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Private Equity (Transfer of Undertakings and Protection of Employment) Bill 2007-08

This is a Private Members Bill introduced by John Heppell MP who came fifth in the ballot, due for Second Reading on 7 March.

The Bill seeks to introduce greater employment protection for employees who work in businesses undergoing changes in ownership by share transfer.

This proposal arises from concerns, often voiced by trade unions, that private equity buy-outs can have a negative effect on employment. This is strongly disputed by representatives of private equity.

The Bill proposes to make certain provisions of the transfer of undertakings regulations (generally known as TUPE) apply where there is an "equity transfer" as defined. Powers are given to the Secretary of State to define in detail the scope of transactions that would be caught by the provisions.

Vincent Keter

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Summary of main points

There is long standing concern among trade unionists about the impact on employment of mergers and buyouts. This has recently focussed on private equity activity, for example job losses at Gate Gourmet and Burton's Foods; as well as the aftermath of buy-outs at Birds Eye, Alliance Boots and the AA. There have been a number of surveys and research reports on the question of the employment impact of private equity but this has not produced many undisputed conclusions or areas of general consensus. The private equity industry disputes that there is a negative impact on employment of private equity ownership.

The main purpose of the *Transfer of Undertakings (Protection of Employment) Regulations* (TUPE) was to remedy the position in common law which meant that when a business was sold as a going concern the employment contracts of all the workers were automatically terminated. The TUPE regulations preserve these contracts and make the buyer responsible for them to the same extent that the seller had been. The regulations do not generally apply to share transfers since the identity of the employer, and hence the contracts of employment remain unchanged.

Private equity buy-outs are share transfers. The Bill proposes that such share transfers should be covered by some of the provisions in TUPE that support and underpin the preservation of employment contracts. Collective agreements between recognised trade unions and employers would also be protected in the same way. The Bill does not define precisely how substantial the transfer should be or which companies would be covered. However, a power is included for ministers to make regulations providing this detail.

There are important rights in TUPE to information and consultation. The Bill proposes that before a private equity transfer is completed these and other enhanced rights should be extended to employees. In addition, any failure by parties to the transfer to ensure that employees have been informed and consulted would allow those employees to apply to the High Court for an injunction to prevent the transfer from proceeding.

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I The Bill

A. Defining the area of application

One of the most acutely disputed issues between business and trade unions is the impact of private equity on employment. In general, not all forms of private equity buy-out generate concerns about negative employment effects. This question goes to the heart of the Bill's proposals which leave the detail to secondary legislation. There are two separate issues: defining the kind of transaction; and defining the entities that take part in the transaction.

The key focus of the Bill is "equity transfers" – the acquisition of a substantial proportion of shares by a private equity company. The full detail of the Bill's area of application is left open for the Secretary of State to provide for in regulations made under powers given in Clause 6 of the Bill.

Clause 1 states that:

> For the purposes of this Act, there is an "equity transfer" if an employer is a body corporate and a substantial shareholding in the employer is disposed of, transferred or acquired by a private equity company.

Clause 1, paragraph 4 states that the term:

> "private equity company" has such meaning as may be prescribed by the Secretary of State in regulations made by statutory instrument

In non-legal language the term "private equity" covers a very wide range of businesses. It may be difficult to define with legal certainty which companies should be caught by the Bill's provisions. Various approaches are possible.

There are a number of ways in which the area of application for the proposed rights could be defined in regulations. Existing company law definitions of size could be a source of analogies, as might the "main purpose test" in tax law.

a. Business size

Legislation may be drafted to exclude certain businesses, such as small firms, on the basis of their turnover or number of employees. For example, section 249 of the *Companies Act 1985* states that a company is 'small' if it satisfies at least two of the following criteria:[1]

1. Aggregate turnover not more than £5.6 million net (or £6.72 million gross)
2. Aggregate balance sheet total not more than £2.8 million net (or £3.36 million gross)]
3. Aggregate number of employees not more than 50

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[1] Sections 382(3) and 466(4) of the *Companies Act 2006* which will supersede section 249 of the *Companies Act 1985* provides the same definitions for small and medium sized companies respectively.

