This implies a turnover rate of about 13 per cent (or 3.1 million employees). Based on this estimate, the number of advertised vacancies would be 2.3 million.

¹⁶³ $2.3m \times 0.12 \times 0.4 = 110,000$ to $3m \times .26 \times .4 = 312,000$.

¹⁶⁴ Average of latest CIPD surveys.

drop in recruitment costs (because there is an increased chance of filling the vacancy satisfactorily) of between £130 and £270 per vacancy, bringing resulting benefits of between **£14 million and £85 million** each year.¹⁶⁵

26. The number of employers using age filters could fall in the future because of demographic changes independent of the legislation, and so this range should be seen as an upper bound on future benefits.

27. Employers may gain further from retaining skills and experience within their organisation, due to lower turnover rates of older workers. Some case study evidence suggests that replacing older workers can increase average turnover rates.¹⁶⁶ There could be some self-selection issues in these case studies with particularly motivated older individuals likely to be currently found in employment. Average recruitment costs for employers are around £4,200 per new worker. We do not attempt to quantify the resulting benefits of lower turnover given the difficulties of estimating demand-side responses over time, but note they could be an issue in wholesale and retail trades, hotels, restaurants and leisure sectors where turnover tends to be relatively high.¹⁶⁷

Costs to business of changes in recruitment practice

28. Employers will need to take greater care when advertising vacancies in order to avoid explicit or implicit differences of treatment, unless objectively justified. Legislation has had a marked impact on employer practice in the United States, Canada and Australia in this area¹⁶⁸, though experience from these other countries has limits. At a practical level the proposed regulations will mean thinking carefully whether phrases such as ‘young dynamic’ or ‘mature persons’ are justified in adverts. The proposed regulations will have a provision for justifying age restrictions and the guidance will help inform employers. This means that management decisions on recruitment will be under greater scrutiny and consequently businesses may need to invest in more formal job specifications - namely that they will have to identify skills and competences and wider advertising to minimise litigation risks.

29. Around 2.3 million to 3.0 million job vacancies in the GB are advertised each year. The Evaluation of the Code of Practice found that between 13 and 16 per cent of employers used either age limits or age ranges when advertising jobs. We therefore assume that about 300,000 to 480,000 advertisements would require attention from personnel staff to comply with the proposed regulations. We assume each of the 300,000 to 480,000 vacancies could take an additional quarter of an hour of a personnel officer’s time, leading to an annual cost of about **£2.1 million to £3.4**

¹⁶⁵ $110,000 \times £130 = £14,300,000$ to $312,000 \times £270 = £84,240,000$. With time there is likely to be a reduction in the numbers who are active but who do not have a job, as the economy expands. This will result in a modest reduction in the benefit, although firms will still benefit from having a bigger pool of applicants to choose from (drawn from employed and unemployed). We do not attempt to quantify this.

¹⁶⁶ ‘Age Works: A case study of B&Q’s use of older workers.’ Hogarth, T and Barth, M (1991). IER, University of Warwick.

¹⁶⁷ CIPD (1999) *ibid*.

¹⁶⁸ ‘Outlawing Age Discrimination: Foreign lessons, UK choices’ edited by Hornstein, Z, Joseph Rowntree Foundation, <http://www.jrf.org.uk/knowledge/findings/socialpolicy/711.asp>

million.¹⁶⁹ This extra attention could range from simply checking an advert to considering what other criteria to attract applicants with the appropriate skills could be used instead of age. These costs will decline in the future as companies become more aware of the legislation and its implications for them. This will be related to average job tenure rates in the labour market and so we assume that after five years the cost will be about £1 million to £1.7 million before tailing off to zero after ten years.

30. In addition, employers may also have to consider more applicants during the selection process, including more sifting and interviewing. It is difficult to quantify these effects because they will depend on the likely increase in applicant numbers and the need to consider more applicants will be offset by the more careful recruitment practices identified above. There will be a limit to the number of extra applications that companies will consider as there will come a point where firms simply prefer to face the risk of being taken to tribunal rather than spend additional time considering marginal applications. We therefore assume that the main cost will be additional sifting rather than carrying out more interviews of candidates. Assuming 280,000 to 780,000¹⁷⁰ vacancies each take an additional 15 minutes of a personnel officer's time in terms of additional sifting, this would lead to annual recurring costs of about **£1.9 million to £5.5 million.**¹⁷¹

31. Total costs to firms as a result of changes in their recruitment process would therefore be about **£4.0 million to £8.8 million** each year.

Net impact on firms from recruitment

32. The estimated benefits net of costs to employers as a result of changes to recruitment practices are therefore about **£9.9 million to £76 million each year.**

Impact on individuals from recruitment

33. Individuals will benefit from being treated more fairly in the recruitment process, which should potentially result in an increase in the employment rates of some age groups. The impact of this is considered further in the discussion of macroeconomic impacts in the overall RIA.

Promotion

34. Under the proposed legislation promotion decisions will need to be more transparent and untainted by unjustified ageism to avoid the risk of successful age discrimination claims.

35. The Evaluation of the Code of Practice on age diversity estimated that about five to six per cent of older workers feel they have not been promoted because of their age.¹⁷² 13 per cent of employers said that used age as a basis for identifying suitable promotion candidates. We therefore assume that between 5 and 13 per cent of older

¹⁶⁹ Average wages of personnel manager = £21.58 (Source: Annual Survey of Hours and Earnings 2004) Total cost: £21.58 x 1.3 (to take into account non-wage labour costs) x 0.25 x 300,000 to £21.58 x 1.3 x 0.25 x 480,000 = £2.1 to 3.4m.

