EXPLANATORY MEMORANDUM TO

THE EMPLOYMENT ACT 2002 (AMENDMENT OF SCHEDULES 3, 4 AND 5) ORDER 2007

2007 No. 30

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

2. Description

2.1 This Order amends Schedules 3, 4 and 5 of the Employment Act 2002 ("the Act").

2.2 The Act introduced a framework for statutory dispute resolution procedures. A failure to follow those procedures can affect the way in which the employment tribunal considers complaints by individuals that their employment rights have been breached, may prevent the tribunal from being able to consider the claim or the response, or may affect any award. The list of jurisdictions within the scope of these procedures is set out in Schedules 3, 4 and 5 of the Act.

2.3 The Order will add three more jurisdictions, set out in Article 2, to the Schedules. These jurisdictions were introduced after the Act gained Royal Assent and could not therefore have been included in the Schedules at the time.

2.4 The Order is due to come into force on 6 April 2007. A copy of the draft Order can be found at http://www.opsi.gov.uk/stat.htm

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

3.1 None.

4. Legislative Background

4.1 Part 3 of the Act provides for statutory dispute resolution procedures, which are set out in Schedule 2 to the Act. Schedule 2 contains both dismissal and disciplinary procedures and grievance procedures. These procedures apply to the employment rights jurisdictions listed in Schedules 3, 4 and 5 of the Act. In addition, section 31 of the Act requires an employment tribunal to vary a compensatory award in certain circumstances where the statutory procedures have not been completed in claims under jurisdictions listed in Schedule 3. Section 32 of the Act provides that, in certain circumstances where the statutory grievance procedures have not been followed, claims may not be presented under the jurisdictions listed in Schedule 4. Section 38 allows an employment tribunal to vary the compensatory award in claims

arising under the jurisdictions listed in Schedule 5, where the claimant has not received the statutory statement of particulars.

4.2 Sections 31(7), 32(8) and 38(8) of the Act contain a power for the Secretary of State to amend Schedules 3, 4 and 5. Section 51(3) of the Act provides that no Order may be made under it unless it has been approved by a resolution of each House of Parliament.

4.3 The amendments will ensure that the jurisdictions listed in Article 2 of the Order are treated in a consistent manner with the jurisdictions already within the scope of the Act.

5. Extent

5.1 The Order will apply to Great Britain.

6. European Convention on Human Rights

6.1 Jim Fitzpatrick MP, the Parliamentary Under Secretary of State for Employment Relations and Consumer Affairs, has made the following statement regarding Human Rights:

> In my view the provisions of the Employment Act 2002 (Amendment of Schedules 3, 4 and 5) Order 2007 are compatible with the Convention rights.

7. Policy background

7.1 The new jurisdictions were added to the statute book in 2004 and 2006 and could not therefore have been included during the Parliamentary passage of the Act. The Government considers that these later jurisdictions provide similar remedies though employment tribunals to those already within the scope of the Act and should therefore be added to the Schedules. The Government therefore considers that this will ensure a more consistent treatment of employment rights and should encourage claims to be resolved at an earlier stage.

7.2 The Department of Trade and Industry began consulting on 16 May 2006. The consultation closed on 11 August 2006 and received 12 responses. The vast majority of responses were supportive of the amendment. A copy of the consultation, together with the Government Response is available at:

http://www.dti.gov.uk/consultations/closedwithresponse/index.html

8. Impact

8.1 An assessment of the compliance costs to business of the measures arising from the Order has been placed in the libraries of both Houses of Parliament. Copies may be obtained from the Department of Trade and Industry, Regulatory Impact Unit, 4th Floor, 1 Victoria Street, London, SW1H 0EN. This is also available at:

http://www.dti.gov.uk/consultations/ria/index.html

8.2 This measure is intended to ensure that the statutory dispute resolution procedures are consistently applied across the new jurisdictions. The consequence of bringing the jurisdictions within the scope of the statutory dispute resolution procedure will have a negligible impact on business.

9. Contact

Steven Greenwell at the Department of Trade and Industry, tel: 020 7215 5056 or email: steven.greenwell@dti.gsi.gov.uk can answer any queries regarding this instrument.

Full Regulatory Impact Assessment
Employment Relations Directorate

The Employment Act 2002 (Amendment of Schedules 3, 4 and 5) Order 2006

November 2006

http://www.dti.gov.uk/consultations/ria/index.html

Executive summary

The statutory dispute resolution procedures (SDR) were introduced in October 2004, in order to improve the standards of dispute resolution in the workplace. The procedures intend to improve the resolution of workplace disputes, setting a minimum standard framework for resolving disciplinary and grievance issues in the workplace.

The Employment Act 2002 (Amendment of Schedules 3, 4 and 5) Order will add three new employment areas or 'jurisdictions' to the Schedules. A regulatory impact assessment (RIA) on the impact of SDR procedures was conducted in 2004, and constructed a methodology for calculating the costs and benefits of the SDR process. This methodology took account of all employment law areas that could involve recourse to a Tribunal, plus an assumption of additional Tribunal claims arising as a result of new jurisdictions being added to the scope of SDR.

This RIA explores the **potential costs and benefits arising over and above that calculated in the original RIA**. The assessment finds that **there will be no additional costs and benefits over and above that calculated in the original RIA.** This is because the costs and benefits of adding new jurisdictions to the scope of SDR were factored into the original cost benefit analysis.

The new jurisdictions are described in more detail in **Annex A.** The original full and final regulatory assessment on SDR procedures is attached in **Annex C.**

Purpose and intended effect of measure

Objective

1. That the current statutory dispute resolution procedures cover the range of employment rights disputes, in order to improve the resolution of workplace disputes.

Background

2. The Employment Act 2002 (Dispute Resolution) Regulations 2004 (the "Regulations") were introduced on the 1st October 2004. A full Regulatory Impact Assessment was conducted in January 2004.[1] The Regulations were intended to cover a wide range of employment rights disputes, including those about discrimination, unfair dismissal, working time and some collective rights.

3. The Regulations were intended to improve the resolution of workplace disputes, setting a minimum standard framework for resolving disciplinary and grievance issues in the workplace. This approach improves the chance that flexible solutions can be found before the breakdown of the employment relationship (which leaves the employee out of work and the employer having to recruit new staff).

4. Before the introduction of these Regulations, the system of dispute resolution worked very differently. Some employers did not have or did not consistently apply adequate disciplinary procedures, and many employees were unwilling to raise grievances in the workplace. Thus, an employee's only opportunity to raise a problem may be through an Employment Tribunal claim, and preceding SDR it was not uncommon for an employer to become aware of a workplace dispute only when summoned to appear before an Employment Tribunal. This is clearly an unsatisfactory solution for all parties concerned.

5. The full regulatory impact assessment explored a wide range of options intended to improve the resolution of workplace disputes. The net present value over ten years was quantified over a wide range of assumptions, under all of which the net present value of the quantified benefits outweighed that of quantified costs. The saving from having fewer Employment Tribunals to defend outweighed the annual recurring policy costs to employers incurred in implementing the new statutory procedures.

6. For a jurisdiction to be included in the scope of SDR, it must be listed in the Schedules 3, 4 and 5 of the Employment Act 2002 (the "2002 Act").[2] However, there are three jurisdictions of a similar nature to those contained within the Schedules which are not currently included (more information on the jurisdictions is detailed in **Annex A**):

- Regulation 45 of the European Public Limited-Liability Company Regulations 2004 (detriment in employment);
- Regulation 33 of the Information and Consultation of Employees Regulations 2004 (detriment in employment); and

1 http://www.dti.gov.uk/access/ria/pdf/ria-dispute_resolution.pdf
2 Employment Act 2002. http://www.opsi.gov.uk/acts/acts2002/20022--l.htm#sch3

- Paragraph 8 of the Schedule to The Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendment) Regulations 2006 (detriment in employment)

Rationale for government intervention

7. There seems no reason for disputes under these jurisdictions to be treated differently from those under other jurisdictions. They were introduced after the 2002 Act, and their exclusion is likely to generate confusion on behalf of both employees and employers with regard to their rights and responsibilities in the event of a dispute.

Consultation

8. This Order will ensure that the dispute resolution framework set out in the 2002 Act is applied to three new areas. The dispute resolution framework was developed after lengthy public consultation in 2001.[3] Further public consultation was carried out in advance of the Employment Act 2002 (Dispute Resolution) Regulations 2004.

9. The DTI held a 12-week public consultation exercise on the draft Order between 16 May 2006 and 11 August 2006. In addition, it has consulted with a number of other government organisations including Acas, the Employment Tribunal Service and the Small Business Service. Annex B contains a list of those who responded to the consultation. There were 4 responses concerning the Partial Regulatory Impact Assessment. Two respondents, the TUC and The British Nuclear Group, broadly agreed with our costs assessment whilst the North Western Local Authorities' Employers' Organisation and the Institute of Directors did not.

10. The North Western Local Authorities' Employers' Organisation felt that it would take around two hours for managers to read and understand the effects of this Order. The Government notes this observation but it does not consider that to understand the minor change would require two hours of management time.

11. The Institute of Directors made observations about the overall costs of the statutory dispute resolution procedure as a whole. The Government notes these observations, but the RIA deals with the impact of the proposed amendment rather than the overall statutory dispute resolution procedure.

Options

Sectors and groups affected

12. All employers involved in a dispute under the aforementioned jurisdictions will be required to follow a statutory 3-step procedure before reaching an Employment Tribunal. The original RIA for SDR found that approximately 1.2 million employers and 7.2 million employees would be affected by the SDR regulations. Of course, only a small proportion of these employers and employees will be affected by extending the scope of SDR to include new jurisdictions. The sectors and groups affected by the jurisdictions are explored in the accompanying RIAs for the regulations (see **Annex A**).

