



Pension schemes – change of service provider

EMPLOYMENT, PENSIONS AND BENEFITS: BRIEFING 182

The Transfer of Undertakings Regulations rules on ‘service provision change’ may apply if there is a change of service provider.

This may affect pension scheme trustees that outsource to a third party scheme administrator and employers outsourcing to any other professional service provider.

Pension schemes are increasingly considering outsourcing to scheme administrators as a way of controlling costs in the ongoing economic downturn or as part of a longer term strategic decision.

Trustees that outsource the scheme administration and employers outsourcing any other business services, such as payroll or IT, should consider the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE) rules on ‘service provision change’, especially when negotiating the outsourcing agreement.

When will TUPE apply to an outsourcing?

TUPE rules on ‘service provision change’ may be relevant at three stages of the contracting-out process:

- when a particular activity or function is outsourced by a company (TUPE may transfer the customer’s employees to the contractor);
- when there is a switch of contractors responsible for that activity (TUPE may transfer the first contractor’s employees to the new contractor); and
- when the activity or function is taken back in-house (TUPE may transfer the contractor’s employees to the customer).

Broadly, if TUPE applies, all employees working in (and assigned to) the activity or function before its transfer to the new contractor will automatically become employed by the new contractor on their existing terms and conditions of employment. If the service is taken back in-house, the contractor’s employees transfer to the client.

It may be seen as an unfair dismissal if an employer dismisses the transferred employees or substantially changes employment terms, to the employees’ material detriment, for reasons connected with the transfer. It may not be an unfair dismissal if this is done for a reason connected with the transfer that is ‘an economic, technical or organisational reason entailing changes in the workforce’.

The transferee and transferor employer have an obligation to inform, and in certain cases consult, representatives of their own employees that may be affected by the transfer or by measures taken in connection with the transfer.

Can TUPE apply when outsourcing a professional service?

There has been some doubt on whether the TUPE rules apply when a professional service is outsourced.

The Employment Tribunal’s decisions in *Royden and others v Barnetts Solicitors* (2009) and *Hunt v Storm Communications* (2007) suggest that the rules on service provision change can apply in these circumstances.

How can this affect pension schemes?

This may affect pension trustees outsourcing, changing third party scheme administrator or bringing the administration back in-house.

If the trustees’ employees (or the scheme sponsor’s employees) previously carried out the administration of

the scheme, these employees may transfer to the third party scheme administrator on an original outsourcing.

If trustees switch their third party scheme administrator, the previous administrator's employees may transfer to the new administrator. This risk may increase the charge levied by the new administrator.

If a pension scheme ends an outsourcing agreement and takes the administration back in-house it may inherit some employees from the former third party administrator.

Employers outsourcing a professional service should also consider the possible TUPE implications.

Will TUPE apply in all outsourcings?

Regulation 3(1)(b) of TUPE restricts the circumstances when employees may transfer in an outsourcing. Employees may only transfer if immediately before the change of service provider:

- there is an 'organised grouping' of employees whose 'principal purpose' is to carry out activities on behalf of the client;
- the client intends that the activities will continue after the transfer and are not in connection with a single specific event, or task, of short-term duration; and
- the activities concerned do not consist wholly or mainly of the supply of goods for the client's use.

These conditions should ensure that TUPE only applies if an organised grouping of employees provides a service to a particular client. Guidance issued by the Department for Business, Enterprise and Regulatory Reform (BERR) commented that these conditions are: 'intended to confine [TUPE's] coverage to cases where the old service provider (ie the transferor) has a team of employees in place to carry out the service activities and that team is essentially dedicated to carrying out the activities that are to transfer (though they do not need to work exclusively on those activities).'¹ However, it is worth noting that a single employee can constitute an 'organised grouping of employees' under TUPE.²

TUPE should not apply if the pension scheme is serviced by several of the scheme administrator's employees on an

inconsistent basis or if a dedicated team provides services to a number of clients.

Furthermore, even if regulation 3(1)(b) is satisfied (ie there is an organised grouping of employees whose principal purpose is to carry out activities for the client), only employees 'assigned' to the service that is being outsourced will transfer under regulation 4 of TUPE.

In practice, it may be difficult for an employee to prove that enough of their duties are 'assigned' to the service if they have split duties and responsibilities (ie only part of their time is spent doing work on the customer's outsourced service). In *Royden*, the tribunal only transferred employees whose duties mostly consisted of work done for the relevant customer (all other work was described as 'a relatively peripheral element of [their] duties'). The tribunal refused to transfer other employees because considerably less than half their work related to the transferred service.

What should trustees do?

Trustees cannot prevent TUPE's application by inserting a contractual term in the outsourcing agreement. However, trustees that are looking to outsource should consider protecting themselves (or any later outsourcer) from any future employment liabilities. For example, they may ask for an indemnity from the third party administrator when negotiating the contract.

For background see our client guide: *Employment aspects of outsourcing* (May 2006).

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¹ The Department for Business, Enterprise and Regulatory Reform's guidance: *A guide to the 2006 TUPE Regulations for employees, employers and representatives – March 2007*. This is available from the Department of Business Innovation and Skills' website.

² See definition of 'organised grouping of employees' in regulation 2(1) of TUPE.