¹⁷⁰ This is the estimate of the number of advertised vacancies that involved some form of discrimination or 2.3m to 3m (advertised vacancies) x 12% to 26% (percentage of recruitment practices that involved discrimination) = 276,000 to 780,000

¹⁷¹ 276,000 to 780,000 x £21.58 x 1.3 / 4 = £1.9m to £5.5m

¹⁷² Evaluation of the Code of Practice *ibid.*

workers are discriminated against when employers are considering who to promote. Given there are around 9.6 million older and younger employees, about 480,000 to 1.2 million employees could have been denied promotion because of their age.¹⁷³

Promotion benefits to employers

36. We quantify a small productivity boost for employers of between 0.1 per cent to 0.5 per cent of labour costs that is not transferred to workers. This amounts to an annual gain of between **£14 million to £180 million**¹⁷⁴ and arises because human resources - namely talent and abilities - are allocated more efficiently as age is no longer used in the promotion process. Again, this is an annual recurring benefit, which we would expect to gradually build up and reach a peak sometime in the first twenty years of legislation.

Promotion benefits to individuals

37. The higher wages paid to promoted individuals reflects their higher skills and productivity. We assume a wage premium of five per cent on promotion¹⁷⁵, and that 90 to 95 per cent of this is pure displacement – namely that other individuals would still have been promoted if discrimination in terms of age had been used. The recurring annual benefit to individuals would therefore be around **£27 million to £140 million**.¹⁷⁶

Training

38. Training is a key issue with respect to an individual's career, job satisfaction and general motivation. Evidence from the Labour Force Survey shows that older employees are less likely to train compared with younger workers. The LFS shows the proportion of employees who say they have received some training in the last thirteen weeks tails off from around 30 per cent to around 10 per cent between the ages of 50 and 65. This negative effect of age on training also holds when statistically controlling for standard economic variables.¹⁷⁷

39. The source of lower training levels among older workers has been debated in the academic literature.¹⁷⁸ Analysing human capital as an investment decision reveals the key incentives and trade-offs involved. In particular, the rate of return to training (and also education) tend to fall with age as the opportunity cost of the individual's time rises (i.e., as older workers generally earn higher pay than younger workers - though not compared to workers aged between 25 and 49 years) and with the declining length of working life (i.e., years to reap benefits falls with age).

¹⁷³ 9.593 million x 5% to 13% = 479,650 to 1,247,090.

¹⁷⁴ 479,667 to 1,247,134 (number of employees affected) x £22,248 x 1.3 (to take into account non-wage costs) x 0.1% to 0.5% (productivity effect) = £13.9 million to £180.4 million.

¹⁷⁵ Booth, Francesconi and Frank (2003) find that promotion leads to average wage increases of about 5% for men in "A Sticky Floors Model of Promotion, Pay and Gender", *European Economic Review* 47,2 pp 295 to 322.

¹⁷⁶ Average wage is about £22,248 per year. Source: Annual Survey of Hours and Earnings 2004. The benefit to employees is therefore £22,248 x 5 per cent (wage premium) x 479,667 to 1,247,134 (number of employees affected) x 5 to 10 per cent (to take into account displacement = £26.7 million to £138.7 million.

¹⁷⁷ Formally, there is a negative coefficient on the training. For a review of these issues see Meadows, P *ibid*

¹⁷⁸ See Taylor, P and Urwin, P "Age and Participation in Vocational Education and Training" *Work, Employment and Society* Volume 15 No 4 pp. 763-779

40. The Evaluation of the Code of Practice on age diversity reported that one to two per cent of firms said they used the age of candidate to decide who should be offered training opportunities; 41-42 per cent said that they used 'likely use of skills learned' to decide who should be offered training, confirming that the return to training is a key criterion for employers. However, the latter may also involve an element of age discrimination, so the one to two per cent may be an underestimate of the amount of policies that have the potential to discriminate on the basis of age.

41. Four to five per cent of older workers said that they had experienced age discrimination when being offered training and development. Because of the uncertainties of the results from employers, for the purposes of assessing the degree of discrimination on the basis of age in training, this RIA takes the results from the survey of workers and assumes that between four and five per cent of employees experience age discrimination when being selected for training. We also assume that only older workers are discriminated against on the basis of age in training.¹⁷⁹

42. Those extra workers, who are trained because of the age legislation, may displace others who would have been trained in the absence of legislation. This would be true if employers had fixed budgets for training rather than a budget allocation per person. It would, however, be logical for employers to train people as long as there is a reasonable return. We therefore assume that displacement will be between zero and 25 per cent.

43. The estimated number extra workers (on the basis of the above assumptions) receiving training is therefore between about 170,000 and 290,000 each year.¹⁸⁰

Training benefits and costs to business

44. The benefits to business are mainly improved productivity and motivation of the trained individual, along with lower turnover. Wage premiums are an indirect measure of this benefit, and there is a wealth of academic research in this area. This tends to put the associated wage premium at between 5-10% - though other research has put it as high as 13%.¹⁸¹ However the effect of training on industry productivity will also be key.¹⁸² The focus on wages as a relevant measure of productivity ignores the gains firms may capture through productivity and the cost associated with different forms of training. With this in mind, we assume a gross efficiency gain to employers of between one to five per cent, giving potential annual business benefits of between **£51 million** and **£420 million**.¹⁸³ Some gains will be shared with workers in the form of increased wages. There is likely to be a profile to these benefits, and

¹⁷⁹ This seems reasonable considering that 36 per cent of employees aged 16 to 24 say that they have undergone education or training in the last 3 months, compared with 32 per cent of employees aged 25 to 49 and 23 per cent aged 50 and over (Source: Labour Force Survey spring 2004)

¹⁸⁰ $5,830,415$ older employees \times 4 to 5 per cent (discriminated against) \times 0.75 to 1 (to take into account displacement) = 174,912 to 291,521

¹⁸¹ See for example papers by Blundell, R, Dearden, L and Meghir, C (1996), The Determinants of Work Related Training in Britain, London: Institute of Fiscal Studies. Booth, A (1991), 'Job-related formal training: who receives it and what is it worth?' Oxford Bulletin of Economics and Statistics, 53, pp.281-94.

¹⁸² Dearden, L, Reed, H and Van Reenen, J. (2000) "Who Gains When Workers Train" IFS working paper W00/04 <http://www.ifs.org.uk/wps/wp0004.pdf>

¹⁸³ $174,912$ to $291,521$ (individuals) \times 0.01 to 0.05 (premium on training) \times £22,248 \times 1.3 (to account for non-labour costs) = £50,588,878 to £421,573,987.

they are likely to build up and peak sometime during the first twenty years of the legislation.