3 See Routes to Resolution, 2001 consultation: http://dti.gov.uk/er/individual/resolution.pdf

13. **Option 1. Do nothing**. Make no amendment to the scope of SDR, allowing certain employment rights jurisdictions to be excluded.

14. **Option 2. Add the jurisdictions**. Amend the legislation so that European Public Limited-Liability Company Regulations 2004; Information and Consultation of Employees Regulations 2004; and The Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendment) Regulations 2006 are included in the scope of SDR.

Costs and Benefits

15. **Option 1. Do nothing.** There appears to be no reason why the jurisdictions listed above should be excluded from SDR. The original RIA attached in **Annex C** finds that, even using a high cost scenario (e.g. using a higher range estimate of time spent by managers) the annual recurring costs associated with implementing SDR is more than offset by the annual recurring benefits from avoiding an Employment Tribunal. Failure to facilitate an alternative dispute resolution under the aforementioned jurisdictions will, on the whole, cost employers more in expensive Employment Tribunal claims than one-off implementation and recurring costs. Therefore to do nothing could prevent employers who are involved in certain disputes from following these procedures.

16. Furthermore, if the anomaly of their exclusion persists, this could promote confusion on behalf of employees and employers as to their rights and responsibilities in the event of a dispute.

17. **Option (2) Add the jurisdictions:** A full cost benefit analysis has already been conducted for the impact of Statutory Dispute Resolution procedures The RIA with the full cost benefit analysis is attached in **Annex B**.

18. Costs and benefits were calculated under the assumption that there are 700-900,000 employment related 'justiciable events' each year that could involve recourse to the law.[4] This figure was calculated on the assumption that 12-16% of disputes in the workplace go to Tribunal,[5] and that there are around 110,000 Tribunal claims per annum. The baseline assumption of 110,000 claims was made assuming an annual number of tribunal claims of 100,000, **plus an additional 10,000 claims for new jurisdictions.**[6]

19. The assumption of an additional 10,000 claims for new jurisdictions implies that the costs and benefits described have been calculated on the basis that each year, approximately 63,000-84,000 justiciable events will occur as a result of new employment law jurisdictions.[7]

20. This assumption more than covers the new employment jurisdictions considered in this RIA. Although it is difficult to predict the number of Tribunal cases that may arise as a result of a new jurisdiction, we can make assumptions based on the number of firms affected by the jurisdictions and the number of persons that might feel a detriment.

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4 A 'justiciable event' is defined as a matter experienced by a respondent which raised legal issues, whether of not it was recognised by the respondent as being 'legal' and whether or not any action taken by the respondent to deal with the event involved the use of any part of the civil justice system.
5 For the basis of this assumption, see footnote 4 of the original RIA, attached in Annex B.
6 Paragraph 72 of the original RIA, Annex B.
7 Assuming 12-16% of justiciable events lead to Tribunal, see para 18 above.

21. The RIA for the Information and Consultation of Employees Regulations 2004 estimates that approximately 6000 – 11,000 companies will choose to engage in information and consultation (I&C) activity, which itself is voluntary.[8] Even if we make the pessimistic assumption that 5 to 7% of representatives engaged in I&C companies will suffer a detriment, this implies just 300-770 justiciable events occurring.[9]

22. Predicting the number of justiciable events arising for European Public Limited-Liability Company representatives and Occupational and Personal Pension Scheme representatives is less straightforward, as in both cases take-up was difficult to ascertain.

23. We can take as a proxy the number of cases where a person has claimed to have suffered a detriment for being any type of employee representative, which up until 2005 was coded by the ETS. See Table 1.

Table 1. Cases accepted by ETS where claimant suffered detriment as an employee representative

	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05
No. cases	25	26	50	45	391	341	692	350
As % of all jurisdictional complaint	0.01	0.01	0.03	0.02	0.25	0.19	0.35	0.22

Source: ETS

24. In each year, the number of cases accepted by the ETS constituted less than one per cent of all jurisdictional complaints that year.

25. Even if we assume that the three new types of employee representatives created by the new jurisdictions in Option 2 double the average number of employment tribunal cases where an employee felt they had suffered a detriment in 2003/04 and 2004/05, then we can assume that approximately 6,500-8,700 justiciable events may be occurring in the workplace, under these new jurisdictions.[10]

26. We can therefore conclude that the assumption of an additional 63,000-84,000 justiciable events as a result of new jurisdictions more than covers the costs and benefits associated with the new jurisdictions contained in this RIA.

27. **Therefore this RIA does not calculate any additional costs and benefits as a result of Option (2), over and above that calculated in the original RIA and summarised above.**

Small Firms Impact Test

28. A small firms impact test was conducted under the original RIA. It found that the 2004 Regulations could potentially have a significant effect on small firms. Therefore, this would be limited insofar as many firms already have dispute resolution procedures in place. Feedback from stakeholders and the Small Business Service directly shaped the 2004 Regulations. Furthermore, two of the jurisdictions[11] do not apply to organisations with less than 50 employees whilst the third is an entirely voluntary regime.[12]

8 http://www.dti.gov.uk/er/emar/inform_consult_ria.pdf
9 Assuming one representative per company. Calculation: (.05-.07)*(6000-11000).
10 Calculation: (1042/(0.12-0.16))
11 The Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendment Regulations 2006 (SI No 349/2006) and the Information and Consultation of Employees Regulations 2004 (SI 3426/2004)
12 European Public Limited-Liability Regulations 2004 (SI 2004/2326)

29. Guidance on the dispute resolution procedure has specifically been developed for small businesses and is available on the Small Business Service website.[13]

Competition assessment

30. A competition assessment was carried out in the original RIA, and found that SDR would be unlikely to affect the competitiveness of a particular sector. The current amendments will have no effect on competition. There are unlikely to be any adverse effects upon new entrants to the market as all new entrants will face the same regulatory standards and this amendment will not change this situation.

Enforcement and sanctions

31. If employers do not go through the minimum steps required under the new Regulations, they face the increased chance of Employment Tribunal proceedings, with their associated risks and costs. Both sides also face adjustment of any award made by the Tribunal by 10%-50% (up for employers, down for employees), if they are held responsible for a failure to make reasonable attempts to follow the statutory procedures. Furthermore, if employers fail to follow the procedure for dismissing an employee, then there will be an automatic finding of unfair dismissal at a Tribunal. If employees do not follow the correct procedure, they may not make subsequent claims arising out of the same facts to an employment tribunal.

Monitoring and Post-implementation review

32. The Government is in the process of reviewing the wider statutory dispute resolution process and intends to publish a consultation document in the New Year.

Summary and recommendations

33. The RIA recommends Option 2. It concludes that there are no additional costs and benefits involved in amending the SDR over and above those calculated in the original RIA and summarised in Table 2 of that document (Annex C), and there appears to be no reason why the additional jurisdictions should be excluded from the SDR.

Ministerial Declaration

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

Jim Fitzpatrick

Jim Fitzpatrick

21st November 2006

13 http://www.businesslink.gov.uk/bdotg/action/layer?r.l2=1074207487&r.l1=1073858787&r.s=tl&topicId=1075122891

Contact Point

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Annex A: New Jurisdictions

European Public Limited-Liability Company Employees

1. The European Public Limited-Liability Regulations came into force in October 2004. The Regulations provide a mechanism for the creation of the European Company, or *Societas Europea*, known as the "SE". The SE is intended to provide a flexible framework for UK companies and is available to companies operating in more than one Member State.

2. In addition, the Regulations allow for employee involvement; information, consultation and potentially employee participation arrangements in the SE. Initially, employee involvement arrangements should be negotiated between the management and employees acting through a Special Negotiating Body (SNB). Employees are entitled to reasonable time off with pay to perform their functions as representatives.

3. Regulation 45 of the Regulations provides that an employee may complain to a tribunal if he has suffered detrimental treatment. Adding regulation 45 to the Schedules of the 2002 Act will ensure that, where an employee believes that he has been subjected to detrimental treatment, falling short of dismissal, both sides will have to follow the statutory dispute resolution procedure..

4. **RIA**: http://www.opsi.gov.uk/si/em2004/uksiem_20042326_en.pdf

Information and Consultation Representatives and Employees

5. The Information and Consultation of Employees (ICE) Regulations 2004 provide a mechanism for employers to inform and consult employees about ongoing matters in the workplace.. The kind of matters which employees should be informed and consulted about are very broadly defined, but can include, for example, strategic decisions about the company and issues which may affect an employees contract. The Regulations apply to undertakings where there are 150 or more employees, and will apply to employers with 50 or more employees from April 2008.

6. The requirement to inform and consult employees is not automatic, and is triggered either by a formal request from employees for an Information and Consultation (I&C) agreement, or by employers choosing to start the process themselves. The Regulations also provide for the retention of pre-existing agreements which have workforce support. Where no agreement is reached following an employee request, certain "standard" provisions for informing and consulting representatives of employees will apply.

7. Any disputes relating to whether an employee has adhered to the process for obtaining an I&C agreement are dealt with by making a complaint to the Central Arbitration Committee (CAC). Such complaints are not and will not be subject to the statutory dispute resolution procedure.

8. Employees wishing to exercise their rights under the Information and Consultation of Employees Regulations should not be subjected to any "detrimental treatment". For example, an employer should not penalise an employee for making a complaint to an employment tribunal to enforce an information and consultation right, or for putting his or her name forward to stand as an Information and consultation representative. Adding regulation 33 of the ICE Regulations to the Schedules to the 2002 Act, will ensure that, where an employee believes that he has been subjected to detrimental treatment, falling short of dismissal, both sides will have to follow the statutory dispute resolution procedure.

