

Case Reports

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Budget considerations can justify indirect discrimination (UK)

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Summary

If an employer has a policy which is indirectly discriminatory and the employer's aim is no more than saving money, the Court of Appeal (CA) has ruled that this cannot justify the discrimination. However, needing to balance the books can potentially be a valid justification for indirect discrimination.

Background

Employers often put forward cost considerations in seeking to justify policies and practices that indirectly disadvantage one or more protected groups. This line of argument is problematic because the European Court of Justice ruled in *Hill – v – Revenue Commissioners* (C-243/95) that “an employer cannot justify discrimination ... solely on the ground that avoidance of such discrimination would involve increased costs”.

The approach in *Hill* was followed by courts and tribunals in the UK. In *Cross – v – British Airways plc* [2005] IRLR 423, the Employment Appeal Tribunal (EAT) interpreted it as meaning that, while a desire to save money cannot by itself amount to a legitimate aim capable of justifying indirect discrimination, cost and budget considerations may be taken into account alongside other factors. This became known as the ‘costs plus’ rule. It was upheld in *Woodcock – v – Cumbria Primary Care Trust* [2012] EWCA Civ 330, where the CA confirmed that “the saving or avoidance of costs will not, without more, amount to the achieving of a legitimate aim”.

The ‘costs plus’ approach has nonetheless come in for significant criticism. One of the rule’s judicial critics,

Lord Justice Underhill, had previously described it as involving an artificial game of “find the other factor”. Underhill LJ now sits as a judge in the CA, so the stage was set for the recent case summarised below to provide a fresh look at the legal position.

Facts

The issues in the case arose from the government’s austerity measures following the financial crisis in 2008, including the imposition of pay restraints across the public sector. As a result, the rate at which probation officers progressed up their pay scales was slowed down from three pay points each year to just one pay point per year. In the case of the claimant, Mr Heskett, this meant that it would take 23 years to progress from the bottom to the top of the pay scale, instead of the seven or eight years it would have taken previously. Mr Heskett argued that this amounted to indirect age discrimination.

The Employment Tribunal (ET) agreed that the policy had a disproportionate effect on younger employees, compared to older employees who were more likely to have reached the top of the pay scale already, so it was potentially indirect age discrimination. The key question was whether the policy could be justified as a proportionate means of achieving a legitimate aim.

Mr Heskett argued that this was all about cost and, according to the ‘costs plus’ rule, avoiding expense could never be a legitimate aim justifying indirect discrimination. Costs and budget considerations could only be legitimate aims when combined with other factors. Rejecting the claim, the ET ruled that this was not just a matter of costs alone and it was legitimate for the employer to seek to live within its means. The EAT upheld the ET’s decision and Mr Heskett appealed to the CA.

Judgment

Dismissing the appeal, the CA unanimously ruled as follows (with Underhill LJ giving the leading judgment):

- It is not legitimate to discriminate purely out of a desire to save or avoid costs. For example, an employer who decides to pay part-timers less per hour than full-timers simply because it is cheaper could not justify that.

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- The ‘costs plus’ rule is correct, but the label should be avoided because the principle needs to be understood differently. It is important to look at the whole story – how can the employer’s aim fairly be characterised? An ‘inappropriately mechanistic approach’ of trying to look for the additional non-cost factor is to be avoided and the total picture needs to be considered.
- The employer in this case was subject to financial constraints which *obliged* it to reduce costs. This was different from costs alone. An employer’s need to reduce its expenditure to balance its books can be a legitimate aim. There is no good basis for ignoring the constraints under which an employer is in fact having to operate.
- Whether any specific policy is justified on the facts depends on a proportionality analysis. The ET was right to find that the pay policy was justified in the circumstances of this case.

Commentary

This case about measures taken in the aftermath of the 2008 recession has taken so long to go through the courts that the CA’s judgment comes just as employers are taking similar cost-cutting measures in the face of new economic turbulence.