45. Training is a costly investment, depending on the type of training and numbers trained. There have been several recent attempts to estimate the employer costs of job training provision.¹⁸⁴ We do not attempt to model these costs but instead note that firms will only train workers as long as they receive a reasonable rate of return, taking into account risk. We assume that any investment in training would require a rate of return of around 13%¹⁸⁵, which for the business benefits above implies annual training resource costs of **£44 to 370million**.¹⁸⁶

46. The net gain to employers will be about **£6.6 to £55 million** each year.

Training benefits to individuals

47. If we assume 10 per cent of the training premium is transferred to workers, they will benefit by **£5 to 42 million** annually.¹⁸⁷ This 10 per cent transfer represents an average transfer and will be higher for general training investments. Where training has a large firm-specific component and where mobility is limited, there may be productivity gains *not* passed on to workers but which are only reflected in the direct measures of productivity. The latter may be particularly important for older workers. We believe this will be a lower bound to benefits associated with additional training because workers will also gain from improved self-esteem and standing following training. Training could also help older workers to reduce the risks of long-term unemployment and bring other benefits such as increased cooperation from the workforce.¹⁸⁸

Benefits to the economy

48. Benefits to the economy will arise from increases in productivity due to firms using more efficient processes. This benefit is split between employers and individuals. There will also be net costs arising from understanding the legislation and from an increase in tribunal claims. The legislation may also result in workers of certain ages remaining more attached to the labour market, in more unemployed finding and keeping a job and even those who want a job but have given up looking becoming economically active.

49. Table 6 summarises the benefits to the economy quantified above. The impact of higher participation rates on the economy is analysed separately in an Annex of the

¹⁸⁴ The Continuing Vocational Training Survey (CVTS) was first carried out during 1994 in the then 12 EU member states (published in the UK as Employer Provided Training in the UK 1993, IFF Research, 1996). A second survey - CVTS2 was carried out in 2000/01, across 25 European states (the 15 EU members, Norway and 10 acceding countries). Information on training expenditure was also collected in the Learning and Training at Work 2000 (LTW 2000) survey and the Employers Skill Survey 2003.

¹⁸⁵ This is in line with the average rate of return for the private sector from 2000 to Q3 2004. Source: Office of National Statistics.

¹⁸⁶ $£50,588,878$ to $£421,573,987$ (value of premium on training) $\times (1 - 0.13) = £44,012,324$ to $£366,769,369$. This is equivalent to about £252 to £1,258 per extra worker trained and seems reasonable when compared with an estimate of training costs per employee (including the cost of staff time) of about £600, from the Employer Skill Survey 2003.

¹⁸⁷ $174,912$ to $291,521$ (individuals) $\times 0.01$ to 0.05 (premium on training) $\times £ 22,248 \times 1.3$ (to account for non-labour costs) $\times 0.1$ (transferred to workers) = $£5,058,888$ to $£42,157,399$.

¹⁸⁸ OECD Employment Outlook, 2004.

summary of all the RIAs. Because of the tentative nature of the analysis this has not been included below.

6. Impact on the economy

Legislation strand	£
First year	
Recruitment	£9.9-76m
promotion	£41-320m
training	£12-97m
Implementation costs	-£65m
Tribunals (see section on enforcement and sanctions)	-£28m
Total first year impact	-£30m - +£400m
NPV over ten years	£240-4,600m
Average annual NPV	£24-460m

NPV is the net present value of costs and benefits from year 1 to year 10 discounted at the Treasury discount rate of 3.5 per cent. The average annual NPV is the NPV over ten years divided by 10.

Equity and fairness

50. There is evidence that discrimination affects both older and younger workers. Both groups of people may be excluded from promotion and older workers may be excluded from training, because of their age. Discrimination can also affect all economically active individuals – broadly speaking those who are in work and those who are looking for work - to the extent that job seekers are discouraged from applying for jobs at the recruitment stage.

Race equality impact assessment

51. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firms impact test

52. Although the Age Positive Code of Practice has been in existence since 1999, the legislation will be new and will also require ‘step changes’ in attitudes. It will cover all firms and there is likely to be a significant effect on smaller firms. They will bear disproportionate implementation costs, which are expected to be relatively high, because of the complex nature of the subject. The cost per small firm is expected to be about £58. Small firms are also more likely to rely on informal methods, such as word of mouth and the use of informal contracts, and so may need to take more actions to comply with the proposed regulations. Very small firms (those employing fewer than 10 people) are also those that are more likely to employ workers over 65. They will be proportionally more likely to be taken to Employment Tribunal.

53. Like all companies, small firms will benefit from improvements in the functioning of the labour market. The total impact (including implementation costs) is estimated to be, on average, a benefit of about £26 million each year¹⁸⁹ – the range of estimates is between a loss of £6 million and a benefit of £59 million each year.

¹⁸⁹ This is the average net present value of costs and benefits over ten years.

54. Consultation so far has led to a mixed reaction from small firms, with some not concerned while others have raised business interests, which might need to justify some form of age discrimination. We have explored these issues further in a structured set of focus groups. For further details see the Small Firm Impact Test.

Competition assessment

55. The legislation on age discrimination is likely to lead to an increase in participation rates, as well as training and promotion opportunities for older and younger workers. This will enhance competition in the labour market, as age is no longer used as a criterion or filter in these key decisions. As a result, talent and ability will be better matched to recruitment and training decisions. Labour market competition will also increase from tapping a greater pool of applicants, increased training and improved promotion prospects.

56. The competition filter was applied. The results appear in the Annex. Small firms may be affected by the legislation because small firms will, as noted above, bear disproportionate implementation costs. This is, however, unlikely to affect the market structure. We identified no other significant effects on competition.

Enforcement, sanctions and monitoring

57. Experience of the current discrimination jurisdictions in Great Britain suggests there could be significant tribunal applications. Evidence of age discrimination in the United States also suggests there could be large numbers of cases, though comparisons with the US should be treated with caution. We assume an average of 8,000 Employment Tribunal (ET) applications per year from the Directive of which 75% might relate to recruitment, training and promotion. The average cost of an ET application where discrimination is the main jurisdiction is £4,900 and for the taxpayer £990.¹⁹⁰ Total employer's cost could therefore be about £29 million.¹⁹¹ We assume that these costs arise even when the employer is not at fault, which we assume to be 75 per cent of the time. The cost when the employer has complied with the legislation is £22 million each year. The Exchequer costs are about £6 million each year.