9. **RIA**: http://www.dti.gov.uk/er/emar/inform_consult_ria.pdf

Occupational and Personal Pension Schemes Representatives

10. The Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendment) Regulations 2006 (the "Pensions Regulations") will apply from the 6 April 2006. The Pensions Regulations will ensure that employers have to consult employees who are active or prospective scheme members, or their representatives, when they are planning to make a "listed" i.e. significant change to their pension schemes. The Regulations will apply to employers with 150 or more employees from April 2006, and will apply to employers with more than 50 employees from April 2008.

11. When a change is proposed, the employer must provide all the affected employees with key information relating to the change. He must also consult with the relevant employees or their representative. This could be for example, a Trade Union Representative, an Information and Consultation Representative, or someone

specifically elected under the Pensions Regulations for the purpose of the consultation. The consultation process should last for a minimum of 60 days. The response to the consultation must then be considered by the person who proposed the change, before a decision is made.

12. The Pensions Regulations contain very similar provisions to the Information and Consultation of Employees Regulations. A representative should not suffer any detrimental treatment as a result of specified conduct in relation to the consultation process. Nor should an employee be treated detrimentally if they make a complaint to the Pensions Regulator about the conduct of the consultation process.

13. Regulation 17 and paragraph 8 of the Schedule to the Pensions Regulations provide protections against detrimental treatment of employees involved in a consultation carried out under the Pensions Regulations. Adding Paragraph 8 of the Schedule to the 2002 Act will ensure that, where an employee believes that he has been subjected to detrimental treatment, falling short of dismissal, both sides will have to follow the statutory dispute resolution procedure..

14. An RIA was produced for the Pensions Bill: http://www.dwp.gov.uk/publications/dwp/2005/occ_pen_schemes/oppscer06.pdf (at page 35)

Annex B: Organisations that responded

A list of those who responded publicly to the consultation:

South East Employers
Institute of Directors
Confederation of British Industry
British Nuclear Group Limited
GMB
National Association of Schoolmasters Union of Women Teachers
North Western Local Authorities' Employers' Organisation
Thompson Solicitors
European Study Group
Trades Union Congress
Greater Manchester Pay and Employment Rights Advice Service
Acas

Full Regulatory Impact Assessment
Employment Relations Directorate

Statutory Dispute Resolution Procedures

January 2004

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

Executive Summary

Policy Objectives

1. The statutory dispute resolution procedures should improve the resolution of workplace disputes. Many firms already have very good dispute resolution mechanisms in place, but others have inadequate or non-existent procedures. These Regulations aim to improve this situation by imposing new minimum standards.

2. By improving standards of dispute resolution in the workplace, these Regulations should provide means for problems to be raised and discussed in the workplace, which in turn can be expected to reduce the incidence of breakdown of the employment relationship due to workplace disputes, and in some cases remove the need to resort to Employment Tribunals. This implies significant benefits to employers, employees and the taxpayer.

Costs and benefits

3. The Regulations will involve significant costs to employers by requiring the introduction and use of the statutory procedures for both disciplinary actions and employee grievances. There will be also, however, significant benefits to employers through better employment relations, increased productivity, lower recruitment costs and fewer Employment Tribunal cases to defend.

4. The Regulations will affect the ability of employees to apply to an Employment Tribunal, by requiring them, in most circumstances, to participate in workplace dispute resolution first. However, in the event of violent, abusive or otherwise unacceptable behaviour of one party, or where it is not practical to comply, employees (and employers) are exempt from the requirement to follow the procedures. Employees should benefit from the increased likelihood both of maintaining the employment relationship and of avoiding the need for a Tribunal.

Equity and fairness

5. The Regulations may have a positive impact on diversity by encouraging quicker and more flexible solutions to discrimination disputes.

Small firms

6. The Regulations will disproportionately affect small firms, since small firms are more likely to have insufficient dispute resolution procedures in place, than larger firms. Consultation with small firms and small firms organisations was carried out with the aims of helping limiting the burden on small firms to what is reasonable and necessary to achieve the aims of the legislation and of finding ways to help them to set up (where necessary) the requisite procedures.

Enforcement/incentives

7. If employers do not go through the minimum steps required under the new Regulations, they face the increased chance of Employment Tribunal proceedings, with their associated risks and costs. Both sides also face adjustment of any award made by the Tribunal by 10%-50% (up for employers, down for employees), if they are held responsible for a failure to make reasonable attempts to follow the statutory procedures. Furthermore, if employers fail to follow the procedure for dismissing an employee, then there will be an automatic finding of unfair dismissal at a Tribunal. If employees do not raise grievances in the workplace, they may not make subsequent claims to Employment Tribunal.

Net effect

8. Summary tables for costs and benefits can be found in the Summary of costs and benefits section at the end of this Regulatory Impact Assessment.

9. The net present value over ten years of the quantified benefits outweighs that of the quantified costs under all compliance scenarios considered, which are: 60%, 80% and 100% initial compliance. Where initial compliance is lower than 100%, it is assumed to rise to 100% after five years. With 80% or 100% initial compliance, quantified benefits will outweigh quantified costs after three years and with 60% initial compliance, quantified benefits are likely to outweigh quantified costs after four years.

10. Once 100% compliance is achieved, quantified recurring annual benefits are estimated at £99-108 million and quantified recurring annual costs at £35-48 million.

11. The annual recurring benefits are made up of a £68-74 million saving to employers from having fewer Employment Tribunals claims to defend, and a £31-34 million saving to the taxpayer from administering fewer Employment Tribunal claims. The annual recurring policy cost is the £35-48 million cost to employers of using the statutory procedures.

12. There are unquantified benefits such as better employment relations, which will have a positive impact on productivity and retention of staff, implying lower recruitment costs. Benefits to individuals arise from solving employment disputes: this can lead to a better working environment, lower stress and jobs retained that might have been lost; and further benefits to individuals arise from avoiding Employment Tribunals and the stress, cost and diminished employment prospects they entail.

13. There are also unquantified costs, such as the time cost of a companion where the right to be accompanied is used and the increased cost to the Employment Tribunal Service through extra time needed to sift cases.

Background and policy objective

1. The statutory dispute resolution procedures should improve the resolution of workplace disputes. Whilst many employers use sophisticated dispute resolution mechanisms, a large number of firms have inadequate or non-existent procedures, or indeed do not use the procedures they have in place.

2. The statutory procedures will set a new minimum standard framework for resolving disciplinary and grievance issues in the workplace. Using internal procedures that conform to the defined minimum standards, disputes will be identified and discussed in the workplace. This approach improves the chance that flexible solutions can be found before the breakdown of the employment relationship (which leaves the employee out of work and the employer having to recruit new staff).

3. These Regulations will apply to all employers and employees. They will affect a wide range of employment rights disputes, including those about discrimination, unfair dismissal, working time and some collective rights (see Schedules 3, 4 and 5 of the 2002 Employment Act for more details).

4. The current system of dispute resolution often works very differently. Some employers do not have or do not consistently apply adequate disciplinary procedures, and many employees are unwilling to raise grievances in the workplace. Thus, an employee's only opportunity to raise a problem may be through an Employment Tribunal claim, and it is not uncommon for an employer to become aware of a workplace dispute only when summoned to appear before an Employment Tribunal. This is clearly an unsatisfactory solution for all parties concerned.

Risk assessment

5. The Regulations seek to mitigate risks both to employers and to employees:

- the risk of employers being drawn into costly Employment Tribunals without any initial opportunity to attempt to resolve the dispute within the workplace: it is estimated that defending a Tribunal claim costs an average of £2000 to employers.[1]
- The risk of individuals being required to pursue Employment Tribunal cases (with the stresses and negative effect on future employment prospects associated therewith) over grievances that were not explored through formal procedures in the workplace, where they could perhaps have been resolved to the parties' mutual satisfaction.
- The risk of using the Employment Tribunal system as a place of first resort, rather than only as the last resort for disputes once it is clear they cannot be settled without litigation. Using it as a place of first resort reduces the system's speed and efficiency to deal with problems that do require legal determination.

Options

1 Estimate bases on Survey of Employment Tribunal Applications (SETA) 1998

6. Given the main policy objective of producing a significant improvement in workplace dispute resolution, four options were considered at the time of the Employment Bill which became the Employment Act 2003:

Option 1. Doing nothing.

Option 2. Advertising the existing Acas code of practice for workplace dispute resolution and raising awareness of the benefits of successful procedures.

Option 3. Introducing statutory minimum procedures for workplace dispute resolution requiring written statement(s) and meeting(s) between the disputing parties.

Option 4. Introducing statutory minimum procedures as in Option 3 with the addition of required mediation.

Options 1 and 2 were discounted, because they would be less likely to achieve the policy objective of significant improvement in workplace dispute resolution. The existing code of practice has already been widely disseminated; so further advertising could only have a marginal impact. Options 1 and 2 would perpetuate the situation where many workplaces are without disciplinary and grievance procedures. Option 4 was not pursued since mediation would impose additional costs, may not be suitable for all parties and could simply delay justice. Option 3 is expected to achieve the policy objective more effectively than Option 4. Option 3 was therefore decide upon and will be implemented through these Regulations.

Key assumptions

7. In order to analyse the costs and benefits of the Regulations, assumptions had to be made on:

1. The annual number of employment-related disputes with legal implications: 700,000 to 900,000 – see footnote 4.
2. The proportion of these disputes which will be exempt from the procedures and the proportion where no action is taken: 5% and 19% respectively - see footnotes 5 and 6.
3. The proportions of firms in different size categories which currently have satisfactory, unsatisfactory or no procedures: see Table 4 in Annex 2.
4. The management time required to introduce the procedures: see Table 6 in Annex 2.
5. The proportions of disputes going through the procedures, which will use the two-step and three-step procedures: 85% and 15% respectively – see footnote 47 in Annex 2.
6. The proportions of disputes coming from workplaces which currently have satisfactory, unsatisfactory or no procedures: 50%, 30% and 20% respectively.
7. The management and employee time required to use the procedures: see Tables 8 and 9 in Annex 2.

