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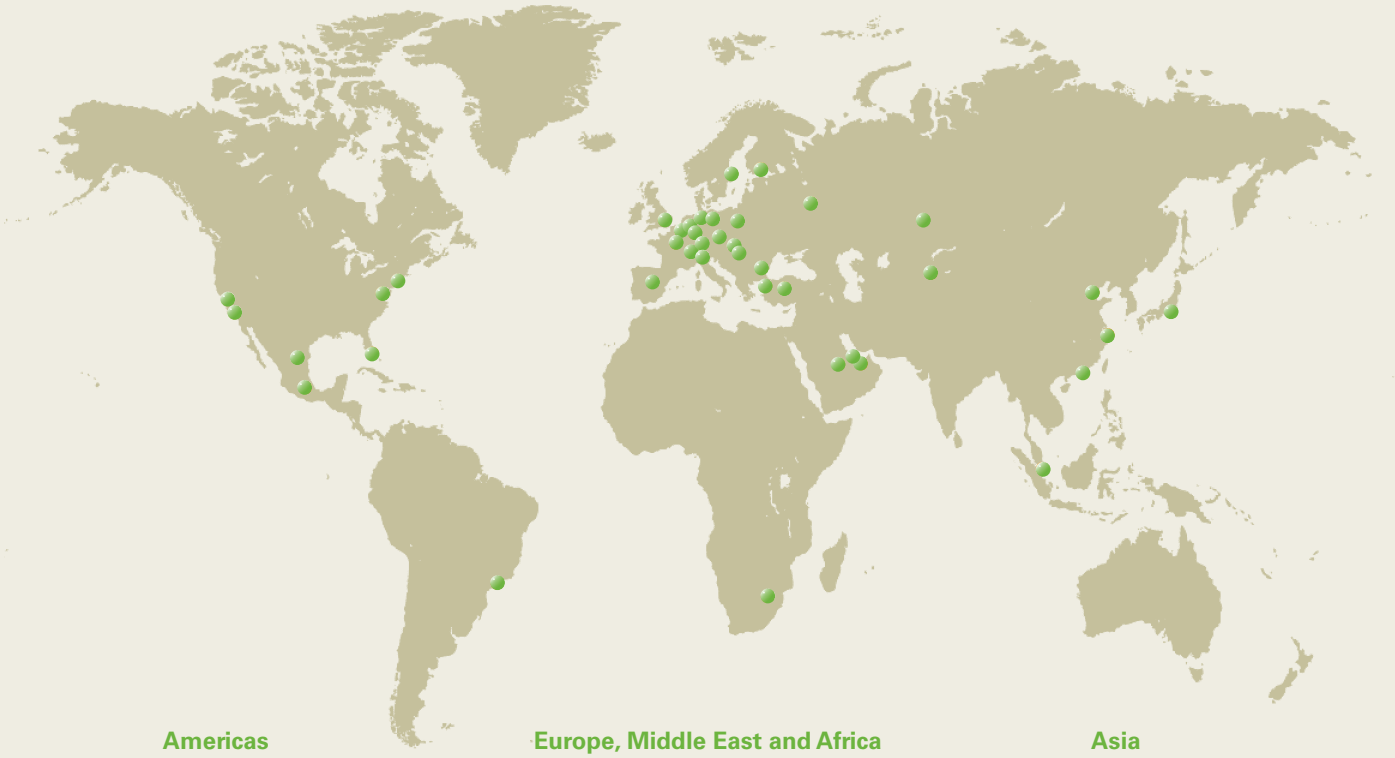

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Business transfers in the UK and Japan: a comparison

The sale of a business typically involves a myriad of employment issues. The key employment issues throughout the world will usually fall into two fundamental categories which need to be considered from the time the transaction is contemplated and not, as is often the case, left until the transaction is well developed.

This is particularly important in cross-border transactions involving multiple jurisdictions with very differing requirements. The two key issues are:

(i) does the employees' employment relationship with the seller transfer automatically by law or, some other way, to the buyer on completion with their continuity of service and terms and conditions of employment preserved; and

(ii) must the employees working in that business be informed and consulted in advance about the transaction?

Following a client seminar on this topic presented recently by the employment specialists in White & Case's offices in London and Tokyo jointly, this article compares the position regarding business transfers in the UK and Japan. While the legislation and requirements differ in these two jurisdictions, the commercial considerations remain similar.

Automatic vs. individual transfer principles

In Europe, the Acquired Rights Directive ("**ARD Directive**") governs the automatic transfer of employees on a business sale. In the UK, the ARD Directive is implemented through the Transfer of Undertakings (Protection of Employment) Regulations 2006 ("**TUPE**"). TUPE provides a level of protection for employees in the UK which is as high as any other jurisdiction within or outside Europe. It is not possible to contract out of TUPE and any failure to comply, or any attempt to manipulate or limit its application, will likely result in claims by the affected employees and/or their representatives. It is for these reasons that parties to transactions will often seek to build indemnity protection against TUPE related liabilities into the sale documentation.

In broad terms, TUPE applies where there is a "relevant transfer" (also known as a business transfer). A "relevant transfer" arises where there is a transfer of an undertaking, business or part of an undertaking or business, situated in the UK immediately before

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the transfer, to another person – i.e. the business must be an economic entity that retains its identity post-transfer. By way of example, where a Japanese company wishes to acquire a UK business, TUPE will apply. When TUPE applies, the employment of all employees who are assigned to the business being transferred will automatically transfer to the buyer on their existing terms and conditions of employment (together with all rights, powers, duties and liabilities, which arise under or in connection with the employment contracts), unless they object to the transfer. It is not possible for the seller or the buyer to 'pick and choose' which employees will or will not transfer.

By comparison, there is no specific equivalent legislation in Japan (or, indeed, in most other non-EU jurisdictions including, for example, Australia, Canada, China and Mexico). In Japan, the Japanese Corporate Act prescribes two limited circumstances in which all employment rights and obligations will transfer automatically to a buyer, namely where there is a merger ("Gappei") or a demerger ("Bunkatsu").