Implementation and delivery plan

58. Subject to parliament's approval the regulations will be in place by March 2006, at least six months before they come into force in October 2006.

59. Good practice guidance will be available around the same time to help employers prepare. In addition to that, we are holding a conference in April to publicise the legislation.

60. Further details on the commencement date, awareness raising measures and guidance for employers and employees are available in the Summary Age Discrimination RIA.

¹⁹⁰ See "Findings from the 1998 Survey of Employment Tribunal Applications" Employment Relations Research Series No 13, 2002

¹⁹¹ $8,000 \times 75\% \times £4,900 = £29m$

Post-implementation review

61. The DTI and DWP have jointly commissioned a series of baseline studies, which include a survey of employers' awareness, perceptions and practices on age discrimination in employment and a study of the age dimension of employers' recruitment and promotion decisions. The DTI has also commissioned a baseline study of official statistics, which has been published. This research will be repeated 2 to 4 years after the legislation is in place. The DTI will also consider commissioning some case study research which will look at the longer term impact on businesses.

Summary and recommendation

62. In implementing the legislation, the Government will aim to improve opportunities and choice for individuals, and encourage labour market participation, whilst still allowing employers to manage their business effectively.

63. The Government therefore proposes to allow employers to objectively justify age related policies in the area of recruitment, promotion and training. Not allowing objective justification could result in employers engaging in practices that would result in reduced benefits for firms and individuals. Consultation has shown broad support for this approach.

64. Table 7 summarises the quantifiable costs and benefits of the proposed option.

7. Summary of costs and benefits of age discrimination legislation

	Benefits Annual	Costs Annual	Costs One-off
Employers			
Implementation (Awareness and Decision Making)			£65 m
Enforcement		£22 m	
Recruitment	£14-85m	£4.0-8.8m ^a	
Training	£51-420m	£44-370m	
Promotion	£14-180m		
Individuals			
Training	£5-42m		
Promotion	£27-140m		
Exchequer			
Enforcement		£6m	
Economy	Net annual benefit of £24-460m (average NPV)		

Notes: a. This cost is annual but gradually declines to about £2.5-6m by 2011.

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

Gerry Sutcliffe

Parliamentary Under-Secretary of State

(Minister for Employment Relations and Consumer Affairs)

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Competition Filter

Competition Filter

Question	Answer
1. In the market(s) affected by the new regulation, does any firm have more than 10% market share?	No
2. In the market(s) affected by the new regulation, does any firm have more than 20% market share?	No
3. In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	No
4. Would the costs of the regulation affect some firms substantially more than others?	Yes
5. Is the regulation likely to affect the market structure, changing the number or size of firms?	No
6. Would the regulation lead to higher set-up costs for new or potential firms that existing firms do not have to meet?	No
7. Would the regulation lead to higher ongoing costs for new or potential firms that existing firms do not have to meet?	No
8. Is the sector characterised by rapid technological change?	Not relevant
9. Would the regulation restrict the ability of firms to choose the price, quality, range or location of their products?	No

Pay and non-pay benefits*

November 2005

<http://www.dti.gov.uk/er>

Purpose and intended effect of measure

Objective

1. The aim of these regulations is to ensure that where employers provide age-based or service-based pay and non-pay benefits to employees that are objectively justified on grounds such as social policy or incentivising staff, that they should continue to be able to do so without the imposition of unnecessary burdens.

Background

2. Pay and non-pay benefits cover benefits an employee receives under a contract of employment, many of which will not be discriminatory for the purposes of age legislation. Article 6.1 of the European Employment Directive (Council Directive 2000/78/EC) provides that differences of treatment on the grounds of age will not be unlawful if "objectively and reasonably justified by a legitimate aim and the means of achieving that aim are appropriate and necessary". However, some pay structures or benefits may result in direct or indirect age discrimination.

Rationale for government intervention

3. In some cases benefits are likely to be potentially indirectly discriminatory, because they require a certain period of service before the benefit is available. There are also examples of directly discriminatory benefits, such as age-based pay structures or the removal of medical or life insurance after a certain age.

4. Recent evidence¹⁹² found that last year 20% of respondents (who were employers and HR managers) used length of service in determining pay. This was less common in the case of senior managers¹⁹³. Other evidence has pointed to this being more typically found in the public and not-for-profit sectors.¹⁹⁴

* Pay and non-pay benefits are referred to as service-related benefits in the consultation document.

¹⁹² *Reward Management Survey*, Chartered Institute of Personnel and Development, February 2004.

¹⁹³ Less than 10% of senior managers had their pay partly determined by length of service.

¹⁹⁴ Booth and Frank, J (1994), *Coverage by incremental scales*, Centre for Economic Policy Research, discussion paper No. 1097. IDS Studies (2003) *Clerical and secretarial pay* Report 757

5. There is also evidence of employers providing other benefits such as medical insurance, holiday entitlement, help with childcare costs and share schemes, whose entitlement depend on length of service.¹⁹⁵
6. Consultation has also shown that service- or age-related pay and non-pay benefits are commonly used by employers to reward experience and loyalty, and to provide incentives for staff. The majority of employers and employees accept and welcome the use of these types of benefits, and in implementing this legislation, we do not want to stifle business with unnecessary burdens.
7. On the other hand, not all service-related benefits are uniformly welcomed, with some concerned about the potential for sex discrimination.¹⁹⁶