Under the Act a medium-sized company must satisfy at least two of the following criteria:

1. Aggregate turnover not more than £22.8 million net (or £27.36 million gross)
2. Aggregate balance sheet total not more than £11.4 million net (or £13.68 million gross)
3. Aggregate number of employees not more than 250.

b. The "main purpose" test

The concept of "main purpose" appears frequently in the UK tax code. It has become a key concept in anti-avoidance legislation, which now uses a standard formulation. By this, the desired tax treatment is only available if a reduction in tax is not "the main purpose, or one of the main purposes" of a course of action or state of affairs. The same formulation is also used in provisions referring to "main object" and "main reason".

c. Evidence of impacts

Another influence in formulating regulations to define the term "private equity company" could be academic surveys on the impacts of buy-outs on employment in subsequent years after the buy-out.

For example, research undertaken by Nottingham University Business School into the employment impacts of buy-outs suggests that there is a distinction to be drawn between management buy-outs (MBOs) and management buy-ins (MBIs). This was summarised as follows in a report by the Work Foundation:

> … there are important distinctions between MBOs (management buyouts, where PE is used to back an incumbent management team) and MBIs (where external investors impose a new management).[2]

Various surveys conducted into the question of private equity and employment are included in the select bibliography in the Appendix.

B. Employment protection

Where there is an "equity transfer" as defined, the Bill extends rights to employees by applying selected provisions of the *Transfer of Undertakings (Protection of Employment) Regulations 2006 SI No.246* (TUPE).

Clause 2 extends various employment protection provisions from TUPE to cover equity transfers such as the provisions on automatically unfair dismissals.[3] Paragraph (1) imports some of the TUPE provisions that protect contracts of employment.

Not all the provisions of TUPE are made to apply. For example, regulation 4(1) of TUPE states that:

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2 Phil Thornton, Work Foundation, *Inside the dark box: shedding light on private equity*, 2007

3 See section IV(A) below

> a relevant transfer shall not operate so as to terminate the contract of employment of any person employed by the transferor and assigned to the organised grouping of resources or employees that is subject to the relevant transfer, which would otherwise be terminated by the transfer, but any such contract shall have effect after the transfer as if originally made between the person so employed and the transferee

The Bill does not import this paragraph. In the case of most share transfers, contracts of employment are not disturbed as the legal identity of the employer remains the same as far as common law is concerned (TUPE would not therefore apply).[4]

However, there are other paragraphs of TUPE regulation 4 that restrict contractual variations (for example pay or other terms of employment) where these are attributable to the transfer. The Bill engages paragraphs 4 and 5 of TUPE regulation 4 which read as follows:

> (4) Subject to regulation 9, in respect of a contract of employment that is, or will be, transferred by paragraph (1), any purported variation of the contract shall be void if the sole or principal reason for the variation is—
>
> (a) the transfer itself; or
> (b) a reason connected with the transfer that is not an economic, technical or organisational reason entailing changes in the workforce.
>
> (5) Paragraph (4) shall not prevent the employer and his employee, whose contract of employment is, or will be, transferred by paragraph (1), from agreeing a variation of that contract if the sole or principal reason for the variation is—
>
> (a) a reason connected with the transfer that is an economic, technical or organisational reason entailing changes in the workforce; or
> (b) a reason unconnected with the transfer.

TUPE regulation 9 deals with variations of contract where transferors are subject to relevant insolvency proceedings. This is intended to relax TUPE in insolvency situations to facilitate rescue bids.

These provisions are clearly intended to address concerns expressed by trade unions about pay and conditions of work following buy-outs and reflect the general long standing theory that:

> "corporate change will lead to management breaking implicit agreements and transferring wealth from employees to new owners." This theory was developed in response to the similar wave of mergers and buyouts in the 1980s, when shareholders also made large gains from increased share prices.[5]

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4 Case law has revealed exceptions to this general position (*Millam v Print Factory (London) 1991 Ltd.* [2007] IRLR 526) which are discussed below.

5 David Hall, Public Services International Research Unit, UNITE, *Methodological issues in estimating the impact of private equity buyouts on employment*, 2007

Clause 3 protects collective agreements to the same extent as employment contracts are protected in the Bill. Paragraphs 4 and 5 of TUPE regulation 4 (quoted above) are made to apply "with the necessary modifications" to collective agreements with a recognised trade union.

C. Information and consultation

One of the key benefits provided by TUPE to employees is a set of enhanced information and consultation rights. These are contained in TUPE regulation 13. Regulations 15 and 16 set out remedies for a failure to inform or consult by the employer which allow complaints to be made to employment tribunals seeking compensation.