In a case of a merger in Japan, the effect will be the same as in the UK, that is, in general, all employees will transfer to the buyer on their existing terms and conditions of employment and it will not be possible to 'pick and choose' who transfers. Likewise, in the event of a demerger, employees who are primarily part of the business division that is being transferred will automatically transfer to the buyer on their existing terms and conditions of employment. As in the UK, all rights, powers, duties and liabilities arising under the contracts of employment will also transfer. The Japanese concepts of a merger and demerger should therefore be seen as equivalent to the UK's concept of a "relevant transfer" as far as any automatic transfer principle is concerned.

In the case of a demerger, if the demerging company arbitrarily seeks to exclude certain employees from the group of employees who are primarily part of the business division that is transferring, such employees will have the right to object to such exclusion and will be entitled to transfer to the buyer. Likewise, in the UK, where a seller seeks to deliberately reorganise employees so that they are no longer assigned to the business being transferred, this will not escape the effects of TUPE. In addition, in both Japan and the UK, the demerging company/the seller and the buyer can also commercially agree to transfer any employees who are not primarily engaged in the transferring business. However, if these employees raise any objection to being transferred, they will be entitled to remain employed by the demerging company/the seller.

Separate from the concepts of a merger or demerger, Japan also has its own concept of a business transfer ("Jigyo-Jyoto"). But in Japan, the effect of a business transfer will depend on what is commercially agreed upon between the parties. In theory, it is possible to 'pick and choose' which employees transfer but if some employees are arbitrarily excluded, the court may deem those employees to have also transferred on the grounds of unfair labour practices or a breach of public policy. In practice, it is common in Japan to ensure that all employees will transfer as part of the commercial arrangement. To this end, separate from the automatic transfer principle, an individual transfer principle will apply in a business transfer scenario, whereby the employment relationship is transferred with the individual employee's consent.

In the UK, such individual transfers do also occur, of course, in circumstances where TUPE would not otherwise apply or in order to transfer any employees who would not otherwise be transferred under TUPE.

Information and consultation obligations

In the UK, TUPE imposes a specific duty on both the buyer and the seller to inform and, where required, consult with appropriate employee representatives concerning the transfer. In addition, the seller is also obliged to provide written information to the buyer about the identities of all transferring employees and all their related employment rights and liabilities.

In Japan, the applicable information/consultation obligations (if any) will depend on the structure of the transaction. There are no specific regulations that require the seller or buyer to inform or consult with employees on a merger or a business transfer. However, from a practical and employee relations perspective, it is common for the seller to inform and consult with employees, employee representatives and/or labour unions. In the case of a business transfer, it will be necessary to obtain individual employee consent to the transfer and so information and consultation is more likely in this scenario.

However, in the event of a demerger in Japan, there is specific legislation, in the form of the Act on the Succession to Labour Contracts upon Demerger ("**Demerger Act**"), which requires the seller to provide certain information to employees and labour unions (as explained below). In contrast to the UK, this is only an obligation to inform and only an obligation on the seller- there is no statutory obligation to consult and no statutory obligation on the buyer.

Who must be informed/consulted with and what must they be informed/consulted about?

TUPE requires that "appropriate representatives" must be informed and consulted with. For these purposes, "appropriate representatives" means:

(i) representatives of an independent trade union recognised by the employer; or

(ii) employees elected by the affected employees as their representatives where no union is recognised.

If the employee representatives are required to be specifically elected for the consultation process, it is the seller's obligation to arrange the election process. The seller can decide how many representatives there will be, but the number must be representative of the transferring employees. Electing representatives will involve a process of inviting nominations and then organising a secret ballot if more than one nomination for any position is received.

In the case of a demerger in Japan (being the only circumstance in which there is a statutory information obligation), the following categories of people must be informed about the transaction:

(i) employees who are primarily engaged in the transferring business;

(ii) employees who are not primarily engaged in the transferring business but are being targeted as additional employees to be transferred to the buyer; and

(iii) labour unions which have entered into collective bargaining agreements with the demerging company.

In the UK, once the appropriate representatives are in place, a distinction is made between information and consultation obligations. The appropriate representatives must be:

(i) informed about the transfer (broadly speaking, the fact it is taking place, when it is taking place, and the reasons for it taking place); and separately,

(ii) consulted on any measures envisaged. In this context, "measures" means any plans envisaged to be acted upon by either the buyer or the seller such as proposed dismissals, restructuring, redundancies, or changes to terms and conditions of employment. If there are no "measures" proposed then, in theory, consultation is not required.

By comparison, in Japan, there is no statutory requirement for consultation, as such, in any case. The Demerger Act requires the seller to only inform employees and labour unions about certain things, including, the target business, the effective date of the transaction, details of the buyer, the scope of the transferred employees and the deadline for any objection.

Changing terms and conditions of employment

Regardless of the jurisdictions in which a transaction is taking place, it is a common feature of business transfers for the buyer to want to make changes to the terms and conditions of the transferring employees, more often than not, in order to bring them in line with the terms and conditions of the buyer's existing employees. There is clear business and practical sense in doing so, however, there are restrictions on the extent to which a buyer can implement such changes.

In the UK, any purported variation of the terms and conditions of employment under which the transferring employees are employed is void if the sole or principal reason for the change is the transfer itself unless: (i) the sole or principal reason is an economic, technical or organisational ("**ETO**") reason entailing changes in the workforce (provided that the employer and employee agree upon the variation); or (ii) the terms of the contract permit the variation to be made. There is no statutory definition of an ETO reason, but it is clear from the case law that the reason must be concerned with the day-to-day running/continued viability of the business. Case law in the UK has also interpreted "entailing changes in the workforce" to mean changes in the numbers employed or changes in the functions performed by employees. Recent changes made to TUPE include change of location within the meaning of an ETO reason entailing changes in the workforce. Guidance from the Department for Business Innovation and Skills in the UK suggests that an ETO reason could include reasons relating to profitability or market performance, the nature of the equipment or production processes which the buyer operates, or to the management or organisational structure of the buyer's business.

Where there is no ETO reason for a change, other options open to a buyer will include, checking to see whether the employees' contracts authorise a change, consulting with and obtaining individual employee consent or terminating employees and re-hiring them on the new terms. These options may even form

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part of the commercial terms of the transaction, and it would not be unusual, for example, for a provision to be included in a sale agreement providing for the termination of contracts of key employees by the seller and the offer of new contracts to those key employees by the buyer (although there is, of course, an increased risk of unfair dismissal claims in these cases).

