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06/12/2024

Business and Trade Committee

House of Commons,

London,

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IoD response to the Make Work Pay: Employment Rights Bill Inquiry

About the IoD

The IoD is an independent, non-party political organisation representing approximately 20,000 company directors, senior business leaders, and entrepreneurs. It is the UK's longest-running organisation for professional leaders, having been founded in 1903 and incorporated by Royal Charter in 1906. Its aim is to promote good governance and ensure high levels of skills and integrity among directors of organisations. It campaigns on issues of importance to its members and to the wider business community with the aim of fostering a climate favourable to entrepreneurial activity in the UK.

The IoD welcomes the opportunity to respond to this call for evidence on the Employment Rights Bill. The provisions of the Bill will have significant implications for employers of all sizes and we are therefore pleased to present our views to the Committee.

In the first section, we provide a summary of our key perspectives on the Bill. We then offer more detailed views in respect of the specific questions posed in the call for evidence.

Summary of the IoD view

Feedback from IoD members on the various components of the *Plan to Make Work Pay* strongly suggests that it will have negative impacts on hiring intentions and practices, business confidence, growth, and investment. These negative impacts are in no small part the result of the fact that the development of the policies and drafting of the Bill have been rushed; complex and new legal measures are being rolled out hastily and without sufficient engagement with business and consideration of potential negative economic consequences.

Specific questions

Impact on businesses

1. **What impact will the areas covered by the Employment Rights Bill have on small, medium and large businesses?**

The cumulative impact of the various provisions of the Employment Rights Bill on businesses of all sizes will be both significant and detrimental. Ultimately, the Bill's measures will make the employment of staff more expensive and riskier.

The government's own impact assessment acknowledges that the costs of the reforms will be disproportionately borne by SMEs. SMEs are both less likely to have the in-house HR capacity necessary to be able to absorb additional compliance burdens and to have the financial resources to absorb increased costs related to employment in several areas.

> "Dumping 28 potential changes on SMEs who do not have in house HR is a tough ask to make, many of which will have real financial implications such as SSP from Day One." – Microbusiness, Professional, scientific and technical activities, East of England

> "Covering the cost of enhanced sickness, maternity, paternity, parental bereavement when one person represents such a large percentage of payroll is challenging. [Financial support from government] would massively help small businesses provide provision for employees and even the playing field when compared to large organisations" – Small employer, Other services, Yorkshire and the Humber.

> "This penalises smaller businesses who are less likely to be able to afford these additional costs and remain competitive."- Medium-sized employer, Construction, South West England

2. **What impact will these measures have on staff retention, hiring practices, probationary periods and wages?**

The Bill's measures will have significant impacts on hiring practices, both in terms of the frequency of hiring and the manner in which hiring is conducted.

An IoD survey of 715 business leaders in August 2024 found that 57% would be less likely to hire in response to the implementation of the Employment Rights Bill (Appendix: Figure 1). The expansion of day one employment rights, particularly in relation to protection against unfair dismissal and the consequent increased threat of tribunals, was the most commonly cited single factor for the increased disinclination to hire. However, respondents frequently emphasised the impact of the package as a whole, with an underlying sense that the measures in the Bill reflect a want of understanding of both the realities of running a business and proper consultation with employers.

> "The overwhelming risk and cost will increase the cost and potential cost of hiring… and make the options of hiring junior staff less appealing. It would really help UK businesses if legislation was amended to make hiring staff *more* attractive." Medium-sized employer, Professional, scientific and technical activities, North West England

> "Hiring (and firing) will become materially more onerous, more risky and, consequently, less likely." – Microbusiness, Professional, scientific and technical activities, Scotland

> "At best this will increase the cost of, and slow down, the recruitment process due to more checking and referencing, and at worst it will cause companies (especially early-stage companies and SMEs) to delay or reduce recruitment due to the increased risk of costly employment disputes." – Small employer, Manufacturing, Scotland

> "Two key deterrents for us would be flexibility; we operate in fast-changing industry where being able to adapt is key, furthermore we are a smaller business with limited resources and any additional burden / administrative tasks are likely to deter us from hiring." – Small employer, Wholesale and retail trade, South East England

In addition to this data, IoD research tracks business leaders' headcount expectations. In November 2024, headcount expectations reached their lowest point (-33) since May 2020 (Appendix: Figure 2). While much of the decline compared to October 2024 (-4) is owed to the increase in employers' National Insurance Contributions (NICs), headcount expectations have been declining steadily in the past few months, with October being the first negative reading – meaning that more employers plan to decrease headcount in the coming year than increase it – since late 2020. This decline is due in no small part to the increased costs and risks associated with employing staff resulting from the Employment Rights Bill.