Clauses 4 and 5 extend these rights to cover the equity transfers which are the focus of the Bill, with adaptations and the following substantive extensions:

- The required steps to inform and consult with employees must be taken at an early stage – before it is decided that the equity transfer should take place.

- The onus will be on the parties to the transfer to ensure that the employer (ie the business whose shares are being transferred) in fact takes the necessary steps to inform and consult employees.

- A wider range and specificity of information extending 5 years after the transfer, covering:

> all relevant facts and matters (actual and anticipated) in relation to the period beginning with the date the information is provided and ending 5 years after the date of the proposed transfer, concerning the structure, economic and financial situation of the transferor, transferee and employer, the probable development of the employer's business and of production and sales, the situation and probable trend of employment, investments and substantial changes concerning organisation, introduction of new working methods or production processes, transfers of production, mergers, cut-backs or closures of undertakings, establishments or important parts thereof, and collective redundancies

- Assistance and training to help employees adapt to changes in the business following the transfer;

- Time, information and facilities for employees to arrange for: an expert study; prepare representations; present a formal opinion; and/or subsequent exchange of views, in respect of the implications of the proposal;

- Seek the agreement of employees to the proposed transfer prior to deciding that it should take place

- A High Court injunction will be available to employees to prevent a proposed transfer from taking place, where the requirements to inform or consult have not been satisfied.

II The TUPE Regulations

A. Provisions of TUPE

The *Acquired Rights Directive*[6] was adopted in 1977 and implemented in UK law by the *Transfer of Undertakings (Protection of Employment) Regulations 1981,* SI 1981/1794. These regulations were revoked and replaced by the *Transfer of Undertakings (Protection of Employment) Regulations 2006 SI No.246* (TUPE). The purpose of the Directive was to "safeguard employees' rights in the event of transfers of undertakings, businesses or parts of businesses". The rules also apply when a "service provision change" takes place (for example, where a contractor takes on a contract to provide a service for a client from another contractor). Where the directive or regulations apply:

- the contracts of employment of employees of the transferor (the seller) are automatically transferred to the transferee (the buyer). Thus, employees transferred from one employer to another continue to receive the same pay and conditions of service and their length of service is not interrupted by the transfer (regulation 4). Occupational pension schemes are not covered by the regulations (regulation 10). The Government has, however, issued guidance designed to ensure that where public sector staff are transferred, their pension rights after the transfer should be "broadly comparable" to those enjoyed before.[7] The *Pensions Act 2005* also addresses transfer of undertakings.[8]

- any collective agreement made between the transferor and a recognised trade union is automatically transferred to the new employer (regulation 5).

- any employee dismissed because of the transfer is considered to have been unfairly dismissed unless the reason for his dismissal is "an economic, technical or organisational reason entailing changes in the workforce" (regulation 7).

- employee representatives must be informed and consulted before the transfer occurs (regulation 13). TUPE originally stated that consultation was only necessary where there was a recognised trade union. But, following a ruling in the European Court of Justice on 8 June 1994 that this failed to implement the Directive properly,[9] the regulations were amended so that - in respect of transfers occurring on or after 1 March 1996 - employers had a duty to consult either a recognised trade union or elected representatives of the affected employees.[10] This ensured that consultation occurred even where there was no recognised trade union, but it also enabled employers to by-pass trade unions should they so wish. The Labour Government

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6 77/187/EEC

7 The guidance is currently contained the Cabinet Office's *Staff Transfers in the Public Sector: Statement of Practice*, issued in January 2000

8 *Pensions Act 2004*

9 *Commission of the European Communities v United Kingdom of Great Britain and Northern Ireland*

10 *The Collective Redundancies and Transfer of Undertakings (Protection of Employment) (Amendment) Regulations 1995*, SI No 2587

introduced a further amendment, applying to transfers occurring on or after 1 November 1999, which provides that where employers do recognise a union they must consult that union.[11]

TUPE does not protect terms and conditions for all time. It is open to the new employer, as it would have been to the old, to try to renegotiate terms and conditions and to make employees redundant.

