THE NOTION OF THE EMPLOYER IN MULTILATERAL ORGANISATIONAL SETTINGS

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ABSTRACT

This thesis explores the notion of the employer in English employment law. It seeks to develop a functional reconceptualisation of that notion in the hope of overcoming the theoretical and practical problems resulting from the tensions inherent in the current approach.

The first part of the thesis analyses the notion of the employer as counterparty to the contract of employment. Two conflicting strands emerge: the employer is simultaneously identified as a single party to a bilateral contract (the unitary strand) and defined through the exercise of a range of employer functions (the multi-functional strand). As a result of this tension, full employment law coverage is restricted to a narrow paradigm scenario where a single legal entity exercises all employer functions. Modern economic developments, from the rise of employment agencies and service companies to corporate groups and Private Equity investors, have however increasingly led to the joint exercise of such functions across multiple entities.

The second part illustrates the practical implications of these developments: regulatory obligations are placed on inappropriate entities, and workers may even find themselves without recourse to any employment law protection. An additional chapter compares this situation with the notion of the employer in German law, where a sophisticated apparatus has been developed in order to address the particular challenges of employment in multi-entity scenarios, in particular in corporate groups.

On the basis of these observations the final part of the thesis then proposes a reconceptualised notion. The employer is defined as the entity, or combination of entities, exercising functions regulated in a particular domain of employment law. Each of the two strands of the current notion is addressed in turn to demonstrate how this more openly multi-functional approach addresses the rigidities of the current notion without abandoning an underlying unitary conceptualisation. It is hoped that the resulting notion of the employer will be able to place employment law obligations on the entity, or combination of entities, exercising the relevant employer functions, regardless of the formal legal organisation of the enterprise in question.

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ACKNOWLEDGMENTS

The author gratefully acknowledges the support of the Arts and Humanities Research Council (*Studentship AH/I012826/1*) in funding this doctoral research project, and Magdalen College, Jesus College and St John's College, Oxford in providing institutional support and homes. Columbia Law School, New York, and the Max Planck Institute for Comparative and International Private Law, Hamburg, kindly extended visiting researcher privileges.

This thesis could not have been written without the support of many individuals, and I am grateful to my teachers, colleagues and friends for their insights, comments and criticism. I am particularly grateful to my parents, Professors Franz Karl and Ulrike Prassl, for giving me a taste of academic life and supporting my own meanderings down that route; and to Abi Adams, whose love, joyful energy and encouragement sustain me every day.

The ideas presented have benefitted greatly from discussions with my examiners, Professors Paul Davies FBA QC and Simon Deakin FBA, the members of the Oxford labour and company law community, as well as scholars in London, Cambridge and beyond. Above all, however, I am deeply grateful to my *Doktorvater*, Professor Mark Freedland FBA QC, for his kind guidance and unfailing support.

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INTRODUCTION

Employment law has traditionally been focussed on analysing and regulating the labour market from the position of the employee;[1] in spite, perhaps, of Lord Wedderburn's famous remark that '[m]ost workers want nothing more of the law than that it should leave them alone'.[2] What started out as the purpose of employment law, in the sense of rebalancing the employee's inequality of bargaining power inherent in the employment relationship,[3] however, soon began to impact on the conceptual question as to which apparatus could best achieve that aim. The wage-taker's status, as an employee, self-employed contractor or later worker thus became one of, if not indeed the, key enquiry of employment law.

Refocusing the Enquiry

This thesis unequivocally accepts the worker's perspective as the appropriate focus for employment law's fundamental concerns.[4] It does set out to question, however, the extent to which a *conceptual* focus on the worker to the exclusion of other concepts may have come to hamper that larger enterprise. Over more than a century, a considerable amount of case law and scholarship has built up to develop, adapt and refine a series of common law tests to determine on which side of the 'binary divide' or the more recent tri-partite scheme any given worker should fall. That model of

1 The terms employment and labour law are used interchangeably throughout this thesis.

2 K Wedderburn, *The Worker and the Law* (2nd edn Penguin 1971) 1.

3 M Freedland and P Davies, *Kahn-Freund's Labour and the Law* (Stevens 1983) 14, 69.

4 For recent discussion, see M Freedland and N Kountouris, *The Legal Construction of Personal Work Relations* (OUP 2011) 364ff (The Personal Work Profile).

employment regulation was seriously challenged by economic and social developments, particularly as regards the scope and application of employment law norms in increasingly complex scenarios, from the development of 'atypical' forms of work [5] to new economic models resulting from the vertical disintegration of enterprise.[6] The long-diagnosed crisis in the fundamental concepts of labour law[7] has therefore become 'if anything more serious, so far as employment contracts are concerned.'[8]

Labour law's near-exclusive focus on the notion of the employee has played a significant part in precipitating this crisis, by allowing a conceptual vacuum to develop on the non-worker side of the employment relationship, filled by nothing more than a vague notion reminiscent of old concepts such as the servant's master. This impact was dramatically exacerbated by developments in the structure and organisation of the modern enterprise. Just as workers have become a very heterogeneous group, so have the firms employing them: there is frequently more than one entity involved in the organisation of work, as a result of the facility with which corporate group structures can be set up and controlled, or with which labour can be sourced from external providers.

As a result of the traditional focus on notions of the employee and the concomitant neglect of the notion of the employer, however, the regulatory responses to increasingly complex work relationships were once again primarily focussed on the

5 S Fredman, 'Labour Law in Flux: The Changing Composition of the Workforce' (1997) 26 ILJ 337, 339.

6 H Collins, 'Independent Contractors and the Challenge of Vertical Disintegration to Employment Protection Laws' (1990) 10 OJLS 353, 356.

7 K Wedderburn, R Lewis and J Clark (eds), *Labour Law and Industrial Relations: Building on Kahn-Freund* (Clarendon Press 1983) vi.

8 M Freedland, *The Personal Employment Contract* (OUP 2003) 26.

definition and position of the worker.[9] The crucial problem with this approach is its assumption of a high degree of homogeneity in employment scenarios generally, and employers in particular. Even a very preliminary sketch of factual situations has shown that this will increasingly rarely be the case; as long as attention remains focussed on the employee category and related secondary conceptions, however, it will be very difficult to address the relevant questions. Indeed, as Freedland and Davies have noted, there may well be a link between this limited focus and the increasing inefficiencies of the current situation, where technicalities create strong avoidance incentives.[10]

Employment law is not alone in its difficulty in grappling with new multilateral organisational models[11] and the resulting complex relationships across legally distinct entities.[12] Their negative impact, however, can be particularly harsh in employment law,[13] which despite conceptual crises and challenges appears to remain set within its traditional techniques and conceptual frameworks.[14]

The answer, therefore, lies in an enquiry into the legal notion of the employer; both as it has been historically received in the common law and as to how it could develop in future within that framework. An extensive discussion of this perspective is

9 In domestic law, see eg the extension of anti-discrimination rights to 'contract workers': *Harrods Ltd v Remick* [1998] ICR 156 (CA). At EU level, see eg the equality duty with comparative workers: Directive (EC) 2008/104 of the European Parliament and of the Council of 19 November 2008 on temporary agency work [2008] OJ L327/9.

10 M Freedland and P Davies, 'Labour Markets, Welfare and the Personal Scope of Employment Law' (1999-2000) 21 CLLPJ 231, 235, 238.

11 G Teubner and H Collins, *Networks as Connected Contracts* (Hart 2011) 98ff.

12 R Gilson, C Sabel and R Scott, 'Braiding: the Interaction of Formal and Informal Contracting in Theory, Practice and Doctrine' (2010) 110 Columbia Law Review 1377, 1389.

13 L Benería 'Shifting the Risk: New Employment Patterns, Informalization, and Women's Work' (2001) 15 International Journal of Politics, Culture and Society 272, 348.

