

A man's head is visible, peering over a white desk. He is looking towards the camera with a slight smile. The room is filled with tall stacks of papers and folders on both sides of the desk, creating a narrow aisle. The lighting is bright, coming from above, casting soft shadows. The overall scene suggests a busy office environment.

# Key Facts in Employment Law



A report by **The Federation of Small Businesses**



The Federation of Small Businesses (FSB) is the UK's largest lobby organisation representing the self-employed and owners of small businesses. Founded in 1974, it now has over 210,000 members across all industries, trades and services. It is a non-party political organisation that exists to promote and protect the interests of all those who own and manage their own business. Together, FSB members employ 2.5 million people and turn over more than £10 billion a year<sup>1</sup>. Small businesses need flexibility in order to grow and thrive but rigid employment legislation can make it very difficult for small businesses to deliver potential benefits within the UK. By the nature of their size, small businesses offer greater scope for a close working relationship between employee and employer. This allows for a fluid, informal flexibility, to the benefit of both parties. The FSB believes it would be detrimental to both employer and employee to impose further regulations to try to formalise this arrangement.

Over the last decade, there has been a significant increase in UK and EU employment legislation, originating from both the EU and the UK. The FSB strongly supports a mutually ethical relationship between employer and employee, but has concerns that if the legislative pendulum swings too far in favour of the employee, that same legislation will cause the opposite effect of what it set out to achieve.

The following statistics and facts were gained from the FSB Employment Survey, which was carried out using an online questionnaire on the FSB website. Members were alerted to the questionnaire by email. It was available for members to complete for two weeks in August 2006. 2826 responses were received.

<sup>1</sup> FSB 2006; *Lifting the Barriers to Growth in Small Businesses, 2006*



## Complex regulation and administrative burdens deter employers from creating jobs

In the FSB Employment Survey, 65% of businesses had employees, whilst 35% did not. Of those businesses without employees, respondents had to identify the three main reasons preventing them from employing. The most common results were as follows:

- Employees considered too great a business risk ..... 36%
- The complexity of employment legislation ..... 32%
- The overall burden of red tape and regulations ..... 31%
- The volume of employment legislation ..... 25%

This shows very clearly that the business community is deterred from creating employment opportunities by the threat of legislation. This should be of significant concern to policy makers, both at EU and UK level, who are looking to small businesses to create jobs in the future. If businesses avoid taking on employees due to fear of employment legislation, the objective of encouraging business growth and increasing employment opportunities will be more difficult to achieve.

## The impact of employment legislation

It is an established fact that many small businesses find employment legislation problematic. When asked about the three most problematic areas of legislation, the responses were:

Legislation	Percentage
Dismissal and grievance rules .....	65%
Parental, paternity or maternity leave.....	52%
Parental, paternity or maternity pay .....	34%
Redundancy .....	31%
Working Time Regulations.....	27%
Right to request flexible working .....	26%
National Minimum Wage.....	26%
Disability discrimination.....	14%
Other.....	9%
Equal Pay and Conditions .....	6%
Race discrimination .....	5%
Sex discrimination.....	5%

**Recommendation >**

The volume and complexity of regulations should be reduced and simplified. Depending on the sector, some regulations are more burdensome than others. It is the cumulative effect that is excessive. However, dismissal and grievance rules are the greatest cause of complaint in almost all sectors. It is crucial that the fear of being taken to court does not stop businesses from taking on employees.

**Recommendation >**

Small businesses do not have the same Human Resources facilities as larger organisations. They rely heavily on guidance from sources such as trade associations, central government websites, HR specialists and accountants to ensure that they are complying with regulation. This is both costly and time consuming.

It is also important to recognise that as most small business owners deal with the paperwork relating to employment legislation themselves, they cannot be expected to be experts, and flexibility must be shown in circumstances where employers have inadvertently not complied with the legislation due to a misunderstanding in the interpretation.

**The most burdensome legislation**

The survey also looked at the reasons why the legislation was considered so problematic. Respondents were asked to indicate the reasons for the employment legislation being considered so burdensome:

- 50% said it was the financial cost of compliance
- 38% said it was the increased threat of legal action
- 30% said it was the time spent on administration in order to comply
- 15% said that it was the difficulty in understanding the requirements of the legislation



**Employers and administration**

The administrative burden on employers is an important factor for small businesses as 78% of the business owners said that they dealt with the paperwork relating to employment legislation themselves. 17% relied on the help of an employee whilst only 3% used an external HR specialist.