8. The likelihood of Tribunal claims when procedures are or are not in place: 10-13% and 18-23% respectively.

9. Of those disputes where action is taken, but an Employment Tribunal claim is not made, the proportion currently solved using workplace dispute resolution procedures: 50%.

8. These assumptions and their sources are all detailed below in the main text and the annexes. To summarise, assumptions for 1, 2, 5 and 8 were based on survey evidence. Assumptions for 3 for the larger firms were also based on survey evidence. For assumptions for 4, 6, 7 and 9, attempts have been made to make reasonable estimates, taking into account responses from consultation where appropriate. The assumptions were checked for internal consistency.

Numbers affected

10. The Regulations will have the following effects:

- All employers will have to ensure that a satisfactory three-step procedure is in place. This affects up to 1.2 million employers.[2]
- It is estimated that up to 7.2 million employees will be affected by these Regulations.[3]
- Those employers and employees who are involved in a dispute will, in most cases, have to follow the procedures. A 'justiciable event' is defined by Genn, *Paths to Justice*, 1998 as a matter experienced by a respondent which raised legal issues, whether or not it was recognised by the respondent as being 'legal' and whether or not any action taken by the respondent to deal with the event involved the use of any part of the civil justice system. These employment events can include: dismissal, changes to terms or conditions of employment, harassment or discrimination, unauthorised deductions from wages and non-payment of the National Minimum Wage.
- We estimate that there are between 700,000 and 900,000 employment-related 'justiciable events' each year.[4] These numbers will of course increase as new employment rights are introduced.
- In some instances, individuals with a potential dispute against their employer will decide not to take any action. It is estimated that this occurs in 19% of cases where disputes arise,[5] and that 5% of disputes will be exempt from following the

2 Small Business Service statistics (SBS) 2002: 1,226,070 businesses employed at least one person in 2002.
3 Calculation based on SBS statistics 2001,2002 and assumptions in Table 4 in Annex 2: number of employees working for firms with inadequate or non-existent dispute resolution procedures.
4 Based on the Legal Services Research Centre (LSRC) Periodic Survey, first findings published 2003, it is estimated that 2.94 million serious employment problems, which might have involved recourse to law, occurred in the three-and-a-half years from January 1998. Over this period, there were about 374,000 Employment Tribunal claims. Over this period, that equates to about 12.7% of disputes going to Tribunal. Over the last three years there were about 110,000 Tribunal claims per annum. Applying the same ratio would imply a slightly higher annual level (853,000 compared to 829,000) of justiciable disputes in the last three years. However, it is equally possible that the proportion of disputes going to Tribunal has increased since the study period with the number of justiciable disputes remaining broadly constant (in which case around 13.3% of disputes go to Tribunal). Genn, *Paths to Justice*, 1998, suggests about 14.6% of disputes going to Tribunal over the period 1992-7. Given these uncertainties, the current proportion of disputes going to Tribunal is taken to be 12-16%, which gives an annual number of disputes of 687,500-916,000, rounded to 700,000-900,000.
5 Based on the LSRC Periodic Survey. 19% of people experiencing justiciable problems at work took no action to resolve the problem. The individual takes no action and procedures to resolve the dispute are not required.

procedures.[6] This means that the total population of disputes to which these Regulations apply is between 532,000 and 684,000 disputes. For the purposes of the RIA, we assume that the total number of disputes occurring each year is constant.

Equity and fairness

11. The proposed Regulations are unlikely to have a significant impact on diversity. However, a number of positive and negative factors exist, which are explored below.

All employees

12. It should be noted that the admissibility provisions will affect the way employees' Employment Tribunal claims are dealt with, in that the admissibility of a claim, and award level at Tribunal if the claim is successful, will depend on their having followed the procedures. However, this will be balanced by the proviso that parties need not follow the procedures if to do so would lead one of them to suffer bullying, intimidation and other unacceptable conduct; this will provide additional protection for those being harassed. Also, extensions to existing time limits will apply to allow the completion of grievance procedures before Tribunal claims are lodged. Lack of awareness should hopefully not be a significant problem because of the initial guidance and advice campaign, and the ongoing guidance and advice of Acas.

Diversity and effects on particular groups of employees

13. The Regulations may have a positive impact on diversity, in that the statutory dispute resolution procedures will encourage more flexible and timely solutions to discrimination grievances.

14. Evidence from Employment Tribunal claimants (see Table 1 below) shows that they are a good representation of the diversity existing in the working population, with regard to age and ethnicity, and fairly good with regard to sex.

15. 2.8% of Employment Tribunal claims in the financial year 2002/3 were in disability jurisdictions as defined by the Disability Discrimination Act 1995, which is an indication (but an underestimate, because not all claims made by disabled people are about disability discrimination) of the proportion of claimants who are disabled. 11% of GB employees aged 16-plus are disabled by the definition of the aforementioned Act.[7] This evidence weakly suggests that the disabled are not over-represented, at least not substantially, in the population of Tribunal claimants. There is no available data yet on the sexual orientation and religion/belief of Tribunal claimants; these characteristics relate to new anti-discrimination regulations that came into force only on the 1st and 2nd December 2003. The evidence above and in Table 1 would imply that as a whole, the effect of the Regulations should be spread fairly evenly over the working population.

6 Analysis of evidence from *Paths to Justice* suggests a possible range of between 1% and 14%. We have opted for a conservative middle of the range of 5%. We use incidents of harassment at work as a proxy of circumstances that would lead to exemption. 14% represents those suffering employment-related problems who had experienced harassment at work. 1% represents the proportion of employees who experienced employment-related problems and did not do anything about it because they were too scared.
7 Labour Force Survey, September to November 2002.

Table 1: Demographic comparison between Employment Tribunal claimants and GB employees

	Employment Tribunal claimants	GB employees aged 16+
Age		
Median age	42	37
Mean age	41	38
Sex		
Men	60%	53%
Women	40%	47%
Race		
Asian	3%	2%
Black	2%	2%
White	93%	95%

Source: ET claimants: Survey of Employment Tribunal Applications (SETA) 1998. GB Employees: Labour Force Survey (LFS) - spring 1998.

16. However, these Regulations will affect all those involved in employment-related disputes, not just Employment Tribunal claimants; so the above evidence is not conclusive as to their effects on particular groups of employees. There is weak indicative evidence that the 'marginalised' members of society (who are those more likely to be discriminated against), are more likely to face employment-related disputes.[8] This would suggest 'marginalised' groups will be disproportionately impacted upon by these Regulations. However, 'marginalised' people are perhaps more likely to be engaged as non-employee workers, rather than as employees, and the new procedures do not apply in respect of non-employee workers.

17. Nevertheless, it is possible that the 'marginalised' members of society face a disproportionate number of the employment-related disputes *of employees*, in which case they will be disproportionately affected by the new Regulations.

18. In any case, there is no evidence to suggest that workplace dispute resolution procedures produce less favourable outcomes than Employment Tribunal cases for those groups of employees who tend to be discriminated against. Employees will still be able to take their grievances to Employment Tribunals if workplace procedures fail to resolve them, so these Regulations should not have a negative impact on such employees. To sum up, even if 'marginalised'/disadvantaged employees are going to be disproportionately affected, they should not be negatively affected by the Regulations.

Sensitivity analysis

19. In the following sections, benefits and costs of the introduction of this legislation are listed and measured (where possible). In order to come up with some estimates of these, certain levels of compliance with the legislation must be assumed. This Regulatory Impact Assessment estimates the costs and benefits based on three

8 LSRC Periodic Survey included an institutional survey of people living in temporary accommodation (hence the more marginalised members of society). In this group around 15% suffered an employment-related justiciable problem, compared to around 6% in the main survey (a random sample of the general population).

assumed initial compliance rates of 60%, 80% and 100%. When only partial initial compliance is assumed (i.e. 60% and 80%), we assume full compliance (100%) will be achieved after five years. If employers fail to comply with these requirements, the costs of implementing and using procedures will be reduced, as will the benefits from reduced Employment Tribunal claims to employers, individuals and taxpayers.

Benefits

20. More employment disputes should be solved, benefiting employers and employees alike, through lower stress, increased productivity and increased job satisfaction.

Better employment relations and its impact on productivity

21. Employment disputes can give rise to tensions at the workplace and damage wider management-employee relations. This may impact adversely on the productivity of the business.

22. There is evidence of a positive relationship between having formal disciplinary and grievance procedures in place and having good workplace well-being measures, such as the number of dismissals and voluntary resignations.[9] Measures that improve workplace well-being may have beneficial effects on economic performance in the long term.

23. Furthermore, there is indirect evidence that points to a likely positive relationship between having formal disciplinary and grievance procedures and above-average labour productivity. Data shows that 62% of workplaces following a certain number of high commitment management practices (one of which is having formal grievance and disciplinary procedures in place), reported above-average labour productivity.[10]

24. Whilst the evidence mentioned above suggests a positive impact from better employment relations on productivity, the data is not conclusive on the potential size of the effect. For this reason we do not attempt to quantify this benefit.

Less damage to individuals' employment prospects

25. Making an Employment Tribunal claim can damage the future job prospects of the individual (as well as leading to increased stress). 44% of those making a Tribunal claim report lower status employment, 51% had lower paid employment and 24% are unemployed following a claim.[11]

26. Solving more disputes in the workplace should allow more employees to stay in post. Therefore, they will retain these higher paid, higher status jobs, and their employment prospects will not be damaged.