14 S Deakin, 'The Comparative Evolution of the Employment Relationship' in G Davidov and B Langile (eds), *Boundaries and Frontiers of Labour Law* (Hart 2006).

long overdue. Conceptually, numerous detailed accounts of the specific legal issues facing different types of atypical workers have been developed in recent years. This has yet to be matched by a similarly extensive body of scholarly thought on the employer side: there might be just as many variations on the work-taking side of personal employment relationships. From a regulatory perspective, the vast majority of measures regarding employers continue to be framed in terms of single entities conforming to a unitary paradigm, thus often imposing liability at a single level even if key decisions regarding the undertaking are taken by multiple entities.

Outline of the Argument and Thesis Structure

The central argument put forward in this thesis is the idea that the current notion of the employer is riddled with internal contradictions, as a result of which employment law coverage can quickly become incoherent or incomplete in complex, multilateral settings. These problems can only be addressed by a careful reconceptualisation and the development of a more openly functional understanding of the notion of the employer.

The thesis is loosely divided into three parts, each reflecting a particular step in that endeavour. Part I focuses on the traditional notion of the employer, and explains how it has increasingly come under pressure. A first chapter explores two potentially contradictory strands of the received common law notion: the employer has come to be characterised as both a unitary and a multi-functional concept. The resulting tension does not readily become apparent in the traditional paradigm model of a single employer. Chapter two, however, sets out a range of multilateral situations where employer functions are shared across or parcelled out between multiple entities. The two specific contexts to be explored are temporary agency work, where functions are divided between an employment agency and an end-user business, and Private Equity

(PE) investee companies, where the PE management company is closely involved in day-to-day decision-making.

Part II then explores the implications of the notion under pressure, in order to demonstrate the significant practical impact of the tension inherent in the current notion of the employer, and to lay the groundwork for the final part. Chapter three demonstrates the fragile scope of employment law coverage, beginning with the near-complete inapplicability of protective provisions in the triangular agency work context. Discussion then turns to the incomplete and incoherent coverage that results from an inability to identify the relevant employer in complex corporate structures, as illustrated in the context of employee consultation in collective redundancies and transfers of undertakings. Chapter four then turns to a comparative excursion, analysing the conceptual apparatus developed in German employment and company law in response to the prevalence of large corporate groups. Put together, these chapters provide some of the fundamental criteria against which subsequent developments can be evaluated.

The third part turns to a reconceptualisation of the notion of the employer. Building on the specific deficiencies identified in previous parts, it proposes a careful modification of the existing notion. To this end, chapter five explores the multi-functional strand: it develops the very idea of a functional notion, and shows different avenues in existing law through which that approach could be operationalised. Chapter six, finally, returns to the need for a single notion to ensure coherence across different domains of employment law. It re-examines each of the aspects of the unitary notion as set out in chapter one to demonstrate how the law has developed in those respects, and sets out a subtle reconfiguration of the unitary idea(l) in response. A brief overall conclusion tests whether the reconceptualisation has been successful, both in practical terms and by addressing the fundamental tension head-on.

Scope and Methodology

In order to facilitate analytical clarity within the limited space available, two limitations of scope are necessary. The first one of these is as to the range of relationships under examination: the focus of the present thesis is firmly on the employing entity as the work-taking counterparty to the contract of employment. This is not to suggest that the notion of the employer is analytically distinct in other personal work relations as a matter of logical necessity – in fact, many aspects are likely to be shared across all contracts to personally execute labour. As the paradigm of employment relationships in the common law, the contract of service provides the most appropriate core model to embark on an analysis of what it means to be an employer. This focus on the contract of employment further means that, for present purposes, the collective dimension of relationships between workers and multiple employers cannot be discussed in great detail. As an area heavily regulated by statutory intervention, its impact on the notion of the employer might at first appear somewhat limited; where relevant, definitional provisions will nonetheless be drawn upon to illustrate particular challenges.

A final point to be addressed is the change in methodology to be deployed at different points of the thesis. Writing in the context of constitutional law, Dicey once noted that the

> possible weakness [of traditional common law methods of reasoning and analysis] as applied to the growth of institutions, is that it may induce men to think so much of the way in which an institution has come to be what it is, that they cease to consider with sufficient care what it is that an institution has [– and here the verbs "should" and "could" must be added –] become.[15]

[15] A Dicey, *Introduction to the Study of the Law of the Constitution* (Macmillan 1885) Preface to the First Edition vii (as cited by C Harlow, 'Changing the Mindset: The Place of Theory in English Administrative Law' (1994) 14 OJLS 419, 426). See also A Robens, *Report of the Committee on*

The structure of this thesis is designed to overcome this weakness by consciously moving through the three steps implicit in Dicey's analysis and looking at what the institution or notion of the employer is at the moment ('*has become'*), what it *could* be and in the light thereof what it *should* be. Parts one and two operate within the realm of existing law, applying a descriptive-analytical framework to tease out the *is*. They identify the underlying tension between two distinct strands of reasoning in the received common law notion, and demonstrate its implications across a wide range of potential factual scenarios. Part two simultaneously serves as a starting point for the analysis of what the notion *could* be, by looking at a range of potential solutions. The chapters of part three continue with this analytical-descriptive approach, insofar as they draw on existing techniques and emphasise the feasibility of different models within current frameworks. At the same time, they mark a break with the previous chapters' limitations, turning to an openly normative approach to suggest that the notion of the employer *should* become a more overtly functional one, by proposing specific reforms to each of the two strands identified at the outset.

This shift from the analytical-descriptive to the normative in part three is not a radical one, however. In eschewing a complete departure from the descriptive, the *should* carefully builds on the *could*: the functional approach advocated will go no further than necessary to resolve existing tensions, and remains as close as possible to the existing framework to address that fundamental problem on its own terms, seeking 'to apply established legal principles to [multilateral organisational settings], and then gradually to adapt these principles.'[16]

Health and Safety at Work, Cmnd 5043 (London 1972) 3 [41]: 'The greatest obstacle [to proposed changes] will be not so much the intrinsic complexities of the subject as the fact that many of the arrangements under review are long established. In the words of Bagehot (*Physics and Politics*) "one of the greatest pains to human nature is the pain of a new idea".'

[16] D Marsden, '"The Network Economy" and Models of the Employment Contract' (2004) 42 BJIR 659, 671.

PART I
A NOTION UNDER PRESSURE

The contract of employment is the central gateway to employment rights in English law.[1] In determining whether a relationship falls within its scope, the courts have traditionally focussed on analysing whether an individual can be classified as an employee. As a result, the notion of the employer has been neglected in both judicial and academic discussions,[2] leaving it inchoate and built on unquestioned or even unstated assumptions. The first part of this thesis sets out to elucidate the notion of the employer by identifying two contradictory conceptions inherent in the current approach; and to show how the resulting tension increasingly leaves workers without recourse to legal protection.

A unitary conception, first, assumes that the employer must always be a single entity: the counterparty to the employee in the contract of employment. A multi-functional conception, on the other hand, defines the employer by reference to the exercise of various functions or roles. A particular 'function' of being an employer in this sense is one of the actions employers are entitled or obliged to take within the open-ended scope of the contract of employment. With the advent of multilateral work settings, from employment agencies to complex corporate group structures, the exercise of such functions is increasingly shared between multiple entities.

1 Employment Rights Act 1996 (ERA), s 230.

2 With the notable exception of H Collins, 'Ascription of Legal Responsibility to Groups in Complex Patterns of Economic Integration' (1990) 53 MLR 731; S Deakin, 'Commentary. The Changing Concept of the 'Employer' in Labour Law' (2001) 30 ILJ 72; J Fudge, 'The Legal Boundaries of the Employer, Precarious Workers, and Labour Protection' and P Davies and M Freedland, 'The Complexities of the Employing Enterprise' in G Davidov and B Langile (eds), *Boundaries and Frontiers of Labour Law* (Hart 2006).

The first part of this thesis is structured as follows. Chapter one explores the received notion of the employer in English law. Chapter two then turns to address the resulting tensions in the notion of the employer. Its unitary, yet multi-functional conception is not merely a doctrinal problem for employment law scholarship, but has far-reaching implications for the scope of employment regulation. Once several parties jointly exercise employer functions the rival conceptions suggest conflicting outcomes, as the unitary notion grapples unsuccessfully with the complex arrangement. This leads to regulatory obligations being placed on inappropriate entities, or even a complete breakdown of employment law coverage in situations where no single employer can be identified.