Consultation

8. The Department has taken a progressively consultative approach on how to implement age discrimination legislation in Great Britain. The first formal consultation in 2001¹⁹⁷ covered all the new equality strands. On age it sought to find out what age-based practices were used by employers, why they used them, whether they wanted to keep them and why. At the end of 2002 the Department launched a second consultation¹⁹⁸ that focused mainly on strands other than age, as well as the general approach to discrimination legislation. In 2003 the Department launched its third consultation¹⁹⁹, which asked for views on proposals for outlawing age discrimination in employment and vocational training, including options for retirement ages. A final consultation on the draft regulations was held in mid 2005.²⁰⁰
9. As well as informal consultation, the Department has had a strategy of continuing engagement with main stakeholders both informally, and formally, with the Age Advisory Group that is chaired by the Minister. We have sought views on policy options, as well as drawing on stakeholders' expertise to inform ourselves better about employment practices.
10. In the *Age Matters* consultation in 2003, we proposed to make specific provision for employers to be able to justify pay and non-pay benefits. However, one of the key messages that came out of that consultation was a significant concern that we had not fully considered the impact the Directive would have on employers, who would effectively have to justify retaining every benefit they provided on an individual basis.
11. Benefits dependent on up to five years' service are exempt from the Regulations, as are those which the employer reasonably considers afford him a business benefit by rewarding loyalty, motivation and experience. There was considerable pressure from employer stakeholders to widen the proposed exemption to extend the five-year exemption or provide that employers do not need to justify any employment benefits

¹⁹⁵ Source: Income Data Services Studies Nos 681, 712, 731, 736, and 745.

¹⁹⁶ For instance, if pay is linked primarily to years of service rather than performance, in some circumstances this could be a disadvantage to women who leave the labour market temporarily or change jobs as a result of having children.

¹⁹⁷ Towards Equality and Diversity: Implementing the Employment and Race Directive.

¹⁹⁸ Equality and Diversity: The way ahead.

¹⁹⁹ Equality and Diversity: Age matters.

²⁰⁰ Equality and Diversity: Coming of Age.

which depend upon length of service. Benefits most often mentioned were incremental pay, holiday entitlement and long service awards.

12. Trade union responses on this issue were divided. One union demanded a complete exemption saying that the possibility of challenge meant that employers would withdraw benefits. Others have made it clear that they considered the provision went too far and that any blanket exemption would immediately be challenged in the courts. Some unions had asked for a 'no levelling down' provision to prevent employers withdrawing benefits.

13. Some employers also called for the proposed minimum wage exemption to be widened so that it would also cover employers paying young workers above the adult rate. Their argument was that without this employers could be obliged to pay young workers the same rate as older ones. This would only be the case, however, where employers could not justify paying the young workers a lower rate.

14. We have considerably simplified the drafting of provisions relating to length of service. In our view wider exemptions would have seriously risked successful challenge, and in practice we do not think employers would find it difficult to rely on the exemptions. We have decided against a 'no levelling down' provision, which would tie employers' hands, complicate implementation significantly and set a difficult precedent.

Options

15. There are three possible approaches to implementation:

- a) Do nothing: require employers to justify any discriminatory benefits on an individual basis – as set out in the *Age Matters* consultation.
- b) Provide that benefits which meet certain criteria to be set out in the regulations are justified. This would rely on an underlying national social policy requiring the protection of these types of benefits. To fall within this category, employers would need to ensure that they met the criteria but would not otherwise have to justify the provision of the benefit.
- c) Provide a blanket exemption, so that the benefit in question would not need individual justification to be lawful.

16. Option a puts the onus on employers to objectively justify all the pay and non-pay benefits they provide. However, this is the approach which received criticism during consultation. It would be a burdensome option for employers, as they may have to justify individual benefits in court, and many employers said to us this approach would mean the withdrawal of benefits or levelling down.

17. Both the exemption by reference to criteria (option b) and the blanket exemption (option c) require the Government to provide justification by way of an underlying social policy. The Government would also have to show that the exemption was proportionate (i.e., the least discriminatory means of achieving the social policy) as well as being supported by evidence. Whilst we do not believe that a blanket exemption is a proportionate means of achieving a social policy aim, some exemptions are sustainable – for example, on the basis of rewarding loyalty.

18. We, therefore, intend to exempt any length-of-service requirement of five years or less. In addition, benefits which depend on length of service will be exempt if they are intended to reflect experience or encourage or reward loyalty or maintain

motivation. That would cover long service awards, for example, or additional holiday entitlement after a number of years of service. Most benefits will fall into one or other of these categories, and others may be justifiable under the ordinary provisions for justification.

Costs and benefits

Business sectors affected

19. All business sectors will be affected. There is evidence of employers using either age- or service-related criteria when providing pay and non-pay benefits, both through the consultation and through large-scale case studies. However, there is little statistical evidence to support a judgement of which industrial sectors will be more or less affected. We do know, that in terms of pay benefits, the public sector and charities are more likely to be affected (see paragraph 4).

Costs and benefits to individuals

20. Where benefits are covered by an exemption in the regulations or where employers choose to objectively justify certain benefits, then individuals are unlikely to be affected.

21. If employers cannot justify certain benefits that are not covered by an exemption, this may result initially in employers removing the benefit. While some individuals will, therefore, lose out, others who would not have qualified because of unjustified discrimination may gain in terms of perceived improved fairness - particularly since it is likely that in order to retain employee loyalty, these benefits will be replaced by other benefits (for instance a slightly higher pay settlement, or the greater use of performance pay).

Implementation costs to firms

22. Firms will need to understand the legislation and to see whether they need to justify any benefits that are dependant on length of service or age. They may need to consider removing some benefits and consider whether they replace them with others. This will take time, including in some cases consulting employees or their representatives. It is likely that it will take more time in medium and large firms compared with small firms (who are less likely to need to hold meetings in deciding what to do). The possible cost of this time is outlined in Tables 1 and 2. These are mean figures and are likely to vary considerably from firm to firm, depending on the types of benefits that they offer, the size and structure of the firm, and employment relations within the firm.²⁰¹

23. The total cost of becoming familiar with the legislation is about £31 million (£29 million for small firms and £2 million for medium and large firms). The total costs to medium and large firms of making a decision on what to do about pay and non-pay benefits that are linked to age or length of service are about £15m.