In Japan, there is no equivalent to an ETO reason and an employer in Japan will need to comply with the normal rules for making changes to terms and conditions. Where there is either a merger or demerger, if the proposed changes are disadvantageous to the employees, the seller and the buyer will need to approach the changes in one of the following ways:

(i) obtain employee consent to the changes (Article 9 of the Labour Contract Act);

(ii) reach agreement with labour unions as to the changes; or

(iii) change the work rules which bind the employees. According to Article 10 of the Labour Contract Act, the factors to be taken into account in reviewing the validity of work rules are: the level of disadvantage, the need for changes to terms and conditions, the appropriateness of the new terms and conditions, and the status of consultation with employee representatives or labour unions. Where any changes are made to work rules, it is open to employees to challenge the validity of such changes and in these circumstances, it would be left to a court to rule on their validity.

Dismissals

In addition to wanting to make changes to terms and conditions of employment, it is also common for buyers to want to make dismissals, particularly in circumstances where the buyer does not require the number of employees who will automatically transfer or does not have jobs that the transferring employees are capable of performing.

In the UK, the dismissal of any employee (before or after the transfer) by reason of the transfer will be automatically unfair, unless it is for an ETO reason. If the dismissal is for an ETO reason, the usual test of fairness will be applied by employment tribunals. It is important to note though, that a seller would not be able to rely upon a buyer's ETO reason in circumstances where, as can often be the case, it is commercially agreed that the seller will make any required dismissals pre-transfer. As a result of this, a seller will often require indemnity protection in respect of any claims that may arise from the dismissals it has agreed to make.

In contrast, in Japan, there are no specific rules regarding dismissals in the context of a transaction. Instead, the normal principles for dismissals will apply, namely, an employer must have reasonable grounds in order to unilaterally terminate contracts of employment (Article 16 of the Labour Contract Act). This remains the case regardless of whether termination occurs pre- or post-transfer. In practice, this may allow for pre-transfer dismissals to be made in order to make the business more commercially attractive for sale, provided that the normal principles for fair dismissals are complied with.

Failure to comply

Where there is any failure to inform and consult under TUPE, the employee representatives (or, in some cases, the affected employees themselves) have the right to present a complaint to an employment tribunal. An employment tribunal may award each affected employee up to 13 weeks' actual pay for failure to inform and consult. This is called a protective award. The buyer and seller are jointly and severally liable for a failure to inform and consult under TUPE. In Japan, where there is a failure to inform employees or labour unions, the employees/labour unions can challenge the validity of a demerger agreement or of any changes to terms and conditions of employment or dismissals.

Uniquely in the UK, it is not possible for employees to waive their statutory claims for failure to inform and consult under TUPE (save in very limited circumstances). Therefore, even in circumstances where employees who are dismissed are required to enter into a settlement agreement, there will be no protection against claims under TUPE for failure to inform and consult. Indemnity protection in this regard will be key in commercial negotiations.

By comparison, in Japan, where parties enter into separation agreements, such agreements typically contain waivers of all claims as there is no restriction on the claims that an employee is or is not able to waive.

Conclusion

Regardless of the jurisdictions concerned, legal advice should be sought at all stages of a business transfer to ensure there is adequate preparation and protection in place.

From a UK perspective, any agreement detailing a potential TUPE transfer needs to adequately deal with the uncertainties of TUPE (including, what is being transferred, whether employees will transfer and if so, which employees, information and consultation obligations), and associated liabilities need to be appropriately allocated and documented in the agreement. Likewise, although there is no equivalent to TUPE in Japan, commercial negotiations in Japan will, regardless of the structure of a transaction, still require discussion as to whether employees will transfer and if so, how this is to be achieved and which employees will transfer.

Employment contract governing law clauses

Challenge

Multinational employers often insert governing law clauses (usually applying home country law) into expatriate employment agreements. But often these clauses may not effectively preclude the application of host country law, forcing the employer to comply with the extra rules of an additional legal regime.

The general rule is that employment protection laws of the place of employment apply notwithstanding a governing law clause by which parties to an employment agreement or incentive plan purport to select the governing law of some foreign jurisdiction with a nexus to the employment relationship. When a multinational employer selects the law of some jurisdiction outside the host country – even a jurisdiction with a genuine nexus to the employment relationship – the selection is usually trumped by host country "mandatory rules" (if more favourable). In the employment context, host country "mandatory rules" normally include, for example, laws relating to: pay rates, overtime, payroll, mandatory benefits, hours, rest periods, holidays, health/safety, trade unions/collective representation, discrimination/harassment, employee versus-contractor classification, restrictive covenant/non-compete/trade secret rules, dismissal/termination procedures, notice, severance/redundancy pay and releases/waivers.

The problem with an employment contract governing law clause is that it applies tougher employment protection laws of the selected jurisdiction without preventing the mandatory application of tougher employment protection laws which apply by force of public policy in the host jurisdiction. Both sets of laws end up protecting the employee. The employee gets to "cherry pick" whichever rules offer better protection. The multinational employer now has to comply with two sets of employment protection laws, rather than just one. A home country governing law clause can, therefore, sometimes backfire and restrict flexibility: the employee gets the best of both worlds while the employer suffers the worst of both worlds.

Indeed, where a governing law clause invokes an additional set of employment protection laws in the selected jurisdiction that otherwise would not have applied to the employee in the host country, the employer often ends up arguing later that the selected jurisdiction's law does not itself reach abroad notwithstanding the governing law clause (because the selected jurisdiction's law has no extraterritorial reach and/or the selected jurisdiction's domestic conflict-of-law rules call for the application of the law of the host country, not the rules of the selected jurisdiction). The employer in effect has to challenge its own governing law clause. Of course, in these situations, the employer should have omitted or narrowed the home country governing law clause in the first place.

Another potential drawback to governing law clauses in employment agreements is that these provisions can needlessly complicate employment litigation, imposing significant additional costs. When disputes arise, local employment tribunals and local judges inevitably wrestle with complex conflict-of-law issues (often involving expensive expert testimony and translations) before coming to the usual conclusion that local employment protection laws apply anyway, by force of public policy.