CHAPTER I
THE NOTION OF THE EMPLOYER

The opening section of this chapter addresses the apparent absence of case law defining the notion of the employer, and suggests how decisions on the classification of workers may be used instead for that purpose, given the close contractual link between the parties. Section two then charts the development of the unitary conception, showing how the employer has come to be understood as a single entity in all circumstances. [3] As will be seen, this is rooted to some extent in the anthropomorphic notion of the master, a logical extension of the very origins of the employer–employee relationship in the law of Master and Servant.[4] A single entity definition is furthermore intrinsic to the law's perception of the wage/work relationship as a contractual one, between two parties conceptualised in personal and individual terms.[5] The unitary notion also accords with prevailing economic theories of the firm as an internal market place, where traditionally bargained-for transactions are subsumed into a single enterprise.[6] As a result, limited liability companies have taken on the mantle of the master in employment law, becoming a modern example of

[3] The present use of the word 'unitary' is not the only one seen in the literature. In Deakin's work on the evolution of the contract of employment, for example, 'unitary' denotes the single status that has emerged for all employees, distinct from that of independent contractors. See eg S Deakin, 'The Evolution of the Contract of Employment, 1900 to 1950 - the Influence of the Welfare State' in N Whiteside and R Salais (eds), *Governance, Industry and Labour Markets in Britain and France - The Modernising State in the Mid-Twentieth Century* (Routledge 1998) 225.

[4] S Deakin and F Wilkinson, *The Law of the Labour Market* (OUP 2005) 43.

[5] M Freedland, *The Personal Employment Contract* (OUP 2003) 40.

[6] R Coase, 'The Nature of the Firm' (1937) 4 Economica 386.

the unitary paradigm. As a matter of company law, an incorporated company is a separate legal entity, distinct from its directors and shareholders, and represented as a single unit towards the outside world.[7] This unitary corporate personality has been readily identified with the personal master or employer.

Section three re-examines the traditional tests for employee status, including control, economic reality and business integration, to show that a unitary conception is not a necessary consequence of the current approach to identifying the scope of employment rights, as the tests would work equally well in a multilateral setting. Seen from this perspective, a competing multi-functional conception emerges: the employer is defined as the entity exercising various specific functions. Five such functions can be identified, from control over the inception and termination of the employment relationship to the management of market risk. The final section then shows how the resulting tension between a unitary and a multi-functional conception comes to the fore in situations where more than one entity becomes involved in the exercise of employer functions.

SECTION I: THE CONTRACT CONUNDRUM

The absence of case law discussing the notion of the employer has already been noted: it is striking that outside pockets such as triangular employment relationships, there are comparatively few decided cases on the question of the nature of the employer, while there is an abundance of judgments on the definition of employees, workers and dependent labour more generally. Upon closer inspection, however, a peculiar feature of that case law, which in other contexts frequently presents major problems, means that most decisions are equally relevant to the question at hand: the contract conundrum. The legal institution of the contract is central to English employment law,

[7] Davies and Freedland (n 2).

most obviously as a key notion in the common law of employment. Through the dramatic increase of legislative activity in the labour market from the second half of the twentieth century onwards,[8] contract gained an additional important function, which may well be in the process of eclipsing the former: it is a legal relationship that confers an externally defined status on its parties. This latter function as a gateway to statutory rights and duties is illustrated in the interpretative provisions of the Employment Rights Act 1996, which simply provide that '"employee" means an individual who has entered into or works under […] a contract of employment.'[9]

Large parts of the British system of labour market regulation are thus designed to hinge on this status, the definition of which is left to the common law.[10] Cases disposing of questions as diverse as obtaining particulars of employment,[11] health and safety provisions,[12] and collective representation rights[13] thus have to deal with the issue of the claimant's status as an initial hurdle. The definition of an individual's legal position, however, traditionally takes place in a rather circular line of enquiry, where two analytically distinct questions become intertwined: that as to the existence and definition of a contract of service and that as to the definition of its parties. On the one hand, both employee and employer could be seen as parties to a contract of service. On the other, a contract of service can only come into existence if both parties to it show the necessary features of employer and employee. Whilst puzzling in some analytical contexts, the resulting conundrum is a useful basis for the present work: it

8 Deakin (n 3) 225.

9 ERA 1996, s 230(1).

10 The same is true for the more recent notion of the worker: ibid, s 230(2).

11 *Carmichael v National Power Plc* [1999] 1 WLR 2042 (HL).

12 *Ferguson v John Dawson Ltd* [1976] 1 WLR 1213 (CA); Construction (Working Places) Regulations 1966, SI 1966/94, reg 28(1).

13 *O'Kelly v Trusthouse Forte Plc* [1984] QB 90 (CA).

facilitates deduction of information about the notion of the employer from pronouncements on the notion of the employee. The decisions are, after all, also on the question of the existence of a contract – and thus in turn on the nature of both, rather than merely one, of the parties to it.

This point is further underscored by the idea of reciprocity which lies at the heart of the bilateral contractual agreement between employer and worker.[14] In *Devonald*,[15] the Court of Appeal implied an obligation on the employer from a contractual duty on the employee. The plaintiff workman had been dismissed following the closure of the employer's tin plant, and claimed for loss arising from the latter's failure to provide him with work during a notice period. The Court made it clear that the contract was a two-sided bargain,[16] and that the employer's duty was a 'necessary implication' of the employee's binding obligation to work.[17] Translated into the present context, the idea of duties implied from obligations means that an analysis of factors that make an individual an employee will equally allow conclusions to be drawn about the notion of the employer.

While the distinction between criteria for the existence of a contract of service and the definition of the parties thereto might thus pose a challenge in some contexts, it is at present an advantage that makes a large body of case law available for detailed analysis.

The enquiry to follow is focussed on the contract of employment and the parties to it. It is nonetheless important briefly to look beyond this subset, noting especially that

[14] Deakin and Wilkinson (n 4) 43.

[15] *Devonald v Rosser & Sons* [1906] 2 KB 728 (CA).

[16] ibid 731 (Jelf J).

[17] ibid 742 (Sir Gorrel Barnes)

none of the conclusions drawn should be read as a suggestion that opposite notions apply automatically in other contracts for the personal execution of labour. Indeed, several observations apply directly to *all* personal work contracts. As regards the *unitary* perception of the employer, for example, this will be shown to be influenced by a range of factors, most of which are common to the vast majority of personal work relations – any conclusions drawn therefore extending by definition beyond the contract of service. The most prominent example here is the key role played by the contractual nature of the relationship: this framework has had a major influence, in both form and substance, in shaping the concept of the employer as unitary. As nearly all work relationships have become perceived through this prism today, the unitary view of the parties to it is an essential feature of any personal work contract.

The tests at the heart of the subsequent enquiry, on the other hand, have traditionally been used to draw a line between different categories of dependent labour, by determining whether a contract of service exists.[18] Conclusions drawn from their analysis are therefore undoubtedly most relevant to the notion of the work-taking counterparty to a contract of employment. Whether there are differences in notions of the employer in different forms of the wage/work relationship is beyond the immediate scope of this work; there is nothing however that would exclude the possibility of similar conclusions in other contexts. First, the focus on a subset of personal work relations does not suggest that it is in all regards analytically distinct from other arrangements for the personal execution of labour. Second, while the conceptualisation of the contract of employment is built up in the case law through a contradiction between employees and those working under a contract for services or other personal work contracts, instructions on how to divide a category (such as

[18] The case law on the definition of the more recent category of the worker is equally relevant, as the courts have found the distinction between workers and employees to be one of degree rather than kind: *Byrne Bros Ltd v Baird* [2002] ICR 667 (EAT); *Redrow Homes Ltd v Wright* [2004] EWCA Civ 469, [2004] 3 All ER 98.

personal work contracts) into subsets (including contracts of service and contracts for services) nonetheless reveal interesting aspects about the larger pool. It is, finally, not the practical application of the various tests that is of immediate interest but rather the inherent notions underpinning each.