²⁰¹ In some larger firms, benefits may be decided by line managers rather than centrally. In such cases managers would need to be informed of new rules, if appropriate. We do not know the extent of these practices, and have, therefore, not attempted to quantify the impact of the legislation on those firms affected. Also, some firms with worker representation may need more time to renegotiate any necessary changes in benefits. We have not attempted to quantify this.

1. Cost of becoming familiar with the legislation

	Small firms	Medium and Large firms
Staff time (hours) per firms	1	2
Hourly cost of staff time ²⁰²	£25	£28
Total cost of staff time per firms	£25	£56
Number of firms	1,160,000	36,000
Total cost	£29m	£2m

Note: Hourly staff costs are estimated by taking hourly wages and multiplying by a factor of 1.3 to take into account non-wage costs. Source: for wages, Annual survey of Hours and Earnings 2004; for number of businesses, Small Business Service, SME statistics 2003 (number of GB businesses have had to be inputted using statistics from the UK and the regions)

2. Cost of making a decision about pay and non-pay benefits related to age or length of service for medium or large firms

Staff time (hours)	6
Hourly cost of staff time ²⁰³	£70
Total cost of staff time per firm	£420
Number of firms	36,000
Total cost	£15m

Note: Hourly staff costs are estimated by taking hourly wages and multiplying by a factor of 1.3 to take into account non-wage costs. Source: for wages, Annual survey of Hours and Earnings 2004; source for number of businesses, Small Business Service, SME statistics 2003 (number of GB businesses have had to be inputted using statistics from the UK and the regions)

24. The total implementation costs to all firms is shown in Table 3. These are estimated to be about £46m, and should fall either just before or just after the legislation is implemented.

3. Total implementation costs

	Cost of becoming familiar with legislation	Cost of making a decision	Total costs
Small firms	£29m	N/a	£29m
Medium and large firms	£2m	£15m	£17m
Total	£31m	£15m	£46m

25. Concerns were raised during the Coming of Age consultation that the implementation costs for smaller employers had been underestimated. However, whereas larger employers are assumed to seek to understand the legislation at once, smaller businesses tend to read the legislation on a “need to know” basis. The estimated cost of implementation presented here is an average cost across all smaller businesses. Furthermore, DTI and Acas will make detailed guidance on the legislation available for employers. As this has been tailored to the needs of small business, it is envisaged that this will significantly reduce the need to seek specialist legal advice.

²⁰² We assume that in a small firm a general manager will be involved in becoming familiar with the legislation and that in a medium or large firm the personnel manager will take on this role.

²⁰³ We assume that decisions of this nature will be undertaken by directors or chief executives.

Policy costs and benefits to employers

26. Employers who have to change their policies as a result of the legislation may suffer some detriment in terms of efficiency. This is more likely to be the case if employers change their benefits solely because of wanting to avoid being taken to an Employment Tribunal. However, there may be some modest efficiency gains if employers change their policies on pay and non-pay benefits because they are unable to justify these objectively, and have to move to policies that are based more on efficiency grounds.

27. Efficiency gains or losses are likely to be modest under both scenarios. If the inconvenience of being taken to an Employment Tribunal is the only reason for not maintaining a particular policy, then it is unlikely that this policy is doing much to increase firm performance. Conversely if removing a policy leads to increases in efficiency, this increase is likely to be modest, otherwise this policy would have been removed in the absence of legislation.

28. Further benefits may be felt because the potential for treating employees unfairly has declined. While not directly affecting efficiency this may have a bearing on the performance of some individuals and the general sense of employee wellbeing.

29. The new regulations are unlikely to add a substantial amount to employers' current statutory payments costs. The cost of removing the lower age limit for Statutory Maternity Pay, Statutory Sick Pay, Statutory Adoption Pay and Statutory Paternity Pay is negligible. Removing the upper age limit from SSP has the potential to bring approximately 220,000 employees over the age of 65 into SSP entitlement.²⁰⁴ However, only a small proportion of these will claim SSP and, of these, some will already be covered by an occupational sick pay scheme, which can be offset against SSP entitlement.

Costs to the Exchequer

30. There may be some increases in the numbers of claims to Employment Tribunals. These are likely to be modest in number compared with the potential arising from other proposals in the legislation and will make up part of our global assessment of the number of claims (see summary).

Equity and fairness

31. The aim of the legislation is to preserve pay and non-pay benefits that are objectively justified. Therefore, in most instances, there will be little change to equity and fairness.

32. Where employers change their policies that are dependant on age this will sometimes affect younger workers and sometimes affect older workers. For instance, many firms are now basing the pay of apprentices on years of training rather than age.²⁰⁵ Any increase in this trend should result in greater fairness and will benefit a part of the workforce that is less attached to the labour market.

33. Where employers change their policies that are dependant on length of service this is likely to benefit those workers that have shorter tenure. These tend to be women and younger workers. Changes could result in greater incentives to those groups to

²⁰⁴ Based on the number of employees over 65 who had earnings over the required level in 2001/2002.

²⁰⁵ Source: Income Data Service (2000) *Employing Young Workers* IDS Studies No 681

stay in the labour market, and in the case of women, some modest narrowing in the pay gap between men and women.

Race equality impact assessment

34. This legislation is intended to apply equally to all employees regardless of their racial or ethnic category. An assessment of the overall effect of these proposals is that there will not be a disproportionate impact across different groups.

Small firm impact test

35. The legislation applies to small firms as well as large firms. Although implementation costs are lower per firm, considering the numbers of employees, small firms are likely to be disproportionately affected. The total implementation costs to small firms is about £29 million.

Competition assessment

36. We have applied the Competition Filter. The results appear in Annex A. We are unaware of any sectors where competition is likely to be affected.

Enforcement, sanctions and monitoring

37. Individuals will have recourse to the Employment Tribunal system, should they feel that employers are retaining pay and non-pay benefits related to age or length of service that are not objectively justified.

Implementation and delivery plan

38. Subject to parliament's approval the regulations will be in place by March 2006, at least six months before they come into force in October 2006.

39. Good practice guidance will be available around the same time to help employers prepare. In addition to that, we are holding a conference in April to publicise the legislation.

40. Further details on the commencement date, awareness raising measures and guidance for employers and employees are available in the Summary Age Discrimination RIA.