Fewer Employment Tribunal claims

27. The Regulations aim to improve dispute resolution within the workplace, through encouraging both parties to use formal procedures. This in turn reduces the likelihood of disputes reaching an Employment Tribunal. Significant numbers of Tribunal cases involve disputes that have not been first explored through workplace procedures. A reduction in Tribunal claims will bring benefits to those individuals who still go to Tribunal, by allowing their cases to be determined more quickly.

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9 Cully M., Woodland S., O'Reilly A. and Dix G., *Britain at Work*, Routledge 1999.
10 Cully M., Woodland S., O'Reilly A. and Dix G, *Britain at Work*, Routledge 1999.
11 SETA 1998.

28. Employer survey evidence from 1998[11] showed that in about 37% of cases which went to Employment Tribunal there was no meeting between the parties, no use of a written procedure and no other attempt made to resolve the dispute. If an attempt is made to solve these disputes in the workplace first, some are of them are likely to be solved and hence the number of Tribunal claims should go down.

29. We assume a reduction of about 31-34% of the assumed annual number of claims of 110,000, which is 34,000 to 37,000 fewer Employment Tribunals per year. This gives a new annual number of claims of 73,000 to 76,000. See Annex 1 for details.

30. Assuming an initial compliance of 60% we would expect the initial number of Employment Tribunals to be around 97,000 (all else equal), a reduction of about 12%. The number would decrease gradually to 73-76,000 after five years (all else equal), as the level of compliance increases gradually to 100% over the same time period. See Annex 1 for details.

31. Finally, assuming initial compliance of 80%, the expected initial number of Employment Tribunals would be around 85,000-87,000, a reduction of around 21-23% gradually easing to 73,000-76,000 over five years (all else equal). It is expected that there would be a lag of perhaps a year from when the procedures are fully implemented. See Annex 1 for details.

Reduced costs to employers of defending Employment Tribunal claims

32. An Employment Tribunal claim costs an employer £2,000 on average in management time and legal fees.[12] The cost will vary substantially from firm to firm and upon the outcome and type of the case. Many claims that are settled or withdrawn at an early stage will cost the respondent very little. Some cases that go to a hearing are very expensive. This cost estimate does not include the cost of awards made to successful claimants. On this basis a reduction of 34,000-37,000 claims will produce annual cost savings of £68-74 million for employers.

33. This amount would be lower for the cases in which only partial compliance is assumed, until they achieve full compliance. When an initial 60% compliance is assumed (13,000 first-year reduction in the number of claims) savings to employers would amount to £26 million, increasing to £68-74 million after five years. If 80% initial compliance were assumed (23-25,000 first-year reduction in the number of claims), initial savings to employers would amount to £46-50 million.

Lower recruitment costs

34. Using the dispute resolution procedures in the workplace should reduce the number of cases where the employment relationship breaks down and the employee leaves the firm. The average saving to the employer per employee retained is £3,900.[13] The order of magnitude of these savings across all employers is likely to be in the tens of millions.[14]

12 Estimate based on SETA 1998.
13 Average derived from Chartered Institute of Personnel and Development (CIPD) Labour Turnover Surveys 2001,2002, 2003.
14 SETA 1998 suggests just 3% of people taking a complaint to Employment Tribunal keep their job afterwards. If 20-30% keep there job following use of workplace dispute resolution procedures, this suggests an illustrative calculation of recruitment cost savings: [0.17 to 0.27] x £3900 x [34,000 to 37,000] = £23 to 39 million rounded to 2 significant figures.

Savings to the taxpayer

35. A reduction in Employment Tribunal claims reduces the costs of running the Employment Tribunal System. It is estimated that it costs on average £910 to process each claim.[15] A 34,000-37,000 annual reduction in the number of claims would save the taxpayer around £31-34 million per year.

36. Lower compliance rates will generate correspondingly lower cost savings. When an initial 60% compliance is assumed, savings to the taxpayer would amount to around £12 million for the first year, going up to £31-34 million after five years. If 80% initial compliance were assumed, savings to the taxpayer would amount to around £21-23 million for the first year.

Costs

Costs of introducing statutory dispute resolution procedures

37. The Regulations will involve **one-off 'adjustment' costs** to all businesses (implementation costs). Annex 2 provides further details on the cost calculations. The adjustment costs represent time taken for businesses to familiarise themselves with the basic procedures model and, for those who already have procedures, checking that their existing procedures comply. To estimate the costs we used two scenarios. Firms with satisfactory procedures already in place will, on average, spend 30 minutes to check whether the procedures meet the statutory standard. This will vary from a phone call between a manager and a personnel officer who knows about the procedures (especially in large firms) to cases where some time is spent on establishing compliance.

38. The differences between the high- and low-cost scenarios regard the amount of management time spent by firms with non-existent or inadequate procedures. Firms with existing procedures that fall short of the minimum level are assumed to spend on average one hour in the low-cost scenario, and two hours in the high-cost scenario on adjusting their procedures. We assume that managers in firms with no procedures will need an average of two hours in the low-cost scenario and four hours in the high-cost scenario to collect the relevant information and to set up procedures. The actual amount of time spent by individual employers may differ from these averages, although the assumptions are reasonable if the employer can access the standardised forms and support material that will be provided by the Department of Trade and Industry (DTI)/Acas. We consider the high-cost scenario to be more realistic than the low-cost scenario.

39. The cost for a firm with no procedures already in place is estimated at around £99, for a firm with unsatisfactory procedures at around £50 and for a firm with already satisfactory procedures at around £12. The total one-off implementation costs are estimated to be £39-73 million (see Annex 2 for details).

40. If only partial initial compliance is assumed (i.e. either 60% or 80%), the one-off cost would be spread over five years, until full compliance is achieved. The first-year cost would be £23-44 million in the event of 60% compliance and £31-58 million in the event of 80% compliance (see Annex 2 for details).

15 Sources: the ETS Annual Report and Accounts 2002/3 and Acas.

A publicity campaign will be launched prior to the introduction of the Regulations. This will increase awareness among employers and employees so that procedures will be more widely adopted and therefore the associated benefits felt in a relatively short time. The publicity campaign will have a non-recurring cost of up to £2 million.

Costs of using statutory dispute resolution procedures

41. Employers will face **recurring costs** in complying with the Regulations, through following the statutory procedures. Previously, these disputes were either not handled at all or were dealt with using sub-standard procedures. The cost of applying the procedures is associated with the absorption of management and employee time. Annex 2 discusses these calculations in more detail.

42. As before, we assume a low-cost and a high-cost scenario for those employers who do not already have procedures in place. The difference between the two is in the written stages of the procedures. Writing the complaint or response is assumed to take two hours in the high-cost scenario and one hour in the low-cost scenario. Table 8 in Annex 2 details the other assumptions on management and employee time required.

43. The average cost to employers who currently have no procedures in place, of using the three-step procedure is £199 in the high-cost scenario and £179 in the low-cost scenario. This compares with an average additional cost of £119 for a three-step procedure where some form of inadequate procedure is used at present.

44. The average cost of the two-step procedure is £72 and £104 in the low- and high-scenarios respectively for firms with no procedures currently in place. This compares with an average additional cost of £60 for the two-step where some form of insufficient procedure is used at present.

45. There will be no additional cost for firms with satisfactory procedures in place already for using either set of procedures. The total annual costs come to £35-48 million (see Annex 2 for more details).

46. If only partial initial compliance is assumed (i.e. either 60% or 80%), initial annual costs would be £21-29 million**1** and £28-38 million**2** respectively. These levels of initial costs would gradually increase up to £35-48 million per year after five years, and thereafter, when full compliance would be achieved.

47. There will be extra costs incurred when the employee chooses to use his or her right to be accompanied at the hearing(s) with the employer. If the companion works for the same employer, then the extra cost will be to the employer, but if the companion is employed by a Trade union, then the cost will be to the Trade union. These costs have not been quantified, because we have no basis for how often the right to be accompanied is used. The order of magnitude is expected to be £1-10 million.**3**

48. There may also be increased costs to the Employment Tribunal Service from extra time needed to sift cases. These costs are explored in the Regulatory Impact

1 Calculated as [£34.9-47.9 million] x 0.6 = £21-29 million rounded to nearest million.
2 Calculated as [£34.9-47.9 million] x 0.8 = £28-38 million rounded to nearest million.
3 For illustration, if we value companion time at £14.90 (New Earnings Survey (NES) 2003 average earnings: £11.46, multiplied by 1.3 to take account of non-wage costs), assume they spend an hour on each meeting and are used in 25% of the 266,000 to 342,000 disputes (see Annex 2) each involving two more meetings as a result of the new Regulations (the average will be less than two, but two used for simplicity), then the extra costs would amount to £2.0-2.5 million.

Assessment accompanying the Employment Tribunal procedures**4** that are due to come into force at the same time as the dispute resolution procedures (October 2004).

Impact on small firms

49. Small firms are likely to be over-represented in those affected by these new Regulations. It is estimated that small businesses (with 1-19 employees) represent 820,000, or 98% of the 840,000 companies which currently have sub-standard or no procedures at all (see Annex 2). They form 92% of the total number of firms (with at least one employee) in Great Britain**5**. Therefore the cost of adopting dispute resolution procedures will affect small firms disproportionately. The Small Firms Impact Test (see Annex 3) explores how the Regulations may impinge on this particular group and explores mitigation strategies for this group.

50. Many small businesses do not have a specialised personnel function and therefore lack staff who deal with human resources issues on a day-to-day basis. Businesses with small numbers of employees are also likely to see certain employment situations occur very infrequently (e.g. parental leave following an adoption). This combination of a lack of specialised personnel and infrequent exposure to employment rights issues may contribute to a greater incidence of disputes in small firms.