Delineating the Relevant Case Law

Turning to the range of decisions where questions about wage-takers' status are asked, at least three broad categories can be identified: cases concerning employment law *per se*, cases straddling the boundary of employment law and other, related, areas such as social security, taxation or health and safety, and cases in entirely different areas of the law that nonetheless turn to some extent on the existence of an employment relationship. It is suggested, however, that for present analytical purposes these are not three distinct sets. Rather, they are on different points of the same spectrum: the question asked remains the same. What differs is its relative importance, and thus prominence, in the context of the overall decision. This can be illustrated with reference to several cases along the spectrum. At one end, the legal question often extends only marginally further than the applicant's status. A good example is the right of an employee to a written statement outlining the particulars of employment,[19] enforceable, if necessary, through recourse to an Employment Tribunal.[20] On several occasions this appears to have been the basis for test cases concerning groups of workers, such as 'regular casual' tour guides[21] or orchestra musicians.[22] This end of

[19] ERA 1996, s 1.

[20] Ibid, s 11(1).

[21] *Carmichael v National Power Plc* (n 11). The right to particulars of employment at that time was set out in s 1(1) of the Employment Protection (Consolidation) Act 1978, and is in all material aspects identical to the ERA 1996.

[22] *Addison v London Philharmonic Orchestra* [1981] ICR 261 (EAT).

the spectrum can also be seen to include cases on the definition of workers, a regulatory tool which saw rapid growth from 1997 onwards.[23] As has already been suggested, the distinction was soon seen as one of degree rather than kind.[24] Academic commentary has similarly tended to conceptualise the worker as another degree of semi-dependent contractor, rather than an analytically distinct category.[25] While the individual weighing exercise in worker-defining cases might thus be different, the fundamental questions about the *notion* of the dependent labourer (and thus in reflection of the employer) remain the same.

One example of cases in areas adjacent to employment law are occupational health and safety provisions such as construction industry employers' duties to erect and maintain scaffolding and protective rail guards. When this duty is owed only to employees, but not to independent contractors, the question as to the nature of the parties' relationship arises.[26] A similar area is tax law. The amount of cases distinguishing employees and independent subcontractors in this area has however decreased somewhat following changes in taxation practices that mandated PAYE tax deduction at source.[27] Finally, illuminating discussions about the notion of the employer may be found even in areas as seemingly unrelated as Intellectual Property. In *Nora Beloff v Pressdram Ltd*,[28] a journalist sued for copyright infringement following publication of an internal memorandum in *Private Eye*. She could only do so, however, if she was the actual owner of the copyright. This, in turn, was dependent

[23] For example in the National Minimum Wage Act 1998, s 54(3) or the Trade Union and Labour Relations (Consolidation) Act 1992 (TULRCA), ss 145A, 145B and 146 (as amended).

[24] For example in *Byrne Bros Ltd v Baird* (n 18).

[25] Though cf G Davidov, 'Who is a Worker?' (2005) 34 ILJ 57.

[26] *Ferguson v John Dawson Ltd* (n 12).

[27] The first provision of this kind was s 28 of the Finance Act 1972. The facts in *Ferguson* fell on either side of the change: (n 12) 1218B.

[28] *Nora Beloff v Pressdram Ltd* [1973] 1 All ER 241 (HC).

on whether the document had been written whilst she had been an employee of the *Observer* newspaper, in which case statute allocated copyright to the publishing company.[29] On the facts of the case, the High Court found that Ms Beloff's relationship with the Observer Ltd had indeed been a contract of service; her copyright infringement claim failed accordingly. Even though the focal point in the last category may thus not be employment law, the suggestion made above holds true: the question as to the relationship of the parties is essentially the same, even if the cases are found on different points along a spectrum when it comes to the importance of that question in relation to other issues before the court.

SECTION II: A UNITARY NOTION OF THE EMPLOYER

With discipline and hierarchy embodied in the very idea of *the master*, to be found in the common law long before a contract of service evolved,[30] a personified unitary notion of the employer is undoubtedly a historically accurate starting point. The present section proceeds in three parts to show key elements from the range of factors that have shaped a unitary notion. A first sub-section will look at external unifying factors, especially the language and fact patterns of the various decisions. Discussion then turns to the crucial influence of contract law doctrine, before concluding with economic theory as reflected in company law.

SUB-SECTION 1: EXTERNAL FACTORS - LANGUAGE AND FACT PATTERNS

An analysis of the language and fact patterns through which early cases developed quickly shows how a unitary notion of the employer came to be shaped and reinforced

[29] Copyright Act 1956, s 4(4).

[30] A Merritt, 'Control v Economic Reality: Defining the Contract of Employment' (1982) Australian Business Law Review 105.

by the singular and traditionally male language used, even when referring to abstract bodies; how the traditional unitary fact patterns were soon extended to increasingly complex structures; and how this unitary thinking soon framed even multilateral scenarios in singular terms.

The use of terms such as *the* master and *the* employer is a clear expression of the unitary nature of the common law's perception of the employer. This strong attachment to singular language is apparent even in rather curious circumstances: the Conference of the Methodist Church, a body with a variety of structures and committees regulating matters both spiritual and secular, for example, has explicitly been referred to as 'the master'.[31] The context for such analyses was originally created by the fact patterns of early cases, quickly hardening into an established notion, which in turn became self-perpetuating in the way future fact patterns were framed. Many of the early leading cases involved individual employers. *Sadler v Henlock*, where the owner of a ditch was held liable for an accident occurring on an adjacent road following shoddy work by his servant, Pearson, is a clear-cut example.[32] A similar understanding, albeit of distinct doctrinal origins, was soon applied to companies,[33] who were equally seen as a unitary master.[34] In the public sector, statutory interventions paved the way for a unification of the employing entity, yet again on different conceptual and policy grounds: when Mr Cassidy sued the Liverpool Corporation for vicarious liability following negligent medical care, the Ministry of

[31] *President of the Methodist Conference v Parfitt* [1984] QB 368 (CA) 373.

[32] *Sadler v Henlock* 119 ER 209, (1855) 4 El&Bl 570.

[33] For example *Simpson v Ebbw Vale Steel, Iron, and Coal Co* [1905] 1 KB 453 (CA) and *Initial Services v Putterill* [1968] 1 QB 396 (CA). A somewhat curious exception is *Hill v Beckett* [1915] 1 KB 578 (HC) where the Respondent was one of three partners in a firm of coal dealers, rather than the partnership itself.

[34] In fact, even in growingly complex business structure scenarios, groups were seen as a (potential) single employer. See for example *Ready Mixed Concrete Ltd v Minister of Pensions* [1968] 2 QB 497 (HC), where other group companies such as RM Finance Ltd also interacted with the lorry drivers.

Health was substituted as a defendant.[35] Despite these widely different backgrounds, the fact pattern was always seen as a singular one, with the enquiry directed at the relationship with *the* master, or later *the* employer.

In the majority of cases this is not a problem in and of itself: a company or even a government ministry can, after all, still legitimately be conceived of as a single entity, even if not in anthropomorphic terms. There are, however, other fact patterns that could not legitimately be perceived as single-employer scenarios, but on which the unitary paradigm nonetheless began to impose its conceptual straitjacket.

An early illustration of this is *Vamplew v Parkgate*.[36] A worker had been killed in the pits, and his dependants brought an action under the Workmen's Compensation Act of 1897. The Court of Appeal, led by Collins MR, affirmed the County Court's decision that the deceased had been an independent contractor, rather than a servant; giving prominent weight to the fact that he had engaged a group of men and boys to work below him. The unitary conception meant that by acting, in part, as an employer, Mr Vamplew could not at the same time also be an employee. This conceptual influence is evident even more explicitly in *Littlejohn v John Brown & Co Ltd*.[37] There, a rivet heater boy had been severely injured after falling into a vessel, due to the shipbuilders' negligent installation of internal scaffolding. Upon an action for compensation, both at common law and under statute,[38] it was held, however, that the shipbuilding company were not the rivet heater's employers, despite a clear relationship with the boy: whilst usually paid and selected by teams of riveters, a strong residual control, up to and including the power to procure dismissal 'if a lad

35 *Cassidy v Ministry of Health* [1951] 2 KB 343 (CA) 360; National Health Service Act 1946, s 6.

