TRANSFERS OF UNDERTAKINGS—PRINCIPLE AND PRAGMATISM IN THE CJEU

The Transfer of Undertakings (Protection of Employment) Regulations 2006 (SI 2006/246) (TUPE) are the current incarnation of the domestic legislation implementing Council Directive 2001/23/EC—the so called Acquired Rights Directive (ARD). The primary purpose of the ARD is "to provide for the protection of employees in the event of a change of employer, in particular, to ensure that their rights are safeguarded" (Recital 3). In the domestic context, TUPE also addresses the common law position that, as a consequence of a transfer of the business in which he or she works, an affected employee is left with no entitlement to continued employment in the business in which he or she was employed prior to the transfer in question, has no right to be employed on his or her previous contractual terms, and has no entitlement to any information about, or consultation in relation to, the transfer and its consequences.

In *Alemo-Herron v Parkwood Leisure Ltd* (C-426/11) [2013] I.C.R. 1116, the Court of Justice of the European Union (CJEU) was called upon to determine the proper application of TUPE in a situation where the terms of employment of the transferring employees were, prior to the relevant transfer, determined by a third party negotiating body in accordance with a collective agreement. In essence, the question was whether, after a transfer of an undertaking, a transferee can remain bound by a pay determination method established by a collective agreement to which the transferor was a party but to which the transferee is not. In this case the claimant employees were originally employed by the London Borough of Lewisham on standard contracts which provided that their terms and conditions were to be determined in accordance with collective agreements negotiated by the National Joint Council for Local Government Services (NJC), a body which included representatives of local authority employers and trade unions. As a result of a TUPE transfer of an undertaking falling within the scope of the applicable legislation, the employment of the employees in question transferred from the London Borough of Lewisham to a private-sector transferee, CCL Ltd, in 2002. The employees continued to receive pay increases in line with pay settlements

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determined by the NJC until a further transfer of the undertaking in which they were employed to Parkwood Leisure Ltd in 2004 following which the new employer sought to argue that it was not bound by any such further pay determinations.

In terms of the legislative background, art.1 of ARD provides that the:

> "transferor's rights and obligations arising from a contract of employment or from an employment relationship existing on the date of a transfer shall, by reason of such transfer, be transferred to the transferee".

This provision is translated into TUPE by its reg.4(1) which, inter alia, provides that the contract of employment of a transferring employee "shall have effect after the transfer as if originally made between the person so employed and the transferee" and its reg.5(2) which provides that all the transferor's rights, powers, duties and liabilities under or in connection with a transferring employee's contract of employment shall be transferred to the transferee. In relation to collectively determined terms of employment, art.3(3) of ARD provides that the transferee is required to comply with any collective agreement applying to the transferor until the date of the termination or expiry of the collective agreement or the entry into the application of another collective agreement. Member States have the ability in their implementing legislation to limit to one year the period for which compliance with collective agreements can be required by their domestic transfer of undertakings legislation. However, TUPE contains no such limiting provision, perhaps reflective of a domestic labour market far less regulated by collective agreements than Continental Europe. Article 8 of ARD permits Member States to adopt domestic provisions which are more favourable than the minimum standards prescribed by ARD.

In *Alemo-Herron* [2009] IRLR 322, the Employment Appeal Tribunal (EAT) had held that the employees were entitled to pay settlements as determined by the NJC in respect of the period in question and therefore to benefit from changes to the collective agreement which came into effect following the date of the relevant transfer. In so doing, the EAT adopted what had become known as the "dynamic"—and contractually orthodox—interpretation of the transfer of undertakings legislation adopted in *Whent v T Cartledge Ltd* [1997] I.R.L.R. 153 (EAT). As Judge Hicks Q.C. put it in *Whent*, "there is simply no reason why parties should not, if they choose, agree that matters such as remuneration be fixed by processes in which they do not participate". The competing analysis of the proper application of ARD in this context was adopted by the ECJ in *Werhof v Freeway Traffic Systems Gmbh* (C-499/04) [2006] I.R.L.R. 40, where it was held that the rights of employees to continue to benefit from collectively agreed terms and conditions after a transfer falling within the scope of ARD are "static" rather than dynamic. Consequently, the transferee was found to be bound by the terms of employment determined in accordance with the relevant collective agreement only as they were in force as at the date of the relevant transfer, but not by the fruits of subsequent collective agreements to which the transferee was not a party.