Despite the drawbacks of a governing law clause purporting to apply home country law in expatriate employment contracts, these clauses remain stubbornly common. We examine the following five situations/circumstances which are often claimed to render a foreign governing law clause advantageous to an employer of an internationally mobile employee: (1) Europe's Rome I Regulation; (2) Global Employment Companies and non-mandatory benefits; (3) restrictive covenants; (4) forum selection clauses; (5) short-term assignments; and (6) the "trick-the-expat" strategy.

1. **Europe's Rome I Regulation:** European law provides for a choice-of-law in contracts regime under the Rome I Regulation, which replaced the earlier 1980 Rome Convention. Some European lawyers have argued that Rome I more effectively empowers governing law clauses to block the mandatory application of host country employment protection laws.

   However, this analysis is wrong. The Rome I Regulation affirms the general rule that, in an employment or other contract, the "overriding mandatory provisions of the law of the forum" apply notwithstanding any governing law clause. Rome I defines "overriding mandatory provisions" as laws "the respect

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for which is regarded as crucial by a country for safeguarding its public interests", and it stipulates that a governing law clause in an employment agreement cannot "depriv[e] the employee of the protection afforded to him by provisions that cannot be derogated from by agreement under the law that, in the absence of choice, would have been applicable." Rome I also declares that a governing law clause cannot override the law of any "country" "more closely connected with" the "circumstances [of employment] as a whole." These Rome I Regulation provisions restate firmly entrenched principles of the predecessor Rome Convention.

In short, under the Rome regime, expatriates whose employment is terminated whilst they are in Europe – even non-European expatriates – and whose contracts contain a foreign governing law clause are often able to select the law more favourable to them, either the law of the selected jurisdiction under their contract or the law of the country "in which the employee habitually carries out his work" – or, indeed, both. Labour courts in Europe decide cases consistent with this analysis all the time. For example, French appeals courts in Grenoble and Paris have overridden governing law clauses providing for Texas and German law by invoking the Rome Convention to impose the French employment code in favour of expatriates working in France.

2. **Global employment companies and non-mandatory benefits:** Whilst the parties often cannot contract around or opt out of "mandatory rules" relating to working conditions, a governing law clause is more likely to be effective in applying home country law if it is confined to those areas of the employment relationship which are not regulated by employment protection laws and "mandatory rules" of the host country.

   Indeed, parties to an international employment relationship can effectively select home country laws that govern discretionary human resources topics outside the realm of local "mandatory rules". In fact, this principle applies in the case of "global employment companies" – so-called GECs, multinational entities set up to employ the body of senior expatriates of a multinational employers who spend most, if not all, of their career working worldwide – and this explains why home country law is expressly stated to govern some international incentive and equity award agreements.

   However, only a small subset of employment laws are discretionary, steering clear of mandatory employment protections. The employment law topics most likely to be discretionary tend to be equity plan rules, executive compensation doctrines, and some (but not all) regulation of non-mandatory benefits, such as rules on voluntary pensions, certain tax and social security totalisation treaties, and some (but not all) rules applicable to discretionary bonuses.
   Even a governing law clause confined to a senior executive's bonus plan, equity award agreement or incentive arrangement will not divest host country "mandatory rules." For example, the two landmark UK decisions of *Duarte v. Black and Decker [2007]* and *Samengo Turner v. Marsh & McLennan, [2007]* both involved whether a US state governing law clause (one case involved a New York law clause and the other a Maryland law clause) in executive compensation arrangements required a English court to defer to US state law in interpreting a restrictive covenant enforced in the UK. The facts in each case involved some twists, but at the end of the day, both English courts predictably ruled that the enforcement of restrictive covenants on UK soil had to be in line with UK public policy and common law principles notwithstanding the applicable US state law – even where the employer seeks to apply the restrictive covenant through a complex compensation or equity award plan.

3. **Restrictive covenants:** The Duarte and Samengo-Turner cases highlight the special challenges of restrictive covenants (non-competition, non-solicitation, confidentiality and employee IP/inventions commitments) in an international employment relationship. Restrictive covenants tend to be governed by "mandatory rules" that apply by force of public policy, and so the rules of interpretation or enforcement in the host country will be critical irrespective of any governing law clause. For example, if an expatriate employee breaches his non-competition obligations under an English law governed employment contract whilst living and working in California, whilst the employer may be able to seek an order for an injunction through the English courts, when it comes to enforcement of that order in California, a Californian court is highly unlikely to respect an English governing law clause to enforce the order not to compete. With post-termination restrictive covenants, the practical enforcement issue usually comes down to complying with the mandatory restrictive

covenant rules and public policy of the jurisdiction where the employer seeks enforcement. This often ends up being the place where the employee goes off to breach the covenant, and may be neither the home nor the host country.

4. **Forum selection clauses:** We have been addressing governing law clauses that invoke a governing law other than that of the host country. A separate but similar issue is choice of forum or jurisdiction clauses that seek to require parties to litigate any disputes in some selected forum – arbitration or a foreign jurisdiction's courts. The challenge with forum selection clauses in employment contracts is that local labour courts tend to enjoy mandatory jurisdiction over employees who work locally. Clauses in internationally mobile employees' contracts and compensation/equity plans purporting to select some forum other than host country courts and tribunals rarely block the jurisdiction of host country labour judges – unless, perhaps, the parties sign a forum selection clause after a dispute arises, or unless the host country is one of a handful of jurisdictions, like Malaysia, with statutes authorising employment arbitration.

5. **Short-term assignments:** We have generally been discussing the choice of governing law clauses in the context of expatriate employees, where the employee has made a long-term move of a year or more. For short-term assignments, however, there is perhaps more reason to entertain the notion of retaining home law as the governing law of the assignment. By virtue of an assignment being short-term, the employee will usually be less willing to "commit" to the host country, and will often be keen to retain as many rights as possible under home law to avoid any perceived detrimental consequences of the assignment and ensure a smooth transition back to the home country. Further, whilst mandatory host country employment laws will continue to prevail, the protections afforded by those laws often will not apply immediately (e.g. where there is a length of service requirement) and so a short-term assignee may consider application or replication of home country laws to offer the best protection in the circumstances. However, although an employee may push for application of home country law, the employer should be careful not to be swayed by the emotion behind such a request if the reality is that there is no real benefit to the employee save that they will be able to "cherry pick" whichever rules offer better protection.