36 *Vamplew v Parkgate Iron & Steel Co Ltd* [1903] 1 KB 851 (CA).

37 *Littlejohn v John Brown & Co Ltd* 1909 SC 169 (CS).

38 Employers Liability Act 1880, s 1.

became obnoxious', rested with the company. There were, therefore, clear multilateral relationships between the claimant, the riveter foremen, and the defendant shipbuilders. The challenging nature of these facts was even acknowledged by the court, with Lord Guthrie noting that '[d]ifficult cases may arise where some of the tests point in one direction and some in another.'[39] Nonetheless his Lordship went on to find that on the day of the accident, the boy had not been in the shipbuilders' employment, and could therefore not recover. The existence of one employer (in the form of riveters Gemmell and Lacy) had automatically negated any potential link with further parties.

The understanding of the employer as a singular and unitary notion thus depicted is by no means a thing of the past. It is just as prevalent in modern situations where reliance on the unitary notion can easily lead to 'morally […] unattractive proposition[s]'[40] being put forward by defendant employers. Even in relatively clear-cut cases, however, the concept is rarely challenged: in *Bolwell v Redcliffe*,[41] the Court of Appeal saw itself bound to choose a relationship of employment with either of two supposedly distinct employers despite their being an economic unit.

SUB-SECTION 2: THE CONTRACTUAL FRAMEWORK

Language and fact patterns are thus the backdrop for the main driver of unitary conceptual channelling today: the contractual framework in terms of which nearly all employment relationships are cast. In 1967, Lord Wedderburn famously referred to

[39] *Littlejohn* (n 37) 174.

[40] *McDermid v Nash Dredging & Reclamation Co Ltd* [1987] AC 906 (HL) 912A (Lord Hailsham).

[41] *Bolwell v Redcliffe Homes Ltd* [1999] IRLR 485 (CA).

contract as the 'fundamental legal institution' of Labour Law.[42] Whilst Simon Deakin has successfully challenged the traditional assumption that a common law system of employment law, based on freedom of contract, predated the welfare state,[43] the institution of the contract and its connected doctrines have nonetheless had a fundamental effect on the perception of the employment relationship in general, and the employer as work-taking counterparty to a contract of service in particular. By looking at the vast majority of personal work relationships through the contractual prism, a unitary view of the employing entity is bound to emerge: if the exchange of wage and work is characterised as a bilateral contractual relationship, emphasis shifts onto a single work-taking counterparty at the non-employee end. When used as the central category of personal work relationships the contract of employment has a strong normative function.

With the exception of very limited categories such as office holding, the paradigm bilateral contract has supplanted all other potential explanations of the employment relationship. It continues to do so in modern contexts, leading to acute problems for employment coverage, most notably in the context of agency workers. There, work is performed in a triangular contractual setup, with workers paid by an agency which in turn provides their labour to its end-user clients. The bilateral contractual model has been the fundamental impediment to the judicial acceptance of a direct relationship between worker and end-user. The existence of a contractual arrangement with the agency crowds out any rival explanations, be it a second bilateral contract or a multilateral agreement between the three parties. In *James*,[44] a housing support worker who had been employed through a series of agencies claimed for unfair

[42] K Wedderburn, *Cases and Materials on Labour Law* (CUP 1967) 1.

[43] Deakin and Wilkinson (n 4).

[44] *James v London Borough of Greenwich* [2008] EWCA Civ 34, [2008] ICR 577.

dismissal. In rejecting her claim for want of a direct relationship with the defendant local authority, the Court of Appeal took up dicta from the earlier decision in *Muscat*.[45] There, the court had explicitly linked the idea that a contract could only be implied where 'necessary'[46] to the business reality test of necessity espoused by Bingham LJ in *The Aramis*,[47] despite the fundamentally different context of that decision.[48] The existence of a contract between agency and worker was therefore enough not only to inhibit the use of implied contracts as a solution to the dilemmas inherent in multilateral employment situations,[49] but also to block the possibility of a second contract between end-user and worker.

In substantive terms, the most significant influence of a contractual analysis in the Employment context is its inherent emphasis on *bilateral* relationships between two individual parties. The nature of the implied contract under consideration in *James* illustrates this fundamental attachment to the notion of unilateral relationships: even clearly multilateral scenarios are tackled through several bilateral contracts.[50]

45 *Cable & Wireless Plc v Muscat* [2006] EWCA Civ 220, [2006] ICR 975.

46 *Dacas v Brook Street Bureau (UK) Ltd* [2004] EWCA Civ 217, [2004] ICR 1437 [16].

47 *Cable & Wireless Plc v Muscat* (n 45) [45]. The idea was also taken up by Elias J in *National Grid Electricity v Wood* [2007] UKEAT/0432/07.

48 *The Aramis* [1989] 1 Lloyd's Rep 213 (CA).

49 See eg E Brown, 'Protecting Agency Workers: Implied Contract or Legislation?' (2008) 37 ILJ 178; M Wynn and P Leighton, 'Agency Workers, Employment Rights and the Ebb and Flow of Freedom of Contract' (2009) 72 MLR 91.

50 *James* (n 44) [5] (Mummery LJ). Despite dicta to the contrary in *Stephenson v Delphi Diesel Systems Ltd* [2003] ICR 471 (EAT) [53], the potential of multiparty contracts is not entirely barred: *Dacas v Brook Street Bureau (UK) Ltd* (n 46) [20], [78]; *Cable & Wireless Plc v Muscat* (n 45) [41].

SUB-SECTION 3: ECONOMIC THEORY AND COMPANY LAW

The factors identified thus far have been of general application to all work-taking counterparties to the contract of employment. Discussion now turns to the single most important form of employing entity in today's labour market: the limited liability company.[51] Despite a multitude of actors, from employees and management to a board of directors and shareholders, it has become a singular focal point for a unitary conception of the corporate entity, with powers and responsibilities perceived in anthropomorphic terms; a notion to which employment relationships then fasten.

In economic theory, the conception of the firm as a singular unit is built on two factors: the firm as internalising what would otherwise be cost-inefficient market transactions between factors of production, and the firm as concentrating management powers in the hands of a small group, thus taking them away from the shareholders of the company. Two different relationships are at stake here – that between employees and the company; and that between owners and the company. Whilst the precise approaches to these groups differ, the outcome is the same: the conceptualisation of a company as a unitary entity.

The former aspect is discussed in Ronald Coase's economic analysis of the corporate firm as a central market actor. There, the rationale behind the existence of a firm is said to be the increase in economic efficiency that results from subsuming one set of actors (those dealing in factors of production) under the centralised control of a single 'entrepreneur co-ordinator'.[52] In particular, Coase looks to the contract of employment as evidence for the importance of directional powers, suggesting that 'it

[51] References to Company or Corporation should be taken as synonyms for this.

[52] Coase (n 6) 388. Today, centralised management exercises the entrepreneur's role.

is the fact of direction which is the essence of the legal concept of employer and employee.'[53]

Turning next to financial structures and corporate governance,[54] ie the relationship between the company (as represented by the management of the firm) and its shareholders (the owners of the equity in the firm), multiple actors within the realm of the company again do not stand in the way of a perception of the enterprise as a single unit. The economic explanation of governance structures sees them as transaction cost-reducing relationships, [55] 'where owners of various resources are seen as committing to some "contractual governance arrangement"'. [56] In Anglo-American corporate structures, this arrangement has traditionally been described as one of diffuse shareholdings, in contrast to the blockholder model frequently encountered in jurisdictions inspired by continental European systems.[57]

Berle and Means identify three functions of enterprise:[58] 'having interests in an enterprise, […] having power over it, and […] acting with respect to it.' Through the corporate form these functions have become separated – especially the traditional bond between the first pair. This is the second facet of the economically unitary view of the corporation, where all actors are kept separate from the commercial entity, either by disappearing within it or being separated from it. Company law developed

53 ibid 404.