51. As discussed in the consultation document, DTI recognises the need for user-friendly guidance and standard forms to reduce the implementation costs, particularly for small firms.

Competition assessment

52. This legislation will apply to all firms. It is unlikely to affect the competitiveness of any particular sector. It is designed to reduce the cost of dealing with disputes in the workplace for both employers and employees. We believe it will also improve the workings of the labour market.

53. Individuals can face both short- and long-run costs from making Tribunal claims. A quarter of all Employment Tribunals claimants are unemployed subsequent to the case**6**. The introduction of statutory dispute resolution procedures, by reducing the number of Employment Tribunal claims, may have a positive impact on labour participation rates.

54. Employment disputes may lead to skilled-labour job resignations for reasons other than professional or career development. By improving dispute resolution within the workplace, this legislation may enhance the match between skills required at work and the skills workers have.

Enforcement and sanctions

4 Available at http://www.dti.gov.uk/er/individual/etregs_ria.pdf
5 Small Business Service 2002.
6 SETA 1998.

55. The Regulations will establish rights and responsibilities for both employers and employees in terms of how they resolve disputes at work.

56. Employers will need to consider the costs of introducing and using the statutory procedures – the cost of introducing the procedures is estimated to be £12-99 on average, and £179-199 each time it is involved in a standard (where the three-step procedure will apply) workplace dispute (see Annex 2). These figures will vary considerably between firms. These costs will need to be weighed up against the possible costs of defending a Tribunal case, estimated to be £2,000 on average.**7** Dismissals that do not use the statutory procedures will be automatically unfair. In addition, if the employer has not fully completed the statutory procedures, any awards to the claimant can be increased by 10%-50%. Taking the median award of around £3200 as an example, this would be increased by £320-1600.**8**

57. In most cases, it is probable that the employment relationship will break down irreparably when a dispute is handled via an Employment Tribunal as opposed to the use of workplace procedures. Replacing an employee is estimated to involve an average cost of £3,900, again with wide variation**9**.

58. Equally, employees have an incentive to use the statutory procedures because this approach is more likely to solve the dispute and preserve the employment relationship. Not following the procedures may affect the admissibility of their case and, if it is admissible, level of award at Employment Tribunal: a £3200 award could be reduced by £320-1600. In addition, employees will avoid the stress and negative impact on future employment prospects associated with going to a Tribunal.

Monitoring and review

The Employment Tribunal Service will be able to monitor the number of cases where failure to comply with the procedural requirements becomes an issue, including the number of cases where awards are adjusted because of procedural failings. The overall volume of Tribunal claims will also be an indicator of effectiveness.

The next Workplace Employment Relations Survey (WERS) will be in the field in 2004. This will look at the incidence of dispute resolution procedures at present and will act as a benchmark for the policy. The Survey of Employment Tribunal Applications (SETA) 2003 will likewise give a pre-Regulations benchmark and includes questions on the demographics of Employment Tribunal claimants and their use of procedures. The DTI intends to carry out further WERS and SETAs, to which the findings of WERS 2004 and SETA 2003 can be compared.

Consultation

7 Estimate based on SETA 1998.

8 The Employment Act 2002 established that in the event that either party in the dispute failed to use the statutory procedures, any subsequent award would be varied by between 10% - 50%, i.e. if an employer failed to use the statutory procedures, any subsequent award to the claimant could be increased by 10%-50%. The median award in cases with unfair dismissal jurisdictions was £3,225 in 2002/03 (Source: Employment Tribunal Service Annual Report). If procedures were not followed this would therefore increase the average costs of a Tribunal where the claimant is successful by up to about £1,600. This includes a possible increase in the award if the employer has not issued a written statement or the statement is incomplete or inaccurate.

9 Chartered Institute of Personnel and Development, Labour Turnover Surveys, average of last three years, 2001-3: £3,899.

59. These Regulations are based on the dispute resolution framework set out in Employment Act 2002. This legislation was developed after public consultation during 2001.**10**

60. The proposed Regulations have been developed with input from a wide range of external stakeholders. An Advisory Group was formed, with representation from small firms associations, trade organizations, trade unions and other key agencies. These groups participated in a pre-consultation phase – views received at that stage have been fully considered and taken into account in finalising the Regulations.

61. The DTI has consulted a number of other government organisations, including Acas, the Employment Tribunal Service and all Government Ministerial Departments.

62. The Government has, in addition, tested its policy plans at the 'grass-roots' level. Focus groups have been held with small firms, large businesses, trade union legal specialists, and Acas advisers and conciliators.

63. The DTI held a 16-week public consultation on the draft Regulations, between 9 July and 29 October 2003.**11** 203 responses were received from respondents with a wide spectrum of viewpoints. More detail on this consultation can be found in the Government's Response to the Consultation, published on 20th January 2004.

Summary of costs and benefits

64. The table below summarises both quantified and unquantified costs and benefits (expressed in 2002/03 prices) once 100% compliance has been achieved. When quantifying benefits and costs we have also used different levels of initial compliance below 100% (i.e. 60% and 80%) in order to assess its impact on costs and benefits. A table with the results can be found in Annex 2.

10 See *Routes to Resolution*, 2001 consultation: http://www.dti.gov.uk/er/individual/resolution.pdf.
11 See the consultation document: http://www.dti.gov.uk/er/individual/dis_res_consdoc.htm.

Table 2: Quantified and unquantified costs and benefits

	Annual benefits	Annual costs	One-off costs
To employers	• Better employment relations with positive impact on productivity • Keeping skilled staff • Lower recruitment costs • Reduced costs from 34,000-37,000 fewer Tribunal claims per annum = £68-74 million	• Annual recurring policy costs of using statutory procedures = £35-48 million, plus time cost of companion where right to be accompanied used (cost may sometimes be to a Trade union)	• Implementation costs = £39-£73 million
To individuals	• More employment disputes solved • Improved employment prospects • Reduced stress and costs from 34,000-37,000 fewer Tribunal claims per annum		
To the taxpayer	• Savings from fewer Tribunal claims = £31-34 million	• Increased costs to the Employment Tribunal Service for extra time needed to sift cases	• £2 million for a publicity campaign prior to the Regulations coming into force

All costs and benefits quoted to 2 significant figures

65. It is likely that initial costs will outweigh initial benefits. Using net present value analysis, with 100% or 80% initial compliance total quantified benefits are likely to outweigh total quantified costs by the third year, and with 60% initial compliance, total quantified benefits are likely to outweigh total quantified costs by the fourth year.

The table below shows the net present value (NPV)**12** of costs and benefits over 10 years, both recurring and one-off, in each compliance scenario. Where initial compliance is less than 100% it is assumed to rise to 100% after five years. The table below assumes the high-cost scenarios for both one-off implementation costs and recurring costs to employers.

Table 3: Net present value of quantified costs and benefits with varying compliance rates over ten years

60% initial compliance		80% initial compliance		100% initial compliance	
NPV benefits	NPV costs	NPV benefits	NPV costs	NPV benefits	NPV costs

12 Net present value is a standard tool in economic appraisals to value future returns. It takes into account that future returns are worth less than returns today. This is captured in the discount rate applied to future returns. The above calculations are based on a discount rate suggested by the Treasury Green Book of 3.5%. See http://www.hm-treasury.gov.uk/economic_data_and_tools/greenbook/data_greenbook_index.cfm.

£697-754m	£355-436m	£751-838m	£379-460m	£847-922m	£405-485m

Using high-cost scenario

As can be seen from Table 3, over ten years quantified benefits outweigh quantified costs under any compliance scenario. This should be considered in conjunction with the unquantified costs and benefits shown in Table 2.

Declaration

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

Signed……

Gerry Sutcliffe, Parliamentary Under-Secretary of State, Department of Trade and Industry

Contact point

66. Any comments on this Regulatory Impact Assessment should be addressed to:

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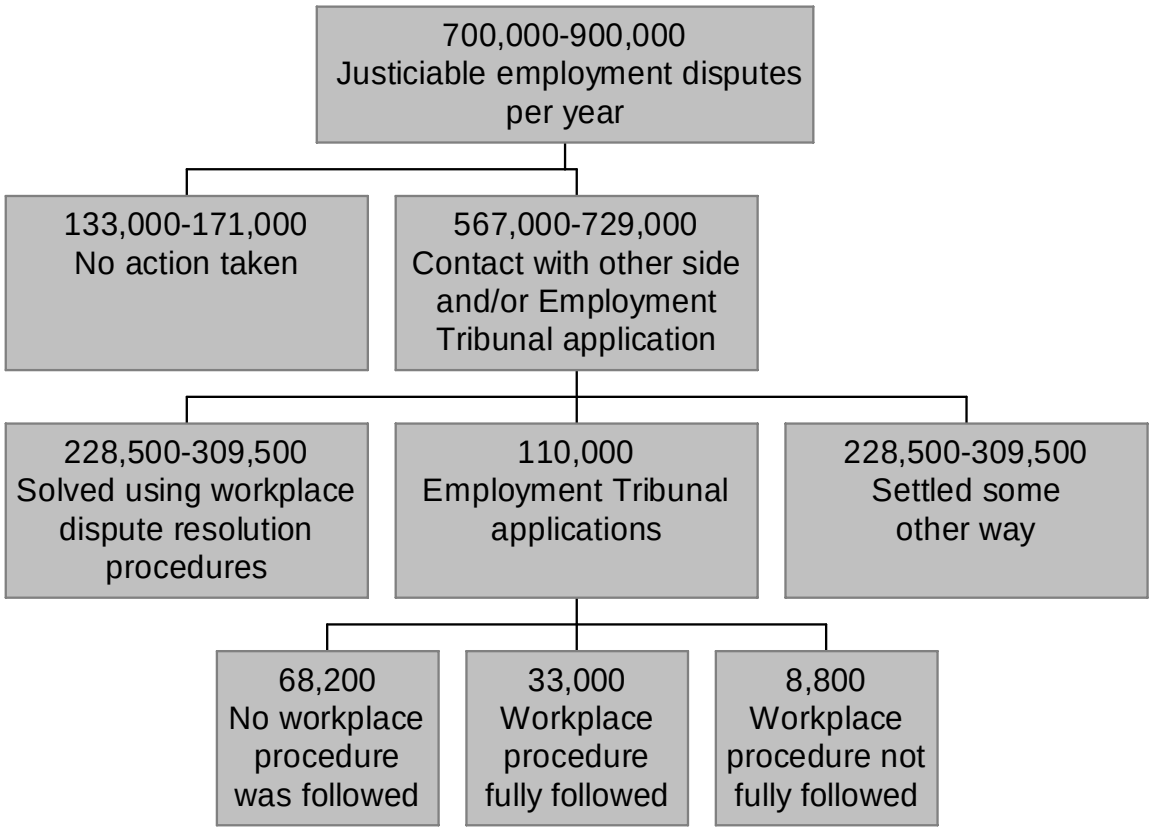
Annex 1:Estimating the effect on Employment Tribunal claims