6. **The "trick the expat" strategy:** A well-known consultant specialising in globally mobile employee issues at a major HR consulting firm used to recommend inserting into the assignment agreements of American expatriates a US governing law and choice-of-forum clause, even though those clauses are extremely unlikely to block local host country employee protection laws and labour court jurisdiction. His theory: some American expatriates, particularly those posted into poor countries, may be so innately sceptical of overseas justice that a US governing law (or forum) clause might dissuade at least those less sophisticated expatriates from asserting inalienable legal rights granted by their new host country. This consultant predicted that American expatriates might believe a US governing law and forum clause means what it says, that any dispute must be resolved under the employer-friendly regime of US employment at-will, so that a governing law clause might blind at least a less sophisticated expatriate to the fact that "mandatory rules" of the current place of employment grant inalienable substantive and procedural rights better (for the expatriate) than those under US law.

   These days, expatriates are increasingly sophisticated and increasingly likely to research their rights on the Internet and to figure out that governing law and choice-of-forum clauses in the internationally mobile employment context are largely powerless to block host country "mandatory rules". Expatriates will soon recognise where host country law guarantees them more employee-friendly labour rights than they would enjoy in their home country.

   This said, though, in some cases a home country governing law or forum selection clause is said somehow to act as an acknowledgment between an expatriate and an employer that their mutual intent, even if non-binding, is to resolve disputes under home country rules. Some expatriates might accept that – even if the law does not force them to.

Employers should be aware, however, that even if the governing law clause of an employment contract is aligned with laws of the host country, an expatriate employee can still be subject to home country laws. This can occur where a home country law has "extraterritorial reach", or where the parties contractually select their home country law. The UK's Bribery Act 2010, for example,

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has extraterritorial application such that, even if an act or omission does not take place in the UK, but the person's act or omission would constitute an offence if carried out there and the person has a close connection with the UK, an offence will still have been committed. A person will have "a close connection with the UK" if they are, for example, a British citizen or a resident of the UK.

Similarly, employees who are US citizens have the right to file discrimination claims with the Equal Employment Opportunity Commission and sue for employment discrimination occurring anywhere in the world if they work for a US corporation or an employer controlled by a US corporation, regardless of whether they work in the US or any other jurisdiction.

It should be remembered, however, that the application of laws by way of extraterritorial reach does not act to exclude mandatory host country laws. Extraterritorial laws are another layer of law to which an employer and employee must have regard; indeed, it is conceivable that if the parties have agreed that the governing law of the employment agreement is different from the law of the host country, and the extraterritorial reach of certain statutes is considered, the multinational employer may have to comply with three sets of employment protection laws, rather than two. Whilst an employer will have difficulty arguing against application of mandatory laws of a host country and extraterritorial reach of home country laws, the option of which law shall govern an employment agreement is generally open to the parties to decide. As the above illustrates, an employer should consider the implications of its choices carefully.

Conclusion

One question comes up time after time when dealing with international human resources questions: which laws apply to internationally mobile employees? The general rule is that because employment protection laws are "mandatory rules" applicable by force of public policy, host country employment law – the law of the current place of employment – tends to apply by operation of law. In addition – but not instead – home country laws sometimes also apply, such as where a home country statute has "extraterritorial reach" or where the parties contractually selected their home country law.

While the law of the current place of employment tends to apply regardless of most other factors, the issues here are nuanced, particularly when the parties signed a contract containing a foreign governing law clause.

At the point of negotiating or choosing the law to govern an employment agreement, an employer should therefore consider carefully what mandatory laws might apply, what laws are likely to reach the employee extraterritorially (and, if so, the likely impact of this), and whether there is any benefit to the employee or employer in maintaining home country law. An informed decision when choosing the governing law has the potential to minimise complexity when determining the respective rights of the employee and employer and, importantly, prevent any surprises in the future should the employment relationship sour.

UK Budget 2014: major changes to accessing pensions savings

On 19 March 2014, the UK's Chancellor of the Exchequer gave his 2014 Budget speech. Major changes to the way that members of defined contribution pension schemes access their pensions savings were announced.

Current situation

At the moment, retirees wishing to access their pension savings have two options:

1. Purchase an annuity; or
2. Drawdown, i.e. withdraw a portion of their pot and leave the rest invested.

The first option has become increasingly less attractive as low rates equate to poor value for money. Additionally, annuities have attracted criticism over the fact that the income is not protected against inflation and that generally, when the individual dies, what is left of the pension pot goes to the annuity provider instead of the spouse.

Under the second option, there are restrictions on how much can be taken out of the pension pot. At present, savers can take 25% of their pension pot tax-free when they retire. However, anyone who chooses to empty the contents of a pension pot above this level faces a hefty tax charge of 55%.

What is changing?

It is proposed that from April 2015, members at normal retirement age will be able to access their pension fund in full without the need to purchase an annuity. The savings will be taxed at the individual's marginal tax rate (20% for most pensioners) rather than the 55% rate currently applied. There will be no requirement for members to purchase an annuity or choose a particular product in order to access their savings.

There are transitional changes from 27 March 2014 which allow for immediate flexibility. The amount of overall pension savings an individual can withdraw, as a lump sum, will increase from £18,000 to £30,000. The requirements for accessing a "flexible drawdown" scheme will be relaxed, with the guaranteed income requirement reducing from £20,000 per year to £12,000 per year. Those in "capped drawdown" arrangements will also have greater access to funds as they will now be entitled to claim 150% of an equivalent annuity (formerly 120%). Additionally, there will be an increase in the size of the "small pension pot" that an individual can take as a lump sum, regardless of total pension wealth, from £2,000 to £10,000.

Impact of changes

At their core, the changes make pensions savings more readily accessible. It is a likely consequence that members will develop a greater sense of ownership and control over their pension, and the prospect of saving a healthy pension pot will become far more appealing. The amendments will additionally be advantageous to those considering their inheritance plans. The changes mean that a pension pot can be taken as cash, become part of the estate, and be passed on to spouses and children.

The impact of the changes on employee members is therefore overwhelmingly positive, and it can be expected that employers will see an increased interest from employees in pension contributions. Employers should be prepared to consider structuring or restructuring employee remuneration to allow for increased pension contributions as a means of incentivising or rewarding employees. Similarly, the structuring of termination payments may see an increased focus on allocation of money to an individual's pension. Importantly, there will be no additional cost to an employer in allocating sums to an employee's pension (and indeed some potential savings in employer's National Insurance Contributions), making this one instance where an employer can afford to be flexible and meet the changing needs of employees.