54 H Gospel and A Pendleton, 'Corporate Governance and Labour Management: An International Comparison' in H Gospel and A Pendleton (eds), *Corporate Governance and Labour Management: An International Comparison* (OUP 2005).

55 O Williamson, *The Economic Institutions of Capitalism* (The Free Press 1985).

56 W Allen, R Kraakman and G Subramanian, *Commentaries and Cases on the Law of Business Organization* (2nd edn Wolters Kluwer 2007) 10.

57 P Gourevitch and J Shinn, *Political Power and Corporate Control: The New Global Politics of Corporate Governance* (Princeton University Press 2005) 4-5.

58 A Berle and G Means, *The Modern Corporation and Private Property* (The Macmillan Company 1939) 119.

against this background, setting the legal boundaries of the company not at the economic remit of all those involved, but on a far narrower basis, shaped by two closely related doctrines: separate legal personality, and limited liability.

The attribution of separate legal personality to a validly incorporated limited liability company is of common law origins.[59] In *Salomon v Salomon*,[60] a sole trader had turned his enterprise into a limited liability company, becoming in effect its only director and principal shareholder. The House of Lords held that shareholders' liability could extend no further than their initial contributions, and that the company was 'a distinct legal persona'.[61] *Lee v Lee's Air Farming*[62] confirmed this when finding that Mr Lee had been an employee of a company which he himself had incorporated and solely managed as both director and controlling shareholder. Lord Morris, giving the speech for the Privy Council, held that 'an application of the principles of Salomon's case demonstrates that the company was distinct from the deceased'.[63]

Today, one further consequence flowing from valid incorporation is limited liability. Through incorporation, shareholders can limit their economic and legal risk exposure to the value of their shares,[64] which is either the amount of money initially paid to the company for an equity subscription, or the market value of the shares if purchased subsequently. This protection of shareholders from claims against their

[59] Though the rules for incorporation are found in statute. The Companies Act 2006, s 3(1)-(3) defines limited liability companies, and Part II of the Act sets out the incorporation process.

[60] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

[61] ibid 42 (Lord Herschell).

[62] *Lee v Lee's Air Farming Ltd* [1961] AC 12 (PC).

[63] ibid 30.

[64] P Davies and S Worthington, *Gower and Davies' Principles of Modern Company Law* (9th edn Sweet & Maxwell 2012) 8-1. The following paragraphs build on the discussion there.

individual assets is often referred to as the corporate veil – hiding the company's members behind it in a manner reminiscent of the earlier economic analysis.

The corporate veil may on occasion be pierced or lifted by the courts,[65] for example in order to impose liability for the company's acts on the shareholders behind it – a process to which the common law has traditionally been very hostile. The orthodox position asserts that the veil may only be lifted (in the sense just outlined) in case of fraud[66] or certain statutory provisions.[67] A range of potential policy explanations support this strict line – most notably the idea that limited liability is necessary for the efficient functioning of public securities markets,[68] and the assignment of creditors to relevant economic units.[69] On the other hand, it has been suggested that the 'tyrannical sway' of the 'calamitous decision' in *Salomon* fosters unnecessary artificiality, leading to a capricious lack of clarity and predictability and the potential for fraudulent abuse.[70]

Not all shareholders are individuals, however: businesses are often structured as a group of companies, holding the entirety of shares in each subsidiary. In these situations, it is difficult to see how above-discussed rationales for limited liability can justify the law's equal application of the doctrine, given its potentially negative impact

65 S Ottolenghi, 'From Peeping Behind the Corporate Veil, to Ignoring It Completely' (1990) 53 MLR 338, 340.

66 The bar for which is set high: *Adams v Cape Industries Plc* [1990] Ch 433 (CA).

67 For example in the Insolvency Act 1986, ss 213 and 214 (fraudulent and wrongful trading).

68 P Halpern, M Trebilcock and S Turnbull, 'An Economic Analysis of Limited Liability' (1980) 30 University of Toronto Law Journal 117 (as cited in Davies and Worthington (n 64)).

69 The 'asset partitioning rationale' set out in H Hansmann and R Kraakman, 'The Essential Role of Organizational Law' (2000) 110 Yale Law Journal 387 (as cited ibid).

70 O Kahn-Freund, 'Some Reflections on Company Law Reform' (1944) 7 MLR 54, 56; K Wedderburn, 'Multinationals and the Antiquities of Company Law' (1984) 47 MLR 87, 90.

on creditors, including wage creditors, of individual subsidiaries[71] – or even on the company itself.[72] For a brief period following the decision in *DHN*,[73] where Lord Denning had led a Court of Appeal in holding that three separate companies 'should not be treated separately so as to be defeated on a technical point',[74] it appeared as if a group enterprise or single economic unit exception to the limited liability of each individual group company could develop.[75] Orthodoxy was however quickly reasserted,[76] ignoring management reality in corporate groups. As Goff LJ put it, the concern of the courts was to be 'not with economics but with law. The distinction [between two group companies] is, in law, fundamental and cannot here be bridged.'[77] Each company, once properly incorporated, is therefore free of the debts and other liabilities of any other company in a group structure.[78]

Hansmann and Kraakman suggest that the independent position of each company allows each creditor to be assigned to the relevant economic unit.[79] This approach may be appropriate in the case of voluntary creditors, despite academic commentary to the contrary.[80] In commercial negotiations with a company, they will be able to

71 Davies and Worthington (n 64) 8-2.

72 The 'boomerang' hitting 'the man who was trying to use it', as envisaged by Kahn-Freund (n 70) 56.

73 *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852 (CA).

74 ibid 860.

75 A development criticised in F Rixon, 'Lifting the Veil Between Holding and Subsidiary Companies' (1986) 102 LQR 415.

76 *Woolfson v Strathclyde RC* 1978 SC (HL) 90.

77 *Bank of Tokyo Ltd v Karoon* [1987] AC 41 (CA) 64.

78 *Re Southard & Co Ltd* [1979] 1 WLR 1198 (CA).

79 Hansmann and Kraakman (n 69).

80 K Wedderburn (n 70) 90.

bargain for appropriate protection through risk pricing mechanisms that account for the legal structure of individual units.

The problem is a different one in the context of involuntary creditors who have no such opportunity to ensure ex-ante protection,[81] as is the case most notably with Tort victims.[82] In the employment context, Davies and Freedland suggest that limited liability applies within group structures

> even though the managerial structure of the group (or part of it) itself ignores the division of the group into separate legal entities. […] The fact that the business organisation of the group ignores the separate legal entities of the group companies will not enable the employee to go behind or beyond his or her employing company.[83]

The potential for abuse of the limited liability form is rarely doubted; the courts have nonetheless shown themselves highly unwilling to lift the corporate veil. *Adams v Cape Industries*[84] provides clear affirmation of the 'right […] inherent in our corporate law'[85] to rely on the principles expounded in *Salomon* in deliberately structuring corporate groups to parcel out liability. Here, two of the leading policy arguments against the corporate veil coincided on the facts: the claimants were involuntary creditors (asbestosis victims), and the defendant one of a large international group of companies forming a single economic unit.[86] Nonetheless, the veil was upheld, subject only to a narrow fraud exception. As Davies and Freedland

81 Most trade creditors, while technically voluntary, are in a similar position.

82 H Hansmann and R Kraakman, 'Towards Unlimited Shareholder Liability for Corporate Torts' (1991) 100 Yale Law Journal 1879 (as cited in Davies and Worthington (n 64)).

83 P Davies and M Freedland, 'The Employment Relationship in British Labour Law' in C Barnard, S Deakin and G Morris (eds), *The Future of Labour Law: Liber Amicorum for Sir Bob Hepple QC* (Hart 2004) 137.

84 *Adams v Cape Industries Plc* (n 66).

85 ibid 544 D-E.

86 Davies and Worthington (n 64) 8-7.

put it, this confirms that 'ignoring the group structure will rarely be a policy available to the courts'.[87]

The perception of companies as anthropomorphic individual units as a result of separate legal personality is thus a further factor contributing to the historical assumption that the employer must be a singular entity, substantively identical across all different domains of employment law. As the following section will show, however, this is rather different from the conception of the employer borne out in another context: the common law tests through which the notion of the employee as party to the contract of employment has evolved.