Where employers do hire staff, the nature of the hiring process will change. A prevalent and concerning theme in feedback from IoD members is that they will take fewer risks when hiring staff. The ability of employers to correct recent hiring mistakes without the threat of being taken to an employment tribunal is key to their frequent willingness to hire staff who constitute a greater risk, for example where they do not have the exact experience or qualifications required on paper. Such a trend would have worrying implications for the likelihood of individuals on the fringes of the labour market – whose re-entry into the workforce will be essential if the government is to meet its target of an 80% employment rate – to gain employment.

> "At our organisation we take a chance with some slightly unusual candidates who on paper may not fit the job spec. This is often very successful - but in around 25% of cases we do have to let them go. This will tighten up our recruiting culture and will lead to marginalised candidates not getting a chance." – Medium-sized employer, Real Estate, South East England

> "Most companies know that hiring is expensive and so try to make it work, but we have all made poor recruitment decisions and it is better for everyone if there is an easy exit from these." – Large employer, Health and social work, South East England

Feedback from IoD members also suggests that, where employers do hire staff, they will be less likely to directly employ staff on permanent contracts. Reforms to zero hours contracts in particular will, ironically, in many cases increase precarity in employment due to individuals being engaged on fixed-term contracts:

> "Employing people is becoming a big risk for small entrepreneurs, we are much more likely to go for contract workers now." – Microbusiness, Professional, Scientific and technical activities, North East England

The impact of the Bill on probationary periods will depend on the maximum length of statutory probationary periods and whether the dismissal process is genuinely light touch. Employers are likely to make greater and more formal use of probationary periods than is currently the case, in order to provide themselves with some protection against unfair dismissal claims.

Feedback from IoD surveys suggest that most employers operate 3–6-month probationary periods but, in order to allow for extensions to probationary periods where necessary, one year should be the legal maximum. Were that to combined with a very light-touch dismissal process then the negative impacts of day one protection against unfair dismissal would be reduced. That being said, in an IoD survey of 642 business leaders in October 2024, only 51% of respondents reported that a nine-month probationary period with a light-touch dismissal would partially mitigate the negative impacts of the policy, while 32% responded that it would not alleviate their concerns at all (Appendix: Figure 3).

The rising costs of employment resulting from the *Plan to Make Work Pay* and the increase in employers' NICs will, for some employers, lead to difficult decisions about not only hiring but remuneration for existing and future employees. Employers are unlikely to recoup all costs via reduced remuneration, but it will be a key component for many.

> "[The Bill] won't stop hiring as long as the business is expanding, but it will certainly reduce future benefit increases and may reduce future pay increases to compensate." – Medium-sized employer, Other services, North West England

3. **How will other areas set out in the Plan to Make Work Pay impact businesses?**

Much of the impact will depend on details yet to be specified. However, continued above-inflation increases in the National Living Wage will lead to businesses responding with a combination of not only reduced profits but reducing employment, increasing prices of products, and reducing business investment in other areas (Appendix: Figure 4).

Employers generally have considerable sympathy with the principles underlying the right to switch off, but any Code of Practice which stipulates that employers cannot contact employees outside of working hours, rather than stating that employees cannot be penalised for not responding outside of working hours, would be completely unworkable and, ironically, based on a conception of traditional, non-flexible working patterns out of kilter with the reality in the vast majority of workplaces.

4. **What impact will strengthened protections, such as day one rights, have on the hiring practices of businesses, UK employment rates and UK investment rates?**

As described above, day one protection against unfair dismissal would both disincentivise hiring and lead employers to take a more conservative approach to hiring decisions. Other proposed expansions to day one rights, such as to Statutory Sick Pay (SSP) and parental leave, would act as a further – though not equal – disincentive to hiring. At its core, employers – especially SMEs – are concerned about the potential of these rights to lead to high costs related to employees who have not contributed to their organisations.