The new regulations were made under powers in section 2(2) of the *European Communities Act 1972*, and section 38 of the *Employment Relations Act 1999*. Fuller details of how TUPE works were given in guidance (by the DTI now BERR - the Department for Business, Enterprise and Regulatory Reform) on the revised 2006 regulations.[12]

The main changes introduced by the 2006 regulations were described as follows:

> **Main Changes in the 2006 TUPE Regulations**
>
> The 2006 Regulations introduce:
>
> - a widening of the scope of the Regulations to cover cases where services are outsourced, insourced or assigned by a client to a new contractor (described as "service provision changes") ;
> - a new duty on the old transferor employer to supply information about the transferring employees to the new transferee employer (by providing what is described as "employee liability information") ;
> - special provisions making it easier for insolvent businesses to be transferred to new employers ;
> - provisions which clarify the ability of employers and employees to agree to vary contracts of employment in circumstances where a relevant transfer occurs ;
> - provisions which clarify the circumstances under which it is unfair for employers to dismiss employees for reasons connected with a relevant transfer.
>
> The rights and obligations in the 1981 Regulations remain in place, though the 2006 Regulations contain revised wording at some points to make their meaning clearer, as well as reflecting developments in case law since 1981.

B. Share transfers

Most commercial companies are limited by shares. This means that when the business is set up as a limited company a share capital is raised and individuals are given shares. A BERR leaflet explains this as follows:

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11 *The Collective Redundancies and Transfer of Undertakings (Protection of Employment) (Amendment) Regulations 1999*, SI 1999/1925

12 BERR, *Employment rights on the transfer of an undertaking: a guide to the 2006 TUPE regulations for employees, employers and representatives*, March 2007

1. What is share capital?

> When a company is formed, the person or people forming it decide whether its members' liability will be limited by shares. The memorandum of association (one of the documents by which the company is formed) will state:
>
> • the amount of share capital the company will have; and
> • the division of the share capital into shares of a fixed amount.
>
> The members must agree to take some, or all, of the shares when the company is registered. The memorandum of association must show the names of the people who have agreed to take shares and the number of shares each will take. These people are called the subscribers.[13]

A limited company interacts with the general system of law as a distinct "legal personality". This means that it can sue or be sued in the courts and enter into contracts with other parties in the same way that an individual can. After the initial shareholding has been established, the company may issue more shares and/or individuals may sell their shares to other individuals or companies. The sale of shares will not change the legal personality of the company, merely its beneficial ownership.

One of the main difficulties with the TUPE regulations has been ascertaining whether or not they apply to any particular transfer. As the Government's September 2001 consultation document said:

> 5. The scope of the legislation is the most extensively debated and litigated aspect of the current Regulations. Ideally, everyone should know where they stand, so employers can plan effectively in a climate of fair competition and affected employees are appropriately protected as a matter of course. In the past, however, this has not always been the case. [14]

It is fairly clear that when one company sells a business to another as a going concern, TUPE does apply. Before TUPE, such transfers ended the existing contract of employment, as there was a new employer. TUPE does not apply to transfers of shares as the same company continues to be the employer and contracts of employment are not ended.

The Bill's broad intention is to make TUPE apply in leveraged buy-out situations. Similar proposals were made recently by the trade unionist Jack Dromey in an article in the Financial Times.[15] The proposals outlined by Jack Dromey were as follows:

- Private equity deals are share transfers that should be covered by TUPE so that contracts of employment are protected

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13 BERR, *Share Capital GBA6 Version 8*, February 2007

14 Employment Relations Directorate, DTI, *Transfer of Undertakings (Protection of Employment) Regulations 1981 (TUPE): Government proposals for reform: public consultation document*, September 2001

15 Jack Dromey, "Protect workers from the private equiteers", *Financial Times,* 3 July 2007

- The right to information and consultation before a private equity deal is completed should be extended to workers and their trade unions
- Compensation for workers resulting from increased debt related risk similar to pension funds and investors

Share transfers do not change the identity of the employer. In terms of preserving the contract of employment itself, making share transfers subject to TUPE could be unnecessary protection. The effect of TUPE is to reverse the position at common law when the legal identity of the employer changes. Without TUPE the employment contract would fall with a change in the identity of the employer. Share transfers or buy-outs leave employment contracts undisturbed in legal terms. If the share transfer did change the legal identity of the employer then TUPE would probably come into effect and the transaction would no longer be just a share transfer.