SECTION III: A MULTI-FUNCTIONAL NOTION OF THE EMPLOYER

In order to explore the factors which shaped the second, multi-functional strand of the received notion of the employer, this section turns to the well-rehearsed common law tests through which employment status is determined. It will be suggested that there is nothing inherently unitary in the traditional notion of the employer. Indeed, the opposite case can be made out: what emerges from the decisions is a deeply multi-functional conceptualisation.

SUB-SECTION 1: REVISITING THE UNITARY CONCEPTION

Most of the relevant case law in this context is directed at classifying the status of individual workers, with the result that any pronouncements on the notion of the employer are *obiter* assumptions. On the basis of the close contractual link identified in the first section, the decisions can nonetheless be used in a conceptual enquiry focussed on the nature of the employer. The specific question to be asked for each of

[87] Davies and Freedland (n 83) 137.

the major tests is whether its requirements are *inherently* unitary: is it logically workable only if a single counterparty exercises the function under scrutiny; with the test thus necessarily tied to a unitary notion of the employer? To illustrate in practical terms, if the regular inspection of worker schedules is a criterion for employee status, this would not point to an inherently unitary notion of the employer: the exercise of such control is not necessarily confined to a single party. It could of course be so limited in practice, for example under a contractual arrangement, but that is not *inherent* in the correlated rights and duties. The enquiry as to whether an individual is part and parcel of an organisation is an example in the opposite direction: even when considered in the abstract, it does not allow for anything other than a single entity conceptualisation.

Control

Control was historically conceived of as a unitary test, in line with the factual contexts set out earlier. The initial assumption was one of a single party, the master, in exclusive exercise of the control right over the servant.[88] That this was not a logical necessity, however, quickly becomes evident when looking at the different functions cited as evidence of control. Even from a very small cross-section, such as the process of engaging or dismissing workers, their supervision and instructions as to the performance of daily duties and their location, it is clear that the functions could be, and in reality often are, split or shared in their exercise between different parties.

With the emergence and inclusion in protective statutory regimes of professional jobs, the courts began to come across more and more situations where control was exercised by several parties. At first, the law's reaction to the ascent of such

[88] *Yewens v Noakes* (1880-81) LR 6 QBD 530 (CA); *Sadler v Henlock* (n 32). The idea that 'No man can serve two masters' can be traced back to the New Testament, Matthew 6:24: '… for either he will hate the one, and love the other; or else he will hold to the one, and despise the other.'

multilateral scenarios was a somewhat awkward search for the party exercising the highest level, or 'most control' over the individual. This approach is evident in the foreman cases discussed earlier: in *Littlejohn*, Lord Guthrie's enquiry focussed on the fact that the shipbuilder's control over the boy was more indirect and remote than that exercised by the riveters.[89] Similarly, in *Ready Mixed Concrete* MacKenna J suggested that 'all […] aspects of control must be considered in deciding whether the right exists in a sufficient degree to make one party the master and the other his servant.'[90] The latter case, incidentally, was one of several turning points away from the control test, for the very reason that it threw into sharp relief the incongruence between the unitary notion and the multilateral results that a strict application of the test would have demanded.

Instead, the courts started to substitute other tests, particularly in cases where control was exercised by a range of different parties. In *Morren v Swinton Borough Council,*[91] for example, this shift to an integration test as a move beyond control is clearly visible. The local authority and its consulting engineers had agreed to engage a resident engineer who, in practical terms, was controlled by both parties. Despite earlier explicit statements from the Council to the contrary, Morren attempted to join its superannuation scheme, arguing that he was in fact a local authority employee. In upholding his claim, the court found that control could not be the decisive test when dealing with a professional man.[92]

There is nothing in the nature of the control test that demands a unitary notion of the employer. If anything, it often instinctively leads to a multilateral analysis. The

89 *Littlejohn v John Brown & Co Ltd* (n 37) 147.

90 *Ready Mixed Concrete Ltd v Minister of Pensions* (n 34) 515F–G.

91 *Morren v Swinton and Pendlebury BC* [1965] 1 WLR 576 (DC).

92 ibid 582B.

emphasis throughout the judgments is on the employee as the controlled. Notwithstanding a unitary paradigm approach, control exercised by a range of different parties is a realistic option on both a practical and theoretical level without necessarily being lethal to the existence of an employment relationship. Despite, or perhaps because of this, the control test came to be supplanted by other criteria, rather than challenging the unilateral notion.

Integration

Amongst the four tests under analysis, the integration test is closest to the unitary end of the spectrum. Both in terms of the language and concepts deployed, it points to an underlying conception of the employer as a single entity. As Denning LJ put it, 'the test of being a servant does not rest nowadays on submission to orders. It depends on whether the person is part and parcel of the organization.'[93]

It is not just the language of this approach that is unitary – on a conceptual level, being part of *the*, or even *an*, organisation can also be seen as supporting a unitary notion: the individual is only an employee if he or she is integrated into one organisation.

This can be illustrated on the facts of *Stevenson Jordan v MacDonald*. MacDonald claimed the copyright to a book published by a former employee. The first of its five parts consisted of a series of lectures given to the public during the author's employment with the claimants. The Court of Appeal, applying a business integration test, found that the lectures had not been given under a contract of service, drawing a stark contrast between 'a man […] employed as part of the business, and his work […] done as an integral part of the business'; and one working 'under a contract for

[93] *Bank voor Handel en Scheepvaart NV v Slatford (No 2)* [1953] 1 QB 248 (CA) 290.

services where his work, although done for the business, is not integrated into it but is only accessory to it.'[94] This demonstrates that, under the integration test, the conception of the employer is so unitary that it excludes from the sphere of the company related, even if somewhat extraneous, functions.

The integration test could therefore, to some extent, be characterized as an opposite conception to that inherently underlying control. In contrast to the latter, however, it never saw a second lease of life, and remains of comparably little significance – possibly because its inherently strong unitary approach sat uneasily with many factual situations.

Economic or Business Reality

In the United States, an enquiry into the economic reality of the relationship between the parties overtook the control test early on. In *US v Silk*,[95] the Supreme Court emphatically rejected a reliance on 'technical concepts', holding instead that the category of '"employees" included workers who were such as a matter of economic reality'.[96] The courts' focus on economic factors in this test is construed very widely, from the provision of tools, other working materials and general investment in a project to the bearing of overall market risk. If none, or few, of these factors fall upon the individual whose status is to be determined, he or she will in all likelihood be considered an employee. There is nothing in the tests, however, that suggests that the various aspects, from micro- to macro-economic factors, need to be concentrated in a single party. The conclusion demonstrated in the discussion of the control test rings equally true here: there is nothing in the reference to a party *other than* the worker to

94 *Stevenson Jordan & Harrison v McDonnell & Evans* [1952] 1 TLR 101 (CA) 111.

95 *United States v Silk* [1947] 331 US 704.

96 ibid 713.

say that it could only be *one* other party. The test is workable with single or multiple employing entities.

The first case directly to import the US Supreme Court's language into English law was *Market Investigations Ltd v Minister of Social Security*, affirming the Secretary of State's finding that a part-time interviewer had been employed under a contract of service. Having discussed *Silk* and other authorities, Cooke J formulated the test as follows: 'Is the person who has engaged himself to perform these services performing them as a person in business on his own account?'[97] Through a focus on the employee, this formulation leaves open a variety of potential accounts of the employer, without at any point hinting at a unitary notion as a logical necessity. In fact, a later paragraph explicitly considers, and approves of, the potential plurality of employers, suggesting that there is nothing

> inconsistent with the existence of a contract of service in the fact that [the interviewer] was free to work for others during the relevant period. It is by no means a necessary incident of a contract of service that the servant is prohibited from serving any other employer.[98]

On a narrow interpretation, this only covers an individual's independent service for two distinct employers.[99] Upon further consideration, however, there is little in the present context to distinguish this from other multilateral scenarios: they are all different variations of not being in business on one's own account.[100] While the paradigm underpinning Cooke J's judgment is clearly one of a unitary relationship

[97] *Market Investigations Ltd v Minister of Social Security* [1969] 2 QB 173 (HC) 184G–H.