5. **To what extent could the Employment Rights Bill cause businesses to offshore employment and continue with weaker workers' protections abroad?**

While we do not consider this likely to be the primary response of employers to the Bill, feedback from IoD members suggests that it will lead to a significant minority of employers shifting employment expansion to outside the UK, particularly in the context of stagnant productivity in the UK workforce.

> "We struggle to hire into certain roles in UK (particularly Product Managers) and therefore we take risk when hiring. If we are unable to take that risk we will come under pressure to hire these roles in the US" – Large employer, Information and communication, South East England
>
> "I will move employment overseas to avoid recruiting new staff in the UK" – Small employer, Manufacturing, London
>
> "[Staff] performance levels are at an all-time low in a tough economy hence why we took an investment visa to live and set up in Texas" – Small employer, Professional, scientific and technical activities, International

Economic growth and wealth creation

How will the Plan to Make Work Pay impact:

1. **Economic growth?**

The *Plan to Make Work Pay* will undermine economic growth by stifling hiring and thus business expansion, as described above.

Certain provisions in the Bill will also undermine employers' flexibility and ability to innovate, and thus growth. Of particular concern are provisions relating to dismissal and re-engagement; by failing to specify that the legislation will apply only to detrimental contractual changes, employers could be prevented from making non-detrimental changes to contracts – such as office location – by the threat of automatic unfair dismissal and a requirement to pay interim relief.

> "There are legitimate times when job roles need to change. Employees should be looked after in a transition but businesses must not be constrained by requirements to retain old jobs. This will limit innovation and competition." – Microbusiness, Education, Scotland

Growth will be further negatively impacted as a result of the increased financial and bureaucratic burdens which will be placed on businesses; even where hiring intentions do not change, businesses' financial sustainability may be undermined, particularly in sectors where profit margins are slim and demand is elastic.

> "Our hiring intentions won't change because we operate in a regulated industry, but the proposed changes will have a financial impact that, as a very small organisation, it will be difficult to absorb." Small employer, Other services, London

Furthermore, where labour market flexibility currently enables employers to take on more work in response to rapid changes in demand, the effective loss of zero hours contracts and the likely contraction of the agency sector will lead some employers to avoid engaging in such additional work:

> "We have employees who are on zero hours contracts because their work is project driven and is not guaranteed, and we can therefore not afford to offer them guaranteed hours… If we were using agency workers, we would likely turn away work that could not be carried out by our own employees rather than get locked into contractual agreements that could lose us money." Small employer, Information and communication, East of England

> “The majority of microbusinesses and virtually all those in the hospitality sector require flexibility in employment to enable growth!” – Microbusiness, Other services, South East England

2. Productivity levels?

The impact of reforms on productivity levels are difficult to predict. However, it is worth noting that recent strengthening of employment rights and increasingly widespread adoption of various forms of flexible working have not reversed the stagnation in the UK’s productivity levels.

3. Rates of investment?

The overall impact of the package on investment is likely to be negative. An IoD survey of 601 business leaders in November 2024 found that investment intentions had fallen to -27, down from -15 in October and the lowest reading since May 2020 (Appendix: Figure 5). While this decline is owed to multiple factors, the increased risk and cost of employment is a key factor.

However, employer investment in automation is likely to increase as they seek to mitigate the impact of the package by reducing their reliance on labour:

> “This will stop me hiring employees - they're going to be too expensive and have no recourse when it comes to taking time off. As an SME times are tight and I'll move to technology replacing people faster because of this.” – Microbusiness, Professional, scientific and technical activities, West Midlands

4. Business start-up rates?

There is a real risk that the increased costs and compliance activity required to meet the demands of the various aspects of the *Plan to Make Work Pay* will deter entrepreneurial activity in the UK. The start-up phase of businesses is already a difficult one with high levels of risk; any addition of risk in people management is therefore unhelpful.