Having said this, in a private equity buy-out, the management of the employer business may change or the existing management may acquire a degree of ownership. This may herald substantial redundancies or other reorganisation that affects workers. Whilst extending TUPE to share transfers would in most cases make little difference to the contractual position of workers, there are a collection of rights contained in TUPE that extend beyond merely the protection of contracts of employment and would provide greater protection for workers in a buy-out situation.

An important right provided by TUPE relates to unfair dismissal. Dismissal of an employee for a reason connected with a sale or other transfer of a business is automatically unfair dismissal, whether it takes place on, before or after the transfer unless it is for an "economic, technical or organisation reason involving changes in the workforce". There are also wide ranging rights to information and consultation contained in regulation 13 of TUPE which extend beyond the normal ongoing rights to consultation. There are also general information and consultation rights under the information and consultation regulations (ICE) although they are framed in a way that may not specifically envisage the buy-out situation.

Although in general a share transfer will not change the identity of the employer, there was a recent rare case where TUPE was held to apply in the case of a share transfer. In the Court of Appeal judgement in the case of *Millam v Print Factory (London) 1991 Ltd.* [2007] IRLR 526, CA the share transfer was between two printing companies: McCorquodale; which acquired Fencourt Ltd. The employee concerned had been employed by Fencourt Ltd but claimed that he should be treated as an employee of McCorquodale by virtue of TUPE. The Tribunal had held:

> … we are not satisfied that the Claimant remained an employee of Fencourt Ltd, discrete from McCorquodale, after McCorquodale's acquisition in 1999. The Share Sale Agreement gave the superficial impression that no TUPE transfer had occurred. The buyer of the shares did far more than a simple shareholder would have done following a simple sale, or in our experience, a parent company of a subsidiary would have done in similar circumstances. In particular, McCorquodale's handling of a significant element of the management of Fencourt set its actions apart from those of a mere shareholder. It made key decisions in relation to Fencourt's workload, it attempted to bring about contractual changes and it ultimately made the decision to put Fencourt into Administration. In all

> those circumstances, we are satisfied that on 2 November 1999 there was a TUPE transfer of Fencourt Ltd to McCorquodale.

This decision was overturned in the Employment Appeal Tribunal but then reinstated by the Court of Appeal. The key test outlined in the Court of Appeal related to control of day to day activities. The evidence:

> demonstrated that McCorquodale had taken over the day-to-day management of Fencourt's business.

III Private Equity and Employment

A. Employment effects of leverage buyouts in the UK

[By Ed Beale, Economic Policy and Statistics Section]

While there is a relative wealth of literature analysing the employment effects of company mergers in recent years, the literature specifically on leverage buyouts (LBOs) is not so widespread. One of the most recent is by the Centre for Management Buy-Out Research (CMBOR) at Nottingham University Business School. They estimated the effect on employment of different kinds of LBOs using a panel of 1,350 UK LBOs[16] observed over the period 1999 to 2004.[17]

Their research found that, on average, in cases of management buy-outs (MBOs) employment dipped initially after the buyout but rose, consistently, in subsequent years. In contrast, for management buy-ins (MBIs), where external investors impose a new management, the employment level fell in the first year and remained below the pre buy-out level. They estimated that, after six years, employment in MBOs had increased by approximately 36% (from the pre buy-out employment level) but had fallen on average by approximately 18% over the same period in cases of MBIs.

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16 This included both private equity backed and non-private equity backed deals.

17 Wright, M. et al, *Private Equity and Buy-outs: Jobs, Leverage, Longevity and Sell-offs*, Centre for Management Buy-out Research, July 2007

Table 1

Post MBO and MBI changes in employment

	Years relative to year of deal					
	t + 1	t + 2	t + 3	t + 4	t + 5	t + 6
MBOs						
Employment change (a)	-2%	3%	7%	21%	26%	36%
% deals with positive change	60%	65%	66%	64%	62%	61%
% deals with negative change	36%	33%	32%	34%	36%	36%
% deals with no change	4%	2%	2%	2%	2%	2%
MBIs						
Employment change	-10%	-10%	-11%	-3%	-5%	-18%
% deals with positive change	58%	60%	59%	56%	56%	65%
% deals with negative change	37%	37%	38%	39%	42%	35%
% deals with no change	6%	4%	3%	5%	2%	0%

Note: (a) % changed compared with t - 1 where t is the year of the deal. For example, an employment change of 36.2% 6 years after the deal indivates that employment grew by 36.2/7 = 5.2% per annum.