[98] ibid 186F.

[99] On the basis of which submissions seem to have been made before Cooke J.

[100] Though, of course, if this number becomes very large, with resulting short service periods, the contracts will be for services: *Hall (Inspector of Taxes) v Lorimer* [1994] 1 WLR 209 (CA).

between a worker and a single employer, this is so as a matter of fact, rather than due to anything inherent in the test.

Examples from case law on the provision of tools and project investment illustrate the same point from a slightly different angle: the focus here is again on the idea that it is not the worker from whom capital inputs stem. Judicial pronouncements to this effect can be found in cases ranging from major capital investment in a large construction project,[101] to those of much less capital-intensive items, for example the provision of necessary tools on-site.[102] As in all variations of the economic reality test, the focus on the employee here means that any other party, or combination of parties, might provide the capital input.

Mutuality of Obligation

The final test to be examined is by far the most prominent in practice today: mutuality of obligation. At first glance, it appears to build on a unitary notion of the employing entity. Both the exchange of work and remuneration and the obligation to offer work and to accept such offers on a long-term basis can be characterised as promises between worker and employer: a bilateral contract, with one party on each side. In *Nethermere v Gardiner*, Dillon LJ summarised earlier case law and held

> that there is one *sine qua non* which can firmly be identified as an essential of the existence of a contract of service and that is that there must be mutual obligations on the employer to provide work for the employee and on the employee to perform work for the employer. If such mutuality is not present, then either there is no contract at all or

[101] *Lee Ting Sang v Chung Chi-Keung* [1990] 2 AC 374 (PC HK).

[102] *Ferguson v John Dawson Ltd* (n 12).

> whatever contract there is must be a contract for services or something else, but not a contract of service.[103]

On the facts of that case, a group of home workers was held to have been employed under contracts of service. More generally, however, the requirement of mutuality of obligation has become a significant hurdle in establishing such a relationship.[104] Regardless of outcome, on the facts of all these cases there was only a single employer under discussion; indeed it would appear that the language of the test makes it clear that it is *the* employer who undertakes to provide future work, and to whom the employee's duties point.

As has already been noted, however, the question here is not how the criterion has been used in practice, but rather what notion of the employer can be seen from the test in the abstract. Considered at this level, there is ample evidence that the notion of the employer underpinning the mutuality of obligation test is not as inherently unitary as it initially appeared: it could be readily applied to multilateral situations. This is, first, evident in the very meaning of the word mutual. On a historical understanding, there may be a bilateral connotation to it; modern definitions however make it clear that mutuality can always refer to 'two or more parties'.[105] Upon reflection, this is already manifested in the case law: any employer with more than one employee enters into mutuality of obligation with several counterparties, promising each of them to provide, and pay for the execution of, work on a regular basis. As a matter of logic,

[103] *Nethermere (St Neots) Ltd v Gardiner* [1984] ICR 612 (CA) 632F–G.

[104] See, for example, the leading cases of *O'Kelly v Trusthouse Forte Plc* (n 13) and *Carmichael v National Power Plc* (n 11). The test itself receives surprisingly little judicial attention in these judgments.

[105] The Oxford English Dictionary defines *mutual* as '1 experienced or done by each of *two or more* parties towards *the other or others*, 2 (of *two or more* parties) having the same specified relationship to each other and 3 held in common by *two or more* parties, before also noting the historically bilateral point made in the text' (emphasis supplied).

there is therefore nothing that would prevent an employee from similarly undertaking to provide his labour to several parties.

A second point arises out of Deakin and Morris' characterisation of mutuality of obligation as a 'fresh emphasis on a form of personal control.'[106] In discussing the latter, the conclusion reached was that the control test could often instinctively point to a multilateral understanding of the employing entity in a wide range of situations. If the mutuality of obligation test can thus be seen as a reworking of a form of the personal control test, what has been said above may be imported *mutatis mutandis* into the present discussion, thus further corroborating the idea that, in the abstract, there is nothing inherently unitary about the mutuality of obligation requirement.

A complete characterisation of mutuality of obligation, and indeed all tests discussed thus far, should not be blind to the reality of most decided cases, where the conception underlying its obligation will frequently be unitary, with single employers undertaking the obligation to provide work. This position, however, is *not* due to anything inherent in the tests: the meaning of the word *mutual* itself is broad enough comfortably to include multilateral scenarios, and as a modern-day version of the control test the criterion should be equally susceptible to being shared amongst multiple parties.

Apart from the short-lived development of an enterprise integration doctrine,[107] none of the traditional tests could thus be said to necessitate an inherently unitary conception of the employer. Indeed, they pose a potentially significant challenge to the unitary strand developed in part two, by painting a highly multi-functional notion.

[106] S Deakin and G Morris, *Labour Law* (6th edn Hart 2012) 164.

[107] *Stevenson Jordan & Harrison v McDonnell & Evans* (n 94) 111; *Bank voor Handel en Scheepvaart NV v Slatford (No 2)* (n 93) 290.

SUB-SECTION 2: A MULTI-FUNCTIONAL NOTION

A 'function' of being an employer is one of the various actions employers are entitled or obliged to take as part of the bundle of rights and duties falling within the scope of the open-ended contract of service. In trawling the established tests for such employer functions, there are endless possible mutations of different fact scenarios, rendering categorisation purely on the basis of past decisions of limited assistance. As with previous sections, therefore, subsequent paragraphs look at the notions underlying different fact patterns, rather than the actual results on a case-by-case basis, in order to classify them into functional groups.[108] The result is the following set of functions, with the presence or absence of individual factors becoming less relevant than the specific role they play in any given context. Individual elements can vary from situation to situation, as long as they fulfil the same function when looked at as a whole.[109] Key to this notion of the employer being a *multi-functional* one is the fact that no one function mentioned above is relevant in and of itself. Rather, it is the *ensemble* of the five functions that matters: each of them covers one of the facets necessary to create, maintain and commercially exploit employment relationships, thus coming together to make up the legal notion of employing workers or acting as an employer.

The *five main functions* (and their functional underpinning) of the employer are:

[1] Inception and Termination of the Contract of Employment

This category includes all powers of the employer over the very existence of its relationship with the employee.

[108] In line with established methodology: Deakin (n 3) 83; Freedland (n 5) 40.

[109] The 'equipollency principle' (Äquivalenzprinzip): L Nogler, 'Die Typologisch-Funktionale Methode am Beispiel des Arbeitnehmerbegriffs' (2009) 10 ZESAR 459, 463.

[2] Receiving Labour and its Fruits

Duties owed by the employee to the employer, specifically to provide his or her labour and the results thereof, as well as rights incidental to it.

[3] Providing Work and Pay

The employer's obligations towards its employees.

[4] Managing the Enterprise-Internal Market

Coordination through control over all factors of production.

[5] Managing the Enterprise-External Market

Undertaking economic activity in return for potential profit, whilst also being exposed to any losses that may result from the enterprise.

The division of employer functions into discreet categories is not a novel idea. Deakin, for example, has suggested three 'overlapping and complementary' functional criteria in the context of developing a potential definition of employing entities, namely:

> coordination, which associates the employment unit (or parts of it) with the presence of centralised managerial control; risk, which treats the employer as a juridical form of absorbing, processing and spreading social and economic risks which are associated with the enterprise; and equity, which sees the employment unit as a space within which the equal treatment principle, in its various forms, should be observed.[110]

[110] Deakin (n 3) 83.

More recently, Mark Freedland has identified four main categories comprised in the notion of employing workers, or acting as an employer:

> (1) engaging workers for employment and terminating their employment; (2) remunerating workers and providing them with other benefits of employment; (3) managing the employment relation and the process of work; and (4) using the worker's services in a process of production or service provision.[111]

Why, then, are employer functions divided into five categories for present purposes? At first glance, the five categories are reasonably similar to the list just set out, subject only to a subdivision