To a limited extent, the CA’s judgment makes cost-cutting measures less susceptible to legal challenge. There may be less need for artificial exercises in which employers are advised to reframe the reasons for their actions and identify an additional reason which is not cost. Budgetary considerations may now be more readily recognised as legitimate reasons for adopting policies that have a potentially indirectly discriminatory impact, or for not immediately correcting such policies.

In most cases, however, there will still be arguments to be had over whether indirectly discriminatory policies are justified. The dispute will move to the question of proportionality. In this case, the fact that the pay arrangements were intended to be temporary was a factor in the proportionality analysis. The CA said that employers should be allowed to justify measures that may be a proportionate short-term means of responding to the problem in question, even if they could not be justified in the longer term. This is a helpful clarification.

It should be emphasised that the CA’s decision relates only to cases of indirect discrimination. Some policies may be directly discriminatory – for example, if they reduce severance pay once an employee is aged 65 or over. In the UK, unlike for other protected characteristics, direct discrimination on grounds of age can potentially be justified, but the CA pointed out that the tests for justification are not the same. To justify direct age discrimination, an employer also needs a ‘social policy’ aim such as promoting intergenerational fairness. In

effect, this means that there is a ‘costs plus plus’ rule for direct age discrimination.

Comments from other jurisdictions

Austria (Lukas Wieser and Vera Habe, Zeiler Floyd Zadkovich): This is an interesting judgment as legitimate aims may justify a discrimination on grounds of age in Austria as well. However, there is no Austrian Supreme Court case law dealing with the question of whether the employer’s need to reduce costs qualifies as such a legitimate aim. Austrian legal scholars argue that solely financial burdens or additional costs (without any other justification) do not justify an unequal treatment on the grounds of age (*Hopf/Mayr/Eichinger/Erler*, GIBG2 (2021) § 20 Mn 43).

Thus, Austrian courts may also argue that a legitimate aim is only established if there are further reasons beyond the employer’s desire to save or avoid costs. As ruled by the CA, the reduction of expenditure in order to balance the books may therefore qualify as such a legitimate aim. Thus, the case at hand is very interesting and will provide guidance also for Austrian legal practitioners when determining whether or not a legitimate aim is established.

Germany (Daniel Zintl and Johannes Pinkert, Luther Rechtsanwalts-gesellschaft mbH): In Germany, the General Equal Treatment Act (*Allgemeines Gleichbehandlungsgesetz*, ‘AGG’) exists to avoid discrimination and inequality in employment relationships. According to Section 8(2) AGG it is not possible to justify an agreement which includes that an employee gets less money for work of equal value, because of enumerated reasons from Section 1 AGG, which include special protection regulations. The reasons in Section 1 AGG concern racism, ethnic origin, gender, religion, handicaps, age and sexual identity. But in Germany there is no specific legal regulation of equal treatment of employees in terms of wage increases.

Similar to the British justice system, German law does not legally determine any justifications for indirect discriminatory actions. Rather, any lawful target can be implemented by proportionate means, which means that also in Germany the proportionality-standard plays an important role when it comes to assessing a possible discriminatory action.

The existence of such a legal justification leads to the exclusion of discriminatory actions. It should be noted that the actions themselves must not serve a discriminatory purpose, but only a legitimate purpose. Furthermore, the principle of proportionality must apply.

Savings of wage payment costs for budgetary reasons alone is to be considered as discriminatory, but according to the ECJ decision from 14 February 2019, the situation is different if the wage reduction is economically justified. In this case, a change in salaries can take place

for every new employee of a certain entry date. Resulting indirect discrimination can therefore be justified on the basis of economic imperative. The German courts have so far not opposed this decision.

Consequently, there are parallels to the British interpretation of the law, according to which it is not to be considered legitimate to discriminate against other employees solely out of the desire to avoid costs. Furthermore it is necessary that economic factors be put forward to justify such indirect discrimination. As a result, indirectly discriminatory measures in Germany can also be justified if they appear to be proportionate and there are reasons providing for justification.

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