Source: Centre for Management Buy-out Research

Notably, while the above table shows an overall fall in employment for MBIs, most of the individual MBI deals showed a positive change in employment in each of the first six years after the buy-out. This would suggest that where there is a negative employment effect it is generally larger in scale, or in larger firms, than buy-outs where positive employment changes were recorded.

A second paper, based on the same dataset, estimated changes in employment following LBOs compared with non buy-out firms (rather than individual firms' pre buy-out position).[18] This found that there was no significant effect of LBOs overall on employment. However, the direction of any employment effect remained different (although relatively small) when comparing non-LBOs with MBOs and MBIs respectively; the study indicated that, overall, employment growth was 0.51% higher for MBOs (compared with non-LBO firms) but wage growth was 0.31% lower. In contrast, for MBIs employment growth was 0.81% lower than in companies which had not undergone a buy-out (and wage growth was 0.97% lower).[19]

The reason for, on average, MBOs and MBIs displaying a different employment effect is attributed by the former study to a number of reasons including: post-MBI restructuring being greater than for MBOs; MBI performance being below that for MBOs; and, a higher failure rate of MBIs compared with MBOs. The study does counter the relatively negative picture of MBIs by noting that the actions taken to restructure the business upon buy-out, including labour shedding, "appear" to reduce the likelihood that the firm will subsequently fail leading to even higher loss of employment.

A second survey, published in April 2007 by the *Financial Times* looked specifically at private equity buyouts. It found that of the largest 30 buyouts in the UK in 2003 and

18 Wright, M. & Amess, K., "The Wage and Employment Effects of Leveraged Buyouts in the UK", *International Journal of the Economics of Business*, Vol 14, No 2, July 2007, pp179-195

19 *ibid.* p191

2004, overall jobs were more likely to have been gained than lost following private equity backed buy-outs; total gains in employment were 49,198 while reported total losses in employment were 12,468 indicating a net increase in jobs of 36,730.[20] However, the article did note that "this crude statistic masks a wide variety of different outcomes and management decisions".

A recent report by the Public Services International Research Unit (PSIRU) at the University of Greenwich suggests there were a number of methodological problems with surveys attempting to analyse the employment effects of such buy-outs.[21] About the *Financial Times* data it stated:[22]

> The great majority of the reported employment changes arise from mergers and acquisitions, not from organic growth; the survey has to rely on unverified data from companies, and some companies, including some with known job losses, excluded themselves from the survey.
>
> […]
>
> [It] is not strictly accurate to say that "PE backed deals are more likely to increase employment". Out of the 30 companies, 10 gave the FT figures showing an increase, 2 said there was no change, 12 gave the FT figures showing there had been reductions, and 6 gave no information. It would be more correct to say that the buyouts were slightly more likely to reduce employment, but the increases were larger than the losses.

The PSIRU report found that the survey by the CMBOR was:[23]

> The soundest research, by Amess and Wright, is compatible with the hypothesis that the net contribution of private equity groups (as distinct from internal managers) is to deliver reductions in wages, and to deliver employment levels lower than the companies' potential, and that these are the mechanisms of an "opportunistic transfer of wealth from employees to new owners".

However, it does highlight a number of issues with the CMBOR study:[24]

> Firstly, the dataset includes management buyouts (MBOs) even where no private equity fund was involved […] This may have a significant effect on interpretation of the results, because Amess and Wright find that it is the subset of MBOs which accounts for the positive contributions to employment levels: they do not report if this is still true for the subset of MBOs where PE funds are involved. It is thus possible that the results for MBOs, and for LBOs overall, overstate employment gains compared with the subset of MBOs including PE funds.

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20 "Private equity deals that cement growth", Financial Times, 1 April 2007. Data are available at: http://www.ft.com/cms/57636bb0-e066-11db-8b48-000b5df10621.xls

21 Hall, D., *Methodological issues in estimating the impact of private equity buyouts on employment*, May 2007

22 *ibid.* pp8-9

23 *ibid.* p9

24 *ibid.* p9

> Secondly, in the control set of companies not subject to LBOs, Amess and Wright excluded firms which showed growth in assets of more than 100% in any one year, in order to exclude the effects of mergers and takeovers […] The rationale for this is not explained, but it means that the growth of the non-LBO sample is deflated by the exclusion of the effect of acquisitions, whereas growth by acquisitions made by the LBOs themselves appears to remain included. This second issue may lead to over-estimating employment growth in LBOs relative to other firms – acquisitions and disposals account for a large proportion of the employment effects observed in the data from the FT survey, for example […].