> “I would like the government to speak to businesses and understand the real challenges we face in managing a workforce with our hand tied behind our backs all the time - it is making people management one of the biggest challenges of running a business these days and I feel this is putting off people taking the step into becoming an entrepreneur.” Medium-sized employer, Professional, scientific and technical activities, Wales

5. Employment levels?

In the context of a relatively tight labour market, reduced job creation may not have a significant negative impact on employment levels. However, the impact would be felt with any loosening of the labour market. At the very least, reduced job creation will severely hamper the government’s ability to increase employment levels to its 80% target.

6. What solutions or actions are required by Government, businesses and workers to effectively support the labour market while boosting productivity and protecting workers’ rights?

The following key changes to the *Plan to Make Work Pay* package would assist in ameliorating the negative impacts of the package on job creation and economic growth:

1. Clarifying that changes to provisions around dismissal and re-engagement will only apply where contractual changes are detrimental.
2. Introduce additional protections against unfair dismissal after 12 months of employment, rather than day one.
3. Clarifying that the Code of Practice on the right to switch off will prohibit employers disciplining employees for not responding to communication outside of contracted working hours, rather than prohibiting all employer contact outside of contracted working hours.
4. Retaining existing thresholds for statutory recognition for unions and for industrial action.
5. Remove 'all' from the requirement for employers to take 'all reasonable steps' to prevent sexual harassment in the workplace.
6. Retain one waiting day before employees can access SSP, to prevent abuse of the system.
7. Amend the reference period for guaranteed hours to 26 weeks and make it a right for employees to request, rather than be proactively offered, a contract reflecting hours regularly worked.

I hope you have found our comments helpful. If you require further information about our views, please do not hesitate to contact us.

With kind regards,

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Appendix

Figure 1: IoD Policy Voice results, August 2024 (715 responses)

The government is planning to introduce an Employment Rights Bill within its first 100 days of office. Measures expected in the Bill include: Giving workers the right to a contract reflecting the hours they usually work; Strengthening the statutory code on fire and rehire; 'Day one' employee rights to parental leave and sick pay, and protection against unfair dismissal; Making it unlawful to dismiss a maternity returner for six months after their return to work, except for in specified circumstances; Simplifying the statutory trade union recognition process; Making Statutory Sick Pay available to more workers by removing the lower earnings limit and waiting period.

What impact, if any, would these reforms have on your organisation's hiring intentions?

More likely to hire	2.2%
Less likely to hire	57.2%
No impact	35.5%
N/A	5.0%

Figure 2: IoD Policy Voice results, November 2024 (601 responses)

Comparing the next 12 months with the last 12 months, what do you believe the outlook for your organisation will be in terms of headcount?

Much higher	2.4%
Somewhat higher	19.0%
No change	45.2%
Somewhat lower	14.3%
Much lower	16.7%
N/A	2.4%
Don't know	0.0%

Figure 3: IoD Policy Voice results, October 2024 (642 responses)

Employees will get protection from unfair dismissal from day one of employment, but employers will be able to operate probationary periods during which there will be a lighter-touch process for dismissing an employee who is not right for the job.

To what extent do you think a 9-month probationary period would alleviate any impact on the cost and risk of employment resulting from staff having day one protection against unfair dismissal?

Fully alleviate	8.6%
Partially alleviate	50.9%
Not at all alleviate	31.9%

Don't know	5.6%
N/A	3.0%

Figure 4: IoD Policy Voice results, August 2024 (715 responses)

In the past two years, the National Living Wage has increased from £9.50 to £11.44 an hour. What action/s if any, has your organisation taken in response to these increases? Please select all that apply.

Absorbed part or whole of the cost through reduced profits	29.1%
Offset costs by raising the prices of goods/services	23.4%
Offset costs by reducing employment	18.0%
No actions taken	15.4%
Offset costs by reducing business investment in other areas	12.4%
Increased employee productivity through higher investment in new technologies and/or automation	11.5%
Increased employee productivity through higher investment in training	8.4%
Other	5.0%
N/A	27.7%

Figure 5: IoD Policy Voice results, November 2024 (601 responses)

Comparing the next 12 months with the last 12 months, what do you believe the outlook for your organisation will be in terms of investment?

Much higher	1.8%
Somewhat higher	17.3%
No change	32.6%
Somewhat lower	28.8%
Much lower	17.8%
N/A	1.0%
Don't know	0.7%