In profile

Valérie jumped at the chance to join White & Case in 2007 when Alexandre offered her a place in his team in Paris.

Valérie Ménard

Valérie was born in Montpellier in the south of France and made the obvious choice to study law in Montpellier at one of the oldest universities in the world founded in the 12th century.

Valérie says that Montpellier was the best place to be a student as she could enjoy outdoor activities especially wakeboarding and snowboarding with friends (Montpellier is ideally located next to mountains and beautiful Mediterranean beaches).

Whilst at university, Valérie had the opportunity to spend a year in San Diego as an intern at a small law firm which specialised in criminal law. The work included homicide and death row cases, visits to federal prisons, and negotiations involving the FBI and a drugs baron! She enjoyed her experience at that firm so much that she strongly considered a career as a criminal lawyer.

On her return to France, Valérie passed the Bar exam in Paris and worked for two years at Baker & McKenzie alongside Alexandre Jaurett, who is now head of White & Case's employment and benefits team in Paris. However, their paths diverged when Valérie was given the opportunity to join Gide Loyrette Nouel where she worked for several years specialising in employment litigation.

Valérie jumped at the chance to join White & Case in 2007 when Alexandre offered her a place in his team in Paris. The prospect of working with a truly global employment team on a wide variety of international issues was extremely appealing to Valérie. She also spent a few weeks in the Firm's New York office working with Don Dowling on many cross-border employment matters.

These days Valérie is not only a full-time lawyer but also a mother to three sons (including twin boys) aged between 1 and 5 years.

Whilst balancing work and family life is often challenging, Valérie does try to make room for hobbies and family activities on the weekend. She has just given her 5 year old son his first skateboard. Once her twins are older, she dreams of the whole family taking part in sporting activities together.

Outside work, she likes to spend time with her family and friends. She attends many concerts (the French touch performers being her favourites) courtesy of her husband who works in the music industry.

Valérie also loves Italian culture and has been a frequent visitor to Italy over the last few years. She enjoys cooking pasta and always has the ingredients ready for a fresh tomato sauce in case a friend shows up unexpectedly!

Valérie was recently promoted to Counsel at White & Case. She has significant experience in employment litigation concerning individuals and collective employment relationships. She has worked on complex discrimination cases and large-scale collective claims. She continues to advise on the implementation of restructuring and employment safeguard plans and is regularly involved in negotiations with trade unions and employee representatives.

News in brief

European Union

Brussels plans fresh rules on executive pay

The recent draft European Commission proposal which would give shareholders in Europe's listed companies a binding vote on pay has been met by criticism from investors and business groups. The proposal allows shareholders to vote down the ratio between board pay and the average full-time worker and introduces the requirement for an explanation of why the director-worker pay gap ratio is considered appropriate.

Such reforms are significant as the ratio of worker-executive pay at the big banks often exceeds 100 times, for example, Barclays pays its chief executive 181 times more than the median pay of its employees.

Investors have reacted with alarm to the proposal, emphasising that it would put Europe at a disadvantage. It is anticipated that the proposal will receive a reserved response from the UK, Germany and other Member States that disregarded such ratios after hard fought domestic debates over corporate governance reform.

However, lobby groups have welcomed Brussels' plans explaining that there is no convincing business case why the value of managers has increased so dramatically relative to their staff and citing examples such as the John Lewis Partnership which has for years limited the pay of the highest paid partner to 75 times the average employee.

Negotiations on the proposal are unlikely to be agreed until late 2015 at the earliest.

Finland

The future of the Finnish job alternation leave system

The purpose of job alternation leave in Finland is to provide an employee with a break or rest (sometimes called a "sabbatical") during their long working lives and at the same time offer an unemployed jobseeker the opportunity to gain work experience through fixed-term employment. It is also an opportunity for an employer to benefit from having someone with new skills and expertise on its workforce. Under this arrangement, the employee and employer jointly agree on the employee's option to take job alternation leave. The employee may use the leave any way he or she wishes.

The minimum period allowed for job alternation leave is 90 calendar days, and the maximum period is 359 calendar days. The employee receives an annual allowance of 70 to 80% of his or her estimated unemployment benefit. To be entitled to job alternation leave, the employee must have worked for at least ten years including a minimum of 13 months with the same employer.

This arrangement is currently the subject of discussion in Finland between the Finnish government and employers who want stricter rules in place, and the trade unions who remain strongly in favour of the existing system. Last autumn, following talks amongst a working group set up to look into job alternation leave, it was agreed that the minimum qualifying requirement of ten years working history be extended to seventeen years. No further changes were made despite demands to cut levels of compensation and limit leave to specific purposes such as studying.

The debate is continuing and recent discussions have focussed on the Finnish government's desire to introduce a minimum unemployment period of three months for any jobseeker seeking replacement work experience. This has been met by opposition from the trade unions who have argued that the requirement of three months unemployment would radically cut the use of job alternation leave particularly in the health sector due to the lack of suitable jobseekers.

Germany

No discrimination liability for recruitment agencies under the German Equal Treatment Act

The German Federal Labour Court has recently stated that an employee's claim for damages under Section 15 paragraph 2 of the German Equal Treatment Act (Allgemeines Gleichbehandlungsgesetz) ("**AGG**") must be brought against the employer and not against third parties involved in the recruiting process, such as recruitment agencies.

Section 1 of the AGG prohibits unequal treatment on the grounds of race or ethnic origin, gender, religion or secular belief, disability, age or sexual identity in relation to conditions for access to employment, including selection criteria and recruitment conditions. Under the AGG, the employer will be required to pay compensation for damages resulting from a discriminative action.

The German Federal Labour Court stated that agencies involved in the recruiting process cannot be held liable for discrimination under the AGG, even if the job advertisement posted by the agency did not comply with the requirements specified in the AGG.

Hungary

New Civil Code

On 15 March 2014, the new Civil Code entered into force, replacing the old Civil Code that has been in effect for over five decades. The Hungarian Labour Code has also been amended and introduces civil law principles. The interpretation and scope of such civil law principles (for example, the rule according to which any provision that is contrary to public morality may be deemed invalid) will be decided by the courts on a case by case basis.