Some contrasting findings to the *Financial Times* and CMBOR studies were provided in a recent study led by Harvard Business School for the World Economic Forum meeting at Davos in January 2008 which indicated that, overall, the employment effect of private equity takeovers on the target firm was negative.[25] The study looked at 5,000 US firms acquired in private equity transactions during the period from 1980 to 2005. It found that the workplaces of firms taken over by private equity had lower net job growth of approximately 10% over the five years after takeover compared with if they had developed in the manner of similar workplaces not bought by private equity (although the *rate* of job growth after five years was "slightly" higher).[26] This was accounted for by initial higher "gross job destruction as the new private equity-backed owners shed presumably unprofitable segments of the target firms".

However, the report did find that bigger job losses at target establishments in the wake of private equity transactions were at least partly offset by bigger job gains in the form of 'greenfield' job creation[27] by target firms.[28] Overall, however, the report concluded that the net impact on *existing* establishments (of a private equity takeover) is "negative and substantial".[29]

A further report by the PSIRU at the University of Greenwich commended the Harvard study stating:[30]

> [Its] approach does not suffer from the methodological problems of the private equity association surveys. It provides data on changes in employment in actual workplaces, and, separately, employment changes in the firm as a whole, including the effects of acquisitions and disposals. It excludes venture capital companies and management buyouts where private equity was not involved. It covers all private equity buyouts in the USA since 1980, not a selected sample. It provides a set of 'control' firms with similar characteristics for meaningful comparisons. The main limitation is that it covers only the USA.

There are a number of industry-produced/affiliated reports on the economic impact of private equity (as mentioned in the above quote) which are not discussed in this research paper.[31]

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25 WEF, *The Global Economic Impact of Private Equity Report 2008*, January 2008
26 *ibid*., p54
27 ie job creation at new establishments opened by target firms following take-over.
28 *ibid*., p44
29 *ibid*., p54
30 Hall, D., *Private equity and employment – the Davos/WEF/Harvard study*, February 2008

IV Other relevant employment rights

A. Employment protection

The normal qualifying period of continuous employment for eligibility for unfair dismissal rights was reduced to **one year** in 1999.[32] This requirement was previously two years. Nevertheless, a dismissed employee who has not completed a year's service can claim compensation if they can bring their claim under one of the headings which do not depend on completion of a period of qualifying service, such as discrimination cases. All forms of discrimination protection apply without qualifying periods. There are also cases in which dismissal is automatically unfair dismissal such as a dismissal for a reason connected with a sale or other transfer of a business covered by TUPE. Most, but not all, dismissals which are made automatically unfair by relevant legislation require no qualifying period of service at all.

In normal unfair dismissal cases, an employment tribunal would determine if the dismissal was fair or unfair "in the circumstances" or "in accordance with equity and the substantial merits of the case". Employment rights legislation provides that in various specified cases the tribunal will be obliged to hold that the dismissal was unfair if particular reasons for dismissal are established. Colloquially, these are referred to as cases of "automatically unfair" dismissal.

The provisions for automatically unfair dismissal can be found mainly in sections 99 – 108 of the *Employment Rights Act 1996* (ERA). Others are found elsewhere in legislation that has conferred separate employment rights.

For example, the normal one year qualifying period is reduced to one month if the dismissal is by reason of a requirement or recommendation specified under section 64(2) ERA, for example contact with dangerous chemicals or exposure to harmful radiation. Also, under section 100 of the *Employment Rights Act 1996* dismissal is automatically unfair in six specified health and safety cases.

In addition to the various health and safety grounds, there are various cases where a dismissal will be automatically unfair, for example dismissal on grounds of "assertion of a statutory right".[33] Other examples include: dismissal for making (or proposing to make) an application for flexible working arrangements; improper selection for redundancy; dismissal for taking time off work for jury service; and (in addition to the normal sex discrimination protection) dismissal for any of the reasons or circumstances set out in secondary legislation concerning pregnancy, childbirth, maternity or maternity or parental leave or taking time off for ante-natal care.