This shows how important it is to keep legislation as simple and jargon free as possible. It also proves how small business owners are very exposed to the administrative burden created by employment legislation. It needs to be recognised that, taken in isolation, it is relatively achievable to comply with most regulations, but when they are cumulatively applied, the resulting burden creates considerable difficulties for the small business community.



**Maternity and Paternity Leave**

**Maternity Leave**

Small businesses wish to be as flexible as they can with regard to maternity and paternity issues. However, some businesses experience considerable difficulties, both with administration and in relation to continuity of work. Small businesses can struggle with the impact of losing a skilled member of staff. One member of staff will make up a significantly higher percentage of the overall workforce than one individual in a larger organisation.

The survey looked at the issues surrounding maternity leave in more detail. In the last 5 years:

- 35% of the sample had experienced one or more employees taking maternity leave
- 80% of those who had experienced one or more employees taking maternity leave said that it had had a negative impact on their businesses
- 63% considered that dealing with paperwork, understanding legislation and calculating pay was a significant problem

**The most burdensome aspect of maternity leave**

- The loss of a skilled employee from the workforce .....70%
- The uncertainty surrounding the return to work date or about contacting the employee during leave .....46%
- Locating a temporary replacement worker .....39%

**Paternity Leave**

One quarter of FSB members surveyed had experienced an employee taking paternity leave. However, with the introduction of increased paternity rights, this figure is likely to increase. 73% of those who had experienced paternity leave said that it had a negative impact on their business and over 80% said that this was again due to the loss of a skilled employee from the workforce.



## Recommendation >

### Employee holiday entitlement

Recent legislation has meant that holiday entitlement in the UK is now set at 28 days statutory minimum to include bank holidays. Previously, employers were allowed to absorb the 8 annual bank holidays into the statutory 20 days. The FSB supports a good work/life balance but is concerned that this steep increase could affect some of the members negatively, many of whom are also trying to meet the extra costs of the NMW increase.

#### The FSB found that:

- At the time of the survey, which was prior to the introduction of the extended Annual Leave legislation, 37% offered their employees the statutory minimum entitlement inclusive of public and bank holidays
- The remaining 63% offer their employees the statutory minimum in addition to bank holidays
- Over 50% of all respondents said the new legislation would have a negative effect on their business



### Employing migrant workers

Immigration is an area of growing complication and significance for the small business community. With new Member States joining the EU, confusion over which workers are legally entitled to work has grown.

- 84% have never employed anyone from outside the European Union
- 78% of respondents said it was relatively difficult to determine whether a worker is legally entitled to work in the UK
- Within the last five years, 8% had to apply for an employee Work Permit
- The Work Permit application procedure is considered time consuming, costly and complex to understand



### National Minimum Wage

The National Minimum Wage (NMW) was introduced in 1999. For the initial period, the NMW was set at a level which did not damage the competitiveness of businesses. However, recent years have seen the NMW rise consistently above the level of inflation until the proposed rise for October 2007. As many small businesses operate on a tight margin, even a small increase in cost is hard to absorb. In order to offset the impact of the NMW, many small businesses are forced to reduce working hours and increase prices.

30% believed that the introduction of the NMW in 1999 had had a direct negative impact on their business. The main impacts on these businesses has been reduced profit margins (72%), increased prices (56%) and a reduction in employees (36%).

In total, a third of respondents had to up-rate workers as a result of the 2006 increase. The main effects were reduced profit margins and increased prices, and 13% had to reduce the number of employees.

## < Recommendation

Increases in the NMW should be kept strictly in line with inflation. It is crucial that the government effectively communicates employment legislation issues such as the NMW to small businesses. The best source of such information is HM Revenue and Customs who are in communication with every employer over PAYE matters.

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Copies of this publication may be obtained by writing to: Federation of Small Businesses  
2 Catherine Place, London SW1E 6HF

**Telephone:** 020 7592 8100

**Facsimile:** 020 7233 7899

**email:** [london.policy@fsb.org.uk](mailto:london.policy@fsb.org.uk)

**website:** [www.fsb.org.uk](http://www.fsb.org.uk)

**Written by:**

Lucie Goodman

*Designed on behalf of the Federation of Small Businesses by*

**Hutton Design, Long Road,**

**Paignton, TQ4 7BB**

**Telephone: 01803 668718**

**Fax: 01803 557148**

**email:** [luke@huttondesign.net](mailto:luke@huttondesign.net)