Flowchart showing main assumptions on employment dispute and Tribunal numbers:



67. Taking the underlying trend level of Employment Tribunal claims as 100,000 a year, and adding 10,000 for new jurisdictions (an average: initial 6,000 later rising to 14,000) gives us a basis of 110,000 claims a year. This implies that about 590,000 to 790,000**13** disputes were resolved in some other way, including those where the employee did not contact their employer or make a Tribunal claim (disputes where no action was taken are estimated to be about 133,000 to 171,000**14**).

68. Employer survey evidence from 1998**15** suggested that 48% of Employment Tribunal claims come from workplaces with no written procedures, 14% from workplaces with written procedures that had not been used and 7% from workplaces where written procedures had been only part used, leaving just 30% of claims where a written procedure had been followed all the way through. Among the Tribunal claims, it can be assumed that 30% (33,000) arose even with full procedures being followed, and that 62% (68,200) had followed no procedure at all (i.e. 48% with no written procedure plus 14% with written procedures that had not been followed).

69. It is assumed that 50% of disputes where action was taken but there was no resort to an Employment Tribunal (i.e. there was contact with the other side only) were

13 Calculated as (700,000 to 900,000) – 110,000.
14 Calculated as 19% (see footnote 4) x [700,000 to 900,000] = 133,000 to 171,000.
15 SETA 1998

settled using workplace dispute resolution procedures.**16** This implies that 228,500 to 309,500 disputes**17** are solved in the workplace. This in turn implies that when action is taken and dispute resolution procedures are used, 10-13%**18** of these disputes will result in a Tribunal claim. However, when action is taken and procedures are **not** used, 18-23%**19** of disputes can be expected to lead to a Tribunal claim.

70. Assuming full compliance (100%), and five per cent of disputes being exempt from the procedures**20**, we would expect approximately 10-13% of the 76%**21** of justiciable employment disputes which will go through the procedures, to lead to an Employment Tribunal. We would expect approximately 18-23% of the 5% of justiciable employment disputes that are exempt from the procedures to lead to a Tribunal. This implies the number of Tribunals will be around 74,000-75,000**22** (all else equal) from the year after the legislation comes into force. This is a reduction of 35,000-36,000. We assume a range of 73,000-76,000 Employment Tribunals per year; that is a reduction of about 31-34% of the assumed annual number of claims of 110,000.

71. Assuming an initial compliance of 60% we would expect the initial number of Employment Tribunals to be around 97,000**23** (all else equal), a reduction of about 12%. The number would decrease gradually to 73,000-76,000 after five years (all else equal), as the level of compliance increases gradually to 100% over the same time period.

72. Finally, assuming initial compliance of 80%, the expected initial number of Employment Tribunals would be around 85,000-87,000**24**, a reduction of around 21-23% gradually easing to 73,000-76,000 over five years (all else equal).

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16 There is no direct evidence on this, but this assumption seems consistent with other assumptions based on WERS98.
17 Calculated as ([590,000 to 790,000] – [133,000 to 171,000]) x 0.5 = 228,500 to 309,500.
18 Calculated as 33,000 / ([228,500 to 309,500] + 33,000) = 9.64% to 12.62% rounded to two decimal places.
19 Calculated as 68,200 / ([228,500 to 309,500] + 68,200) = 18.06% to 22.99% rounded to two decimal places.
20 Analysis of evidence from *Paths to Justice* suggests a possible range of between 1% and 14%. We have opted for a conservative middle of the range of 5%. We use incidents of harassment at work as a proxy of circumstances that would lead to exemption. 14% represents those suffering employment-related problems who had experienced harassment at work. 1% represents the proportion of employees who experienced employment-related problems and did not do anything about it because they were too scared.
21 Calculated as 100% minus 19% where no action taken minus 5% which are exempt from following procedures.
22 Range derived as [9.64% x 76% x 900,000 + 18.06% x 5% x 900,000] to [12.62% x 76% x 700,000 + 22.99% x 5% x 700,000] ≅ 74,065 to 75,185 rounded to 74,000 to 75,000.
23 Calculated as: [(9.64% x 0.6 + 18.06% x 0.4) x 76% x 900,000 + 5% x 18.06% x 900,000] to [(12.62% x 0.6 + 22.99% x 0.4) x 76% x 700,000 + 5% x 22.99% x 700,000] ≅ 97,102 to 97,252 for the initial year, rounded to 97,000. To be consistent with a final range of 73,000-76,000, a similar calculation was used, based on 607,000 to 1,225,000 disputes per year, to give 96,947-97,382 for the initial year, rounded to 97,000.
24 Calculated as: [(9.64% x 0.8 + 18.06% x 0.2) x 76% x 900,000 + 5% x 18.06% x 900,000] to [(12.62% x 0.8 + 22.99% x 0.2) x 76% x 700,000 + 5% x 22.99% x 700,000] ≅ 85,583 to 86,219 for the initial year, rounded to 86,000. To be consistent with a final range of 73-76,000 a similar calculation was used, based on 607,000 to 1,225,000 disputes per year (the numbers of disputes which give a final range of 73,000 to 76,000 Tribunals), to give 84,974-86,692 for the initial year, rounded to 85-87,000.

Annex 2: Details of cost calculations

73. The costs to employers of introducing and using the statutory procedures arise from the opportunity cost of the management and employee time the procedures require.

Cost to employers of introducing procedures

74. All employers will face adjustment costs. Once the firm has become familiar with and understood the procedures and implications of non-use, they will not face this cost again.

75. Table 4 shows the assumptions made about the existing (pre-legislation) use of procedures. The data for larger firms are based on WERS98 data.**25** It is assumed that small firms are less likely to have procedures at all or ones that meet the minimum requirement (labelled as 'sub-standard').

Table 4: Proportions of firms with satisfactory and unsatisfactory procedures

Number of employees	Number of firms[1]	Satisfactory procedures	Sub-standard procedures	No procedures
1-4	797,000	25%	25%	50%
5-9	216,000	30%	30%	40%
10-19	119,000	40%	30%	30%
20-49	57,000	79%	9%	12%
50-99	19,000	79%	9%	12%
100-199	8,000	79%	9%	12%
200-249	2,000	79%	9%	12%
250-499	4,000	79%	9%	12%
500+	4,000	79%	9%	12%

1 Source of employer numbers is Small Business Service, Statistical Bulletin, Small and Medium Enterprises, Statistics for Great Britain, 2002

Table 5 shows these expressed as numbers of firms.

25 Cully M., Woodland S., O'Reilly A. and Dix G., *Britain at Work*, Routledge 1999.

Table 5: Numbers of firms with satisfactory and unsatisfactory procedures[26]

Number of employees	Satisfactory procedures	Sub-standard procedures	No procedures
1–4	199,000	199,000	398,000
5–9	65,000	65,000	86,000
10–19	48,000	36,000	36,000
20–49	45,000	5,000	7,000
50–99	15,000	2,000	2,000
100–199	7,000	1,000	1,000
200–249	1,000	200	200
250–499	3,000	300	400
500+	4,000	400	500
Total	386,000	308,000	532,000

All rounded to nearest 1,000

76. Table 6 then lists the assumptions made about the amount of management time required to understand the new requirements and, if necessary, to improve procedures and make any necessary changes to written statements.

Table 6: Introduction of procedures: time spent by managers (in hours)

	High-cost scenario			Low-cost scenario		
Number of employees	Satisfactory	Sub-standard	None	Satisfactory	Sub-standard	None
1-4	0.5	2	4	0.5	1	2
5-9	0.5	2	4	0.5	1	2
10-19	0.5	2	4	0.5	1	2
20-49	0.5	2	4	0.5	1	2
50-99	0.5	2	4	0.5	1	2
100-199	0.5	2	4	0.5	1	2
200-249	0.5	2	4	0.5	1	2
250-499	0.5	2	4	0.5	1	2
500+	0.5	2	4	0.5	1	2

77. Multiplying the numbers of firms affected in Table 5 by the hour assumptions in Table 6 and valuing management time at £24.82 per hour**27**, this implies total one-off adjustment costs of £39-73 million.**28**

26 Source of employer numbers is Small Business Service, Statistical Bulletin, Small and Medium Enterprises, Statistics for Great Britain, 2002.

27 In 2002, the average hourly pay, excluding overtime, of a manager/senior official (1 digit SOC 2000) in Great Britain was £19.09. Source: New Earnings Survey (NES) 2003. The cost of a manager's time includes non-wage costs and overheads, estimated at 30% of wage costs. The hourly cost of a manager's time is, therefore, £19.09 x 1.3 = £24.82 rounded to nearest penny.