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31 See for example:
BVCA, *The Economic Impact of Private Equity in the UK 2007*, February 2008
EVCA/CEFS, *Employment Contribution of Private Equity and Venture Capital in Europe*, November 2005
NVCA/Global Insights, *The Economic Importance of Venture Capital Backed Companies to the U.S. Economy*, 2007

32 *Unfair Dismissal and Statement of Reasons for Dismissal (Variation of Qualifying Period) Order 1999*, SI 1999/1436 amending section 108 of the *Employment Rights Act 1996.*

33 Relevant statutory rights for this purpose are defined in section 104(4) ERA

B. ICE Regulations

European *Directive 2002/14/EC* requires Member States to establish national systems for informing and consulting employees in undertakings with at least 50 employees. Countries that did not already have a "general, permanent and statutory system of information and consultation of employees" (i.e. the UK and Ireland) were able to limit the directive's application to undertakings with at least 150 employees until 23 March 2007 and to undertakings with at least 100 employees until 23 March 2008.[34]

Provision for implementation is contained in the *Employment Relations Act 2004* under which the *Information and Consultation of Employees Regulations 2004* SI No. 3426 (ICE) were made. The ICE regulations came into force on 6 April 2005. They provide that an employer must establish information and consultation procedures when 10% of the workforce formally requests an Information and Consultation (I&C) agreement, or if the employer voluntarily chooses to start this process. Enforcement and resolution of complaints takes place through the Central Arbitration Committee (CAC). If the employees wish to remain anonymous they can make this request via the CAC or a Qualified Independent Person. If the employer has a pre-existing agreement on information and consultation and this carries employee approval then that procedure will continue. If no agreement exists, or an existing agreement lacks employee support, then a new one must be negotiated. The employer may hold a ballot to ascertain the employee support for the request to negotiate a new agreement.[35]

The parties will be free to negotiate an agreement which best suits their needs and circumstances, in light of government guidance. If there is a failure to conclude a negotiated agreement then the statutory provisions based on Article 4 of the directive apply. This involves the setting up of an I&C committee elected by the employees. The employer then has various duties to inform and consult the employees via the committee. Complaints about any failure on the part of the employer to establish I&C procedures or complaints about the operation of established procedures will be heard by the CAC.

The ICE Regulations are quite complex and include many specific definitions and information on what constitutes an I&C agreement; the meaning of the term 'undertaking'; calculations on numbers of employees and the meaning of the term 'employee'; how the regulations apply to temporary, agency or contract workers; election or appointment of representatives; the setting up of consultation arrangements; and resolution of complaints by the CAC. Further information can be found in the government guidance to the Regulations.[36]

The Regulations apply to undertakings with over 150 employees from 6 April 2005; over 100 employees from 6 April 2007; and over 50 employees from 6 April 2008. The regulations do not apply to undertakings with fewer than 50 employees.

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34 *Directive 2002/14/EC of the European Parliament and of the Council of 11 March 2002, establishing a general framework for informing and consulting employees in the European Community*

35 The Draft Regulations are available on the DTI website

36 BERR, Information and Consultation

There are three categories of information that employers who are subject to the standard provisions must provide to I&C representatives. These are information on:

- The recent and probable development of the undertaking's activities and economic situation
- The situation, structure and probable development of employment within the undertaking
- Decisions likely to lead to substantial changes in work organisation or in contractual relations

Employees who act as negotiating or I&C representatives have certain rights and protection under the legislation, including the right to take reasonable time off during working hours to perform their functions as representatives.

C. Other information and consultation rights

There are also consultation rights for workers under the *Collective Redundancies Directive 75/129/EEC* and the *European Works Councils Directive 94/45/EC*. Under the *Collective Redundancies Directive,* employers are required to consult appropriate representatives of the workforce when they propose making collective redundancy dismissals. A collective redundancy situation arises where the employer proposes to dismiss as redundant at least twenty employees at one establishment within a ninety day period. The *European Works Councils Directive* covers undertakings or groups of undertakings with at least 1,000 employees located within the European Economic Area (EEA) and at least one establishment employing a minimum of 150 workers in each of two Member States. Either at management's own initiative or at the request of employees, these undertakings must establish a European Works Council (EWC) or another procedure for informing and consulting employees. The statutory fallback EWCs must meet once a year for an information and consultation meeting covering various specified topics.

Appendix: Private equity and employment - selected bibliography (2005-2008)

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