Given the absence in TUPE of provisions equivalent to art.3(3) expressly limiting the potential enforceability of collective agreements, the employees argued before the Court of Appeal [2010] EWCA Civ 24; [2010] I.C.R. 793 that TUPE simply preserved the provisions of the transferring employees' employment contracts and

made no distinction between the enforcement of provisions deriving from collective agreements and those individually agreed. Moreover, they contended that *Werhof* did not preclude the United Kingdom, in its domestic implementation of the Directive, from applying the dynamic interpretation and what was described as the "conventional application of ordinary principles of contract law to the statutory consequences [of TUPE]" (at [46] per Rimer L.J.). Nonetheless, and consistent with the employer's case that *Werhof* was indistinguishable from the facts in *Alemo-Herron*, the Court of Appeal held that *Werhof* had established the proper interpretation of ARD and rejected the dynamic interpretation in favour of the static interpretation.

The matter reached the CJEU following a reference from the Supreme Court [2011] UKSC 26, in essence of two questions—first, whether the dynamic or the static interpretation should be applied in interpreting ARD and, secondly, if the static interpretation is the correct approach, whether it is open to the national court to construe the relevant domestic provisions more generously—see at [26] per Lord Hope. The CJEU held that the static interpretation is the correct one. Article 3 of ARD:

> "must be interpreted as precluding a Member State from providing, in the event of a transfer of an undertaking, that dynamic clauses referring to collective agreements negotiated and adopted after the date of transfer are enforceable against the transferee, where that transferee does not have the possibility of participating in the negotiation process of such collective agreements concluded after the date of the transfer" (at [37]).

Third party pay determination cannot bind a transferee post-transfer where the transferee does not have a seat at the negotiating table.

From the perspective of the transferee employer who will not now be bound post-transfer by collective pay determination negotiations which it cannot influence, no doubt this decision will be welcome. But what is particularly novel and potentially important about the decision is the analysis deployed by the CJEU in reaching not only its finding that the static interpretation should prevail but also its conclusion (effectively) that Member States should not be permitted to adopt the dynamic interpretation which would be more favourable to employees.

On the CJEU's analysis, ARD does not aim solely to safeguard the interests of employees in the event of transfer but also seeks to ensure a fair balance between the interests of employees and the transferee and that the transferee "must be in a position to make the adjustments and changes necessary to carry out its operations" (at [25]). On this analysis the dynamic interpretation would "limit considerably the room for manoeuvre for a private transferee to make such adjustments and changes" following a transfer from the public sector and this would run counter to the "fair balance" now identified as underpinning ARD (see at [28] and [29]). This interpretative approach was also seen as entirely consistent with and also justified by reference to the European Union's Charter of Fundamental Rights and, in particular, the freedom to conduct a business under art.16 of the Charter. This freedom, as applied to ARD, led the CJEU to conclude that:

> "the transferee must be able to assert its interests effectively in a contractual process to which it is party and to negotiate the aspects determining changes

> in the working conditions of its employees with a view to its future economic activity" (at [33]).

The art.16 freedom would be prejudiced where the employer could not participate in the relevant collective bargaining body, but was bound by its agreements. One can see how this rationale led to the preference for the static interpretation in relation to ARD. But then the CJEU went further—art.3 of the ARD cannot be read as entitling Member States to take measures which are liable adversely to affect the very essence of the transferee's freedom to conduct a business. So not only is the static interpretation correct so far as ARD is concerned; it must also apply in domestic transfer of undertakings legislation to the exclusion of the dynamic interpretation. As provided by its art.8, ARD does not in general preclude Member States from adopting more favourable protection than the minimum requirements of ARD. However, in this specific context—of pay review determination mechanisms to which the transferee is not party—more favourable treatment by domestic legislation is not permitted. The CJEU effectively on this occasion suspended the application of any form of legislative subsidiarity in domestic transfer of undertakings legislation.