28 Calculated as: [£24.82 x (0.5 x 386,000 + 2 x 308,000 + 4 x 532,000)] to [£24.82 x (0.5 x 386,000 + 308,000 + 2 x 532,000)] = £39-73 million rounded to 2 significant figures.

78. If only partial initial compliance is assumed (i.e. either 60% or 80%), the above one-off cost would be spread over five years, until full compliance is achieved. This is shown in the table below.

Table 7: One-off adjustment costs with varying compliance rates

		Year 1	Year 2	Year 3	Year 4	Year 5
60% compliance	Low cost	£23m	£4.0m	£4.0m	£4.0m	£4.0m
	High cost	£44m	£7.3m	£7.3m	£7.3m	£7.3m
80% compliance	Low cost	£31m	£2.0m	£2.0m	£2.0m	£2.0m
	High cost	£58m	£3.6m	£3.6m	£3.6m	£3.6m

All to 2 significant figures

Cost to employers of using procedures

79. In all cases where procedures are not currently used, or where those procedures do not meet the new minimum requirements, employers will incur additional costs from running these procedures.

80. There are estimated to be 700-900,000 disputes per year that could involve recourse to the law. It is further assumed that in 19% of these action is not taken and in a further five per cent parties to the dispute are exempt from following the procedures. This leaves 532-684,000 disputes where some form of action will be taken. It is assumed that, at present, procedures that meet the new minimum standard are used in 50% of all cases where action is taken (i.e. 266,000 to 342,000). It is further assumed that in 30% of cases (i.e. 159,600 to 205,200 cases) a procedure is used but it does not meet the minimum requirements. And in the remaining 20% of cases (106,400 to 136,800 cases), no procedure is followed at all.

81. Tables 8 and 9 set out the assumptions on the average amount of time that employers and employees need to spend using the three-step and two-step procedures, respectively. Assuming a 50-50 split on grievance and disciplinary procedures, both average employer (manager) time and employee time spent on the three-step procedure equal four-and-a-half hours in the low-cost scenario. They both equal five hours in the high-cost scenario. In the two-step procedure, the manager's time on average would amount to two and three hours in the low- and high-cost scenarios respectively, while the employee's time would amount to one-and-a-half and two hours in the low- and high-cost scenarios, again respectively.

Table 8: Average company time used to complete the modified (three-step) grievance/ dismissal procedures

	Dismissal and disciplinary procedure				Grievance procedure			
	Manager time (hours)		Employee time (hours)		Manager time (hours)		Employee time (hours)	
	High cost	Low cost	High cost	Low cost	High cost	Low cost	High Cost	Low cost
Writing complaint	2	1	-	-	-	-	2	1
Hearing	2	2	2	2	2	2	2	2
Appeal hearing	2	2	2	2	2	2	2	2
Total	6	5	4	4	4	4	6	5

Table 9: Average company time used to complete the modified (two-step) grievance/ dismissal procedures

	Dismissal procedure				Grievance procedure			
	Manager time (hours)		Employee time (hours)		Manager time (hours)		Employee time (hours)	
	High cost	Low cost	High cost	Low cost	High cost	Low cost	High cost	Low cost
Writing complaint	2	1	-	-	-	-	2	1
Writing response	-	-	-	-	2	1	-	-
Appeal hearing	2	2	2	2	-	-	-	-
Total	4	3	2	2	2	1	2	1

82. On the basis that management time costs £24.82 per hour and employee time costs £14.90 per hour**29**, the average cost of using the three-step procedure is around £179-199**30** and the average cost of the two-step procedure is around £72-104**31**, both to the nearest pound. These are the additional costs that will apply when no procedures at all are used at present. Where procedures are used, but need to be improved, the additional cost will be lower; here it is assumed to be three and one-and-a-half hours of both manager and employee time, for the three- and two-step procedures, respectively, which produces a unit cost of around £119 per case for the three-step procedure and around £60 for the two-step procedure, both to nearest pound. Where satisfactory procedures are already used, there will be no additional recurring cost from these Regulations.

83. Multiplying these unit costs by the number of disputes where new or better procedures will be required, and assuming that the two-step procedure is used in fifteen per cent of the disputes where any action is taken,**32** and that there is full compliance with the new legislation, it produces a total recurring cost estimate of £35-48 million**33** (£35-45 million under the low-cost scenario, and £37-48 million under the high-cost scenario).

84. If only partial initial compliance is assumed (i.e. either 60% or 80%), initial annual costs would be around £21-29 million**34** and £28-38 million**35** respectively. These levels of initial costs would gradually increase up to £35-48 million per year after five years, and thereafter, when full compliance would be achieved. This is shown in table 10.

29 This is calculated as the average gross hourly earnings of all employees on adult rates, excluding overtime all occupations, whose pay was not affected by absence. GB: £11.46. (Source New Earnings Survey 2003) Multiplied by a factor of 1.3 to take into account non-wage labour costs: £14.90 to nearest penny.

30 Three-step procedure calculated as [4.5 x (£14.9+£24.82)] to [5 x (£14.9 + £24.82)] = £179-199 rounded to nearest pound.

31 Two-step procedure calculated as [(2 x £24.82) + (1.5 x £14.9)] to [(3 x £24.82) + (2 x £14.9)] = £72-104 rounded to nearest pound .

32 Provisional analysis of the SETA 2003 dataset suggests 38% of Employment Tribunal claimants ended their employment before submitting their application and were not suing for unfair dismissal. This is an indication of the proportion likely to go through the two-step procedures. However, the proportion should be quite a lot lower, since we would expect the employment relationship to be more likely to be still intact at the time of going through the procedures, and even when it has ended, in order to go through the two-step grievance procedures, both parties must agree in writing to not go through the three-step procedures, or it must be not reasonably practicable for one or other party to attend a meeting. We therefore assume 15% of applicable disputes will go through the two-step procedures, and 85% will go through the three-step procedures.

33 [106,400 to 136,800] x ([£178.74 to £198.6] x 0.85 + [£71.99 to £104.26] x 0.15) [cases with no procedure] + [159,600 to 205,200] x (£119.16 x 0.85 +£59.58 x 0.15) [cases with sub-standard procedure] = £35-48 million rounded to 2 significant figures.

34 Calculated as: [£34.9-47.9 million] x 0.6 = £21-29 million rounded to nearest million.

35 Calculated as: [£34.9-47.9 million] x 0.8 = £28-38 million rounded to nearest million.

Table 10: Annual costs with varying compliance rates

		Year 1	Year 2	Year 3	Year 4	Year 5
60% compliance	Low cost	£21-27m	£24-31m	£28-36m	£31-40m	£35-45m
	High cost	£22-29m	£26-33m	£30-38m	£33-43m	£37-48m
80% compliance	Low cost	£28-36m	£30-38m	£31-40m	£33-43m	£35-45m
	High cost	£30-38m	£32-41m	£33-43m	£35-45m	£37-48m

All figures quoted to 2 significant figures, ranges come from range of 700-900,000 justiciable disputes per year

Annex 3: Small Firms Impact Test

Small Firms Impact Test – Stage One

85. The first stage of the Small Firms Impact Test clearly indicated that the Regulations could have an impact on small firms. The Stage One Impact Test 'Sounding' involved a broad portfolio of stakeholder organisations. An advisory group was formed to act as a sounding board for policy, legal and guidance developments. Participants include the British Chambers of Commerce, the Small Business Council, the Forum for Private Business and the Federation of Small Business. Priority sectors, such as construction, hospitality and retail, were also represented by specialist groups – e.g. the British Retail Consortium, the Construction Confederation and the British Hospitality Association/ Restaurant Association. The advisory group has met a number of times (and will continue to meet to discuss the ongoing guidance campaign for these Regulations).

86. These stakeholder groups generally accepted that the statutory dispute resolution procedures could have a strong positive impact on solving workplace problems. The stakeholder groups were keen to ensure that the Regulations should be as pragmatic and straightforward as possible. They were concerned that overly complex requirements would be unworkable for small firms. The group also provided valuable input on developing a suitable communications and guidance programme.

87. The Small Business Service was consulted, and it agreed that these Regulations could have a significant impact on small businesses. As a result, it was necessary to carry out Stage Two.

Small Firms Impact Test – Stage Two

88. Stage Two of the Impact Test requires soundings to be taken with small firms. With that in mind, the Small Business Service organised two small firms focus groups on 15 and 16 April 2003.

89. Eleven organisations drawn from across the United Kingdom participated in the two events – an additional four were also invited but could not attend. There were seven small firms represented from a variety of sectors including construction, consultancy, training, and software; and four trade associations, from the hospitality, professional services and retail sectors. These firms were drawn from a database held by the Small Business Service – it is possible that the firms were not truly representative of the small business community as a whole, but they were intentionally drawn from those sectors considered likely to be most affected by the new requirements.

90. The focus group participants felt that the procedures could be adopted without too much difficulty. Most firms felt their existing procedures were largely in line with the proposed Regulations. There was no feeling that the modified dismissal procedure would encourage employers to dismiss summarily, as the standard procedures were not seen as being unduly onerous.

91. Successfully informing small firms about the new Regulations was seen as a particularly important challenge, and the participants' preferred approach to communicating these policies was discussed in some depth.

Small Firms Impact Test - Conclusions

92. Both stages of the Small Firms Impact Test confirmed that the proposed Regulations could potentially have a significant effect on small firms. However, the evidence gathered in focus groups suggested that there would be limited consequence to the many firms that already have dispute resolution procedures in place. Policy feedback from main stakeholder organisations has directly shaped the proposed Regulations to address the concerns of small firms.