Amongst the civil law principles introduced, of particular note is the provision whereby a party (normally the employer) who exercises its rights in a manner that is inconsistent with previous conduct may be held to be acting in bad faith if the other party (normally the employee) had reason to rely on such conduct.

The rules of the new Civil Code relating to the protection of personal rights (which includes, inter alia, the right to equal treatment, the right to the protection of personal data, the right to "personal confidentiality" and the rights attached to images and voice recordings) will also be the subject of much scrutiny. As a result of the new rules, employees whose personal rights have been violated by their employer will now be able to claim damages as "restitution" for the harm suffered. Consequently, employers will have to place more emphasis on complying with data protection rules and exercise increased caution when monitoring the work of employees (e.g. installing CCTV systems or monitoring employee emails). However, employers will also be able to claim damages from employees who breach business confidentiality.

Amongst the more technical changes to the Hungarian Labour Code, the most important is the easing of certain formal requirements. For example, instructions by the employer relating to working time (e.g. overtime) and performance criteria can now be communicated to employees in a manner that is considered customary at the given company (e.g. by posting on the staff notice board or by email).

Further, certain rules intended to protect pregnant employees and employees on maternity leave (by granting additional free time and banning the termination of the employment of such employees) will also now be mandatory in respect of "executive employees" (i.e. senior management).

Poland

New rules for working on Sundays and public holidays

The Polish Parliament has adopted new rules allowing work on Sundays and public holidays. From 4 March 2014, an employee will be permitted to work on Sundays and public holidays in Poland where he or she provides services using electronic means of communication or telecommunications equipment (for example, by telephone or email). The new regulation permits that the services must be carried out electronically, the recipient of the services must be based outside Poland and the public holiday or Sunday in question must be a business day in the country where the recipient of the services is located. An employee who is permitted to work on a Sunday or public holiday will be granted a day off in lieu.

The new provisions of the Polish Labour Code are aimed at increasing the level of competitiveness of companies providing cross-border services by introducing more flexible working hours 365 days a year.

New social security rules for civil contractors and supervisory board members

On 6 March 2014, the Polish Government presented Parliament with proposed amendments to the laws regarding social security in Poland. Contributions for pension and disability security will now be levied at an amount equal to at least the minimum wage. Additional changes were also proposed to supervisory board members' insurance. Under the new rules, all supervisory board members receiving remuneration will be covered by compulsory disability and retirement insurance regardless of whether they are insured under other arrangements.

Russia

Work permits for foreign citizens

From 10 January 2014, foreign citizens who are seconded to work in the Russian Federation, by a foreign organisation registered in a World Trade Organisation member state, may apply for a work permit to enable them to work at either:

(i) a Russian subsidiary of such foreign organisation; or

(ii) a branch or representative office of such foreign organisation.

The right to apply for a work permit will only be open to foreign citizens who have been employed by the foreign organisation for at least one year prior to their secondment and who are seconded to either:

(i) the representative office to manage and coordinate the activities of the representative office; or

(ii) the branch or Russian subsidiary as key personnel (for example, the head of the branch or another position where the salary is at least 2 million rubles (approximately US$65,000) per year).

Golden Parachutes

On 24 January 2014, the State Duma adopted law No. 378667-6 (the "**Bill**") which proposes to limit the amount of severance payment due to certain senior managers (for example, chief executive officers and their deputies, chief accountants and members of collegiate executive bodies) of state corporations and other companies which are more than 50% state owned.

The Bill provides that in cases where a senior manager's employment terminates due to a change of ownership of the company or on the basis of a decision by the relevant governing body, then such manager will be entitled to a severance payment of three to six months' salary.

The Bill also specifies that no severance payment shall be made to senior managers whose employment is terminated by mutual agreement.

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Tax registration of foreign citizens

From 1 January 2014, a new procedure has been established to ensure that foreign citizens who work in the Russian Federation are registered with the local tax authorities.

Along with the general procedure under which an individual can apply for tax registration, an automatic procedure of tax registration has been specifically created for foreign citizens. Under this procedure, the migration authorities are obliged to report the following information to the tax authorities:

(i) when they register foreign citizens at their place of residence in the Russian Federation;

(ii) when they issue a work permit to such registered foreign citizens; and

(iii) when they accept the application for the issuance of a work permit for foreign citizens who are not registered with the migration authorities.

Based on the above notifications, the local tax authorities will automatically register the foreign citizens as taxpayers and report this to the migration authorities.

Sweden

Proposal to modify or abolish Laval Law

The so called "Laval Law" followed a ruling by the European Court of Justice declaring that the industrial action taken by the trade unions against a construction site in Sweden where temporarily posted Latvian personnel worked was contrary to community law.

Pursuant to the Laval Law which was implemented in 2010, industrial action may not be taken in order to force a foreign service provider posting workers in Sweden to sign a Swedish collective agreement provided that the foreign service provider has entered into an agreement in its home country that complies with the minimum standards of the applicable Swedish collective agreement.

However, the Laval Law has been criticised for allowing foreign entities to circumnavigate Swedish collective bargaining agreements while operating in Sweden. LO, Sweden's blue-collar trade union confederation has for the first time produced an election manifesto demanding that Sweden abolishes the Laval Law. The demand to abolish the Laval Law has also been put forward by the Social Democrat Party as one of the party's election pledges for the national election in 2014. The Social Democratic leader Stefan Löfvén has declared that Swedish collective agreements should apply on the Swedish labour market.

In its annual report for 2013, the ILO Committee of Experts on the Application of Conventions and Recommendations (CEACR) stated that the limitations imposed on Swedish trade unions' right to take industrial action to convince a foreign service provider posting workers to Sweden to sign a collective agreement have been found to be in violation of ILO Convention No. 87 on the freedom of association and the right to organise. Furthermore, CEACR has requested that the Swedish government review the legislation to ensure that trade unions are not restricted simply because of the nationality of the enterprise.

However, if the Laval Law is abolished or modified, Sweden may once again have to appear before the European Court of Justice.