Post-implementation review

41. The Department of Work and Pensions and the Department of Trade and Industry has jointly commissioned a baseline survey which will ask, amongst other age related practices, about the extent of pay and non-pay benefits. This survey will be repeated two to four years after the legislation is implemented. The Department will also commission a longitudinal study (based on case studies) that will look at the impact of age legislation as a whole, including any changes to the provision of pay and non-pay benefits.

Summary and recommendation

42. Several options for implementation were considered. These included employers having to objectively justify pay and non-pay benefits that are in some way based on age or length of service, a blanket exemption, and exemption by reference to criteria. As a result of consultation, an option that enables firms to retain policies that are

justifiable on grounds such as social policy at least cost to business has been chosen and assessed. This option is a combination of exempting by reference to certain criteria and allowing employers to justify policies that do not match these criteria.

43. The implementation costs of the chosen option to business come to about £46 million. This will be a one-off cost which business are likely to incur either just before the legislation comes into effect or just after.

44. Where policies that employers feel they can no longer justify are removed, this may result in a small increase in fairness and equality. There may be some modest policy costs and benefits to employers, and employees where more equitable policies are put in the place of unjustifiable ones.

Ministerial declaration

I have read the Regulatory Impact Assessment and I am satisfied the benefits justify the costs.

Signed:

Gerry Sutcliffe

Date: 7th March 2006

**Gerry Sutcliffe
Parliamentary Under-Secretary of State
(Minister for Employment Relations and Consumer Affairs)**

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Competition Filter

Competition Filter

Question	Answer
1. In the market(s) affected by the new regulation, does any firm have more than 10% market share?	No
2. In the market(s) affected by the new regulation, does any firm have more than 20% market share?	No
3. In the market(s) affected by the new regulation, do the largest three firms together have at least 50% market share?	No
4. Would the costs of the regulation affect some firms substantially more than others?	No
5. Is the regulation likely to affect the market structure, changing the number or size of firms?	No
6. Would the regulation lead to higher set-up costs for new or potential firms that existing firms do not have to meet?	No
7. Would the regulation lead to higher ongoing costs for new or potential firms that existing firms do not have to meet?	No
8. Is the sector characterised by rapid technological change?	Not relevant
9. Would the regulation restrict the ability of firms to choose the price, quality, range or location of their products?	No

Draft Employment Equality (Age) Regulations 2006

Transposition Notes

Council Directive 2000/78/EC of 27 November 2000 establishing a general framework for equal treatment in employment and occupation		
<p>Directive 2000/78/EC prohibits discrimination in employment and vocational training on grounds of religion or belief, disability, age and sexual orientation. The age 'strand' of the Directive is implemented in Great Britain by these Regulations; separate regulations have already implemented the other strands. Separate regulations will implement the age "strand" of the Directive in Northern Ireland.</p> <p>This table has been prepared by the Department of Trade and Industry. It sets out the main objective of each article of the Directive, and how it is to be implemented in Great Britain so far as the age strand is concerned. The Secretary of State is responsible for each aspect of implementation.</p>		
Article	Objectives	Implementation
1.	Sets out purpose of Directive to combat discrimination on the grounds covered.	No implementation required.

<p>2.</p>	<ul style="list-style-type: none"> • Prohibits direct and indirect discrimination, as defined; indirect discrimination may be justified. • Prohibits harassment, as defined. • Prohibits instructions to discriminate. • Permits exceptions for public security and other specified reasons. 	<p>Regulation 3 defines direct and indirect discrimination. Regulation 3 also provides that direct and indirect discrimination may be justified.</p> <p>Regulation 5 provides less favourable treatment by reason of a refusal to follow, or complaint about, an instruction to discriminate is itself a form of discrimination.</p> <p>Regulation 6 defines harassment.</p> <p>The substantive provisions in regulations 7 to 24 (see below) set out the circumstances in which such discrimination or harassment is unlawful.</p> <p>Regulation 25 provides that an employer is liable for the acts of employees.</p> <p>Regulation 26 provides that a person, who aids another to do an unlawful act, does an unlawful act himself.</p> <p>Regulation 28 provides an exception for national security.</p>
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<p>3.</p>	<p>Specifies that the Directive applies in relation to:</p> <ul style="list-style-type: none"> • access to employment; • employment conditions; • access to self-employment and occupation; • vocational guidance; • vocational training; • membership of workers' (or other professional) organisations. 	<p>Access to employment, self-employment and occupation, and employment conditions are implemented by the following provisions in the Regulations;</p> <ul style="list-style-type: none"> • Regulation 7 (applicants and employees); • Regulation 9 (contract workers); • Regulation 11 (trustees and managers of occupational pension schemes); • Regulation 12 (office-holders etc); • Regulation 13 (police); • Regulation 14 (Serious Organised Crime Agency); • Regulation 15 (barristers); • Regulation 16 (advocates); • Regulation 17 (partnerships); • Regulation 18 (trade organisations); • Regulation 19 (qualifications bodies); • Regulation 21 (employment agencies, careers guidance etc); • Regulation 22 (assisting persons to obtain employment etc); • Regulation 24 (relationships which have come to an end); • Regulation 25 (liability of employers and principals); • Regulation 26 (aiding unlawful acts). <p>Vocational guidance is implemented by;</p> <ul style="list-style-type: none"> • Regulation 21 (employment agencies, careers guidance etc); • Regulation 23 (institutions of further and higher education). <p>Vocational training is implemented by;</p> <ul style="list-style-type: none"> • Regulation 20 (providers of vocational training); • Regulation 22 (assisting persons to obtain employment etc); • Regulation 23 (institutions of further and higher education). <p>Membership of workers' (or other professional) organisations is implemented by Regulation 18 (trade organisations).</p>
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4.	Permits exceptions where a characteristic is a 'genuine occupational requirement' (GOR) for a job.	<p>Regulation 8 provides a 'general' GOR exception which applies in relation to;</p> <ul style="list-style-type: none"> • Regulation 7 (applicants and employees); • Regulation 9 (contract workers); • Regulation 12 (office-holders etc) • Regulation 13 (police); • Regulation 14 (Serious Organised Crime Agency); • Regulation 17 (partnerships); • Regulation 20 (providers of vocational training); • Regulation 21 (employment agencies, careers guidance etc); and • Regulation 23 (institutions of further and higher education).
5.	Obligation on employers to take appropriate measures to meet the needs of disabled persons.	No implementation required in relation to age.