Even though the analysis of the CJEU in this case was developed to deal with the specific conflict between the static and the dynamic interpretations, the principles which the CJEU identifies are potentially of more general application. The CJEU's approach appears to present a significant shift of emphasis in how ARD should be interpreted by introducing into legislation previously thought primarily to concern employee protection the balancing of the interests of employer and employee and making relevant the employer's need to make changes necessary to run its business. This approach is certainly not how the transfer legislation has been viewed in the domestic caselaw. By way of just one example, in *OTG Ltd v Barke* [2011] I.R.L.R. 272 (EAT) at [21], the view was expressed that TUPE's primary purpose of employee protection "in any doubtful case must prevail". It will be interesting, to say the least, to see if and how the CJEU's new found, and apparently business friendly, approach to the interpretation of ARD—and by extension TUPE—influences any other aspect of their application.

One area in which such business friendly arguments could be deployed is in relation to the principle that changes made to employees' contractual terms and conditions of employment are void if made by reason of the transfer in question. This is the case even if the employees agree to those changes. The principles that the protection of employment terms on transfer under ARD is a mandatory and inderogable right and that the transferee cannot justify contract changes which are detrimental to the employee on the basis that they are compensated for by other favourable amendments were established in *Foreningen af Arbejdsledere i Danmark v Daddy's Dance Hall AS* (C-324/86) [1988] I.R.L.R. 315, and have been reiterated in many subsequent decisions. These principles made their way into the domestic case law concerning TUPE in the associated decisions in *Wilson v St Helen's Borough Council*; *British Fuels Ltd v Meade and Baxendale* [1999] 2 A.C. 52 and the subsequent decision in *Martin v South Bank University* (C-4/01) [2004] I.R.L.R. 74. This line of authority has caused employers considerable difficulties in relation to their ability, for example, to harmonise the employment terms of the transferring employees with those of their existing workforce.

That ARD is now to be interpreted as entailing a fair balance between the interests of the relevant employees and of the transferee, and should not prevent employers from making the adjustments and changes necessary to carry on their operations, provides scope for an argument that the approach adopted by the domestic cases in applying *Daddy's Dance Hall* is too strict. As *Daddy's Dance Hall* confirms, the objective of ARD is to ensure protection of the employee as against the transferee to the same extent as applied in respect of the transferor. The analysis deployed in *Alemo-Herron* could be utilised to argue that mandatory protection of employment terms post-transfer is no longer appropriate, on the basis that this principle constitutes a fetter on the ability of employers to make changes necessary to carry on their operations. This argument would contend that, once an employee has transferred from the transferor to the transferee on his or her existing terms and conditions of employment, then ARD has done its job in terms of employment protection and subsequent changes should be permitted to the extent allowed for by domestic law and as they could have been pre-transfer. The CJEU's approach—applying a considerable degree of pragmatism to its determination of the issue of principle as to whether the static or the dynamic interpretation should be adopted—may give greater purchase to this argument.

There is more than a little irony in the fact that in *Alemo-Herron* the CJEU has interpreted a European Directive aimed at employment protection explicitly to disallow the application of the orthodox domestic common law dynamic interpretation which would be more favourable to the affected employees. As far back as *McGrath v Rank Leisure Ltd* [1985] I.R.L.R. 323 (EAT), Waite J. noted, in relation to the process of the implementation of ARD into domestic law:

> "the almost insuperable difficulties which faced [the draftsman of TUPE] when he was required to patch new Flemish broadcloth upon the fine weave of our domestic employment law—with instructions to do the minimum damage to either fabric" (at [2]).

The CJEU decision in *Alemo-Herron* may have patched up an important aspect of the proper interpretation of TUPE but the way in which it has done so raises potentially very significant questions about the future direction of travel of the interpretation of both ARD and TUPE.

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