Turkey

Inspection of overtime practices

In the final quarter of 2013, Turkish banks and certain other sizeable companies underwent a series of inspections by the Ministry of Labour in relation to overtime practices. The press reports have indicated that the majority were found to be in breach of the Turkish Labour Law and relevant overtime regulations and were subject to substantial administrative fines exceeding millions of Turkish liras. These sizeable fines alerted many companies operating in Turkey to take a closer look at their overtime practices and to conduct compliance reviews of their employment contracts, company policies and day-to-day operations in order to make the necessary adjustments.

It is market practice in Turkey that blue collar employees are paid separately for overtime on an hourly basis but commonly employment contracts of white collar employees include provisions stating that overtime payments are to be incorporated as part of salary and no extra payments for overtime will be made. To the extent that overtime does not exceed 270 hours a year, the Court of Appeal accepts such provision for white collar employees.

Mis-applied overtime practices may attract a number of administrative fines that could be significant for an employer. Further, overtime claims are subject to a 5 year limitation period which is a lengthy time period for a contingent liability.

United Kingdom

Prudential Regulation Authority (PRA) proposals regarding clawback to vested variable remuneration

The PRA proposes to require firms to amend employment contracts to enable them to apply clawback to vested variable remuneration. The proposed rule will amend the Remuneration Code and come into force on 1 January 2015. The PRA wants firms to have risk-focused remuneration policies that promote effective risk management and are consistently applied across the industry.

Clawback will apply when there is reasonable evidence of employee misbehaviour or material error, when the firm suffers a material downturn in its financial performance, or when the firm suffers a material failure of risk management. However, the PRA proposes that clawback should not be limited to employees directly culpable of malfeasance and suggests that in relation to material failure of risk-management or misconduct, firms should apply clawback to employees who could have been reasonably expected to be aware of the failure or misconduct at the time but failed to take adequate steps to address it, or by virtue of their role or seniority could be deemed indirectly responsible or accountable for the failure or misconduct. Thus, clawback could apply to senior staff in charge of setting the firm's culture and strategy.

Firms will be expected to amend employment contracts to allow for the application of clawback to all vested awards up to six years after vesting. Further, the PRA expects firms to take all reasonable steps to amend employment contracts to reflect awards made prior to 1 January 2015, but which vest after that date (again subject to a limit of six years after vesting). The PRA recognises that it may not be possible to amend contracts in such a way, but nevertheless will still expect firms to adopt specific and effective arrangements to manage the risks raised by the inability of the firm to apply clawback to awards made before 1 January 2015.

United States

Final US Tax Regulations clarify when a substantial risk of forfeiture exists under Section 83

The United States federal tax authorities recently issued final regulations clarifying the meaning of "substantial risk of forfeiture" under Section 83 of the US tax code. Section 83 generally provides that when property (such as employer stock) is transferred to an employee as compensation, the property is taxable to the employee in the year he or she receives the property. However, if the property transferred to the employee is subject to a substantial risk of forfeiture (i.e., unvested) the property is taxable to the employee only when the substantial risk of forfeiture lapses, unless the employee elects under Section 83(b) to be taxed immediately upon receiving the property.

For purposes of Section 83, whether a risk of forfeiture is substantial or not depends upon the facts and circumstances. The new regulations provide that:

- a substantial risk of forfeiture may only be established through a service condition (e.g., continued employment for a specified period of time) or a condition related to the purpose of the transfer (e.g., the employer's attainment of a financial performance goal).
- in determining whether a substantial risk of forfeiture exists based on a condition related to the purpose of the transfer, both the likelihood that the forfeiture event will occur and the likelihood that forfeiture will be enforced must be considered.
- with certain limited exceptions, transfer restrictions do not create a substantial risk of forfeiture, including those that carry the risk of disgorgement or forfeiture of the property, or other penalties, such as lock-ups, if the transfer restriction is violated.

Upcoming events

Global Equity Organisation's 15th Annual Conference, Miami

7 – 9 May 2014

The Global Equity Organisation's 15th annual conference will take place in Miami on 7 – 9 May 2014. Nicholas Greenacre (White & Case, London) will be presenting, together with Lindsey Doud and Caroline McCann from RBC cees International Limited, on the strategies and regulatory, administrative and cultural challenges around effectively incentivising both local and globally mobile employees in the Middle East and Latin America. The panel will also look at how plan governance models from the developed markets (in particular the US and the UK) can effectively be replicated in local plans in emerging markets and provide a stable structure to the fundamentals of plan design. The panel will examine perceived and real advantages and disadvantages in the Middle East and Latin America of phantom stock plans when compared with longer term savings and international pension plans which are seeing growing prevalence in these territories. As part of the session, the panellists will draw on specific recent client examples and situations.

White & Case and 11KBW breakfast seminar: Key Individual and Team Moves; Managing the Risks for the New Employer and the Team

22 May 2014, 8.00am – 10.00am

White & Case LLP, London

Stephen Ravenscroft (White & Case, London) and James Baker (Director, Frazer Jones, Global HR Recruitment) will host a practical, interactive workshop in London to consider the risks, liabilities, strategies and tactics for successful key individual and team moves.

ENR+Dodge Global Construction Summit: Market Trends and Critical Business Issues

McGraw Hill Financial Global Headquarters

May 13 – 14 2014

New York

Don Dowling (White & Case, New York) will participate in the ENR+Dodge Global Summit to address international employment issues related to industry leaders from large engineering and construction firms that are doing business globally or seeking to expand beyond their current borders, as well as for construction project owners (public and private), industry associations, governmental and trade organisations and policymakers.

The ESOP Centre: Employee Equity Plans: helping to solve the cost of living crisis, Rome

5 – 6 June 2014

The ESOP Centre will be hosting a conference in Rome on employee equity plans on Thursday 5 to Friday 6 June 2014. Nicholas Greenacre (White & Case, London) will be presenting on the regulatory aspects of employee equity plans in Europe. Registration details and additional information regarding the conference can be found at: http://www.esopcentre.com/event/diary-date-rome-2014/.

The National Association of Stock Plan Professionals (NASPP), 22nd Annual Conference, Las Vegas

29 September – 2 October 2014

NASPP's 22nd annual conference will take place in Las Vegas from 29 September to 2 October 2014. Nicholas Greenacre (White & Case, London) and Jason Rothschild (White & Case, New York), in association with Deloitte LLP, will be presenting on the subject of the Foreign Account Tax Compliance Act (FATCA). Registration details and additional information regarding the conference can be found at: http://www.naspp.com/conference2014/.

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