6.	Permits the justification of some differences of treatment on grounds of age.	<p>Differences in treatment are provided for in the following regulations;</p> <p>Regulation 3 (discrimination on grounds of age); Regulation 11 and Schedule 2 (pension schemes); Regulation 27 (exception for statutory authority); Regulation 30 (exception for retirement); Regulation 31 (exception for the national minimum wage); Regulation 32 (exception for provision of certain benefits based on length of service); Regulation 33 (exception for provision of enhanced redundancy payments to employees); and Regulation 34 (exception for provision of life assurance cover to retired workers).</p>
7.	Permits ‘positive action’ measures which prevent or compensate for disadvantages.	Regulation 29 permits positive action in relation to facilities for training, opportunities for work, and trade organisations.
8.	Sets out the principle that Member States may maintain a higher level of protection than the Directive requires, but may not justify a reduction in the level of protection by reference to the Directive.	No implementation required.

9.	<p>Requires Member States to ensure that:</p> <ul style="list-style-type: none"> • procedures are available for individuals to enforce the Directive's obligations; • procedures are also available in relation to discrimination which takes place after the relevant relationship has ended; • organisations with a legitimate interest may engage in proceedings on behalf of or in support of a complainant. 	<p>Enforcement procedures are provided by regulation 36 (jurisdiction of employment tribunals) and regulation 39 (jurisdiction of county and sheriff courts). The usual rules of procedure in tribunals and courts apply in relation to complaints.</p> <p>Regulation 42 lays down the time limits for bringing proceedings. Regulation 41 and Schedules 3 and 4 also provide a questionnaire procedure to assist complainants in obtaining information related to complaints.</p> <p>Regulation 24 makes unlawful an act of discrimination that takes place after the relevant relationship has ended.</p> <p>Under the relevant rules of procedure there is no obstacle to organisations supporting a complainant in proceedings. No further implementation is required.</p>
10.	<p>Requires that the burden of proof falls on the respondent to a complaint, once the complainant has established facts leading to a presumption that discrimination has taken place.</p>	<p>Regulations 37 and 40 provide for the burden of proof in tribunal and court proceedings, as required by the Directive.</p>
11.	<p>Requires protection for persons who suffer victimisation as a result of a complaint of discrimination.</p>	<p>Regulation 4 defines victimisation as a form of discrimination. The substantive provisions in regulation 7 to 24 (see above) set out the circumstances in which discrimination (including victimisation) is unlawful.</p>
12.	<p>Requires Member States to bring attention to the implementation of the Directive, using all appropriate means.</p>	<p>Implementation of the Regulations will be brought to the attention of employers, individuals and providers of vocational training through a variety of Government-led promotional campaigns and through stakeholders such as non-departmental public bodies, the social partners and voluntary organisations.</p>

13.	Requires Member States to promote dialogue between social partners in accordance with national traditions and practice, to promote equal treatment. Also requires Member States to encourage social partners to conclude collective agreements, where consistent with national traditions and practice to do so.	<p>The Government promotes dialogue by encouraging partnerships at work – for example through the Partnership Fund – but it recognises that styles of partnership will be dependent on individual organisations’ cultures and history and does not, therefore, promote any one particular model of partnership working. The Partnership Fund provides funding for projects which aim to improve the relationship between employers, employees and their representatives, and is open to social partners.</p> <p>UK tradition and practice does not include promotion by the Government of collective agreements as a model preferable to others for employer-employee dialogue on equality or any other grounds, and it would be inconsistent with that tradition and practice for the Government to do so now.</p>
14.	Requires Member States to encourage dialogue with appropriate non-governmental organisations with a legitimate interest in combating discrimination.	<p>Non-governmental organisations were consulted during the implementation of the Directive on all matters from first principles to the detailed draft regulations. Dialogue took the form of;</p> <ul style="list-style-type: none"> • formal written consultation (with the publication of the <i>Age Matters</i> and the <i>Coming of Age</i> documents); • meetings chaired by ministers of the Age Advisory Group. (The group’s role included advising government on matters to do with implementing the age strand of the directive); and • face-to-face meetings. <p>Further dialogue with appropriate non-governmental organisations is taking place in the development of information, advice and guidance on the new legislation.</p>
15.	Permits exceptions for Northern Ireland in relation to police and teachers.	No implementation required in Great Britain.

16.	Requires Member States to ensure that any laws or administrative provisions contrary to the Directive are abolished, and that any provisions in contracts, collective agreements, and internal rules of undertakings, may be made void.	<p>A trawl of primary and secondary legislation has taken place. Laws permitting discrimination on grounds of age contrary to the Directive are abolished or amended by Schedules 8 and 9.</p> <p>No other laws or administrative provisions permitting discrimination on grounds of age contrary to the Directive have been identified in Great Britain.</p> <p>Regulation 43 and Schedule 5 implement the Directive's requirements as to contracts, collective agreements and internal rules of undertakings.</p>
17.	Requires Member States to provide for effective sanctions to enforce obligations under the Directive.	Regulation 38 provides the remedies for complaints in employment tribunal proceedings, which include payment of compensation. In accordance with regulation 39, in county or sheriff court proceedings the usual remedies for claims in tort apply, including the payment of compensation.
18.	Requires Member States to adopt the necessary laws and provisions to comply with the age strand of the Directive by 2 December 2006.	The Regulations will come into force on 1 October 2006.
19.	Requires Member States to report to the Commission by 2 December 2005 (and every five years thereafter) on the application of the Directive.	<p>The UK reported to the Commission on 30 November 2005 on the application of the Directive other than in relation to age.</p> <p>No further implementation is required until 2010.</p>
20.	Provides that the Directive entered into force on 2 December 2000.	No implementation required.
21.	Indicates that the Directive is addressed to the Member States.	No implementation required.

Department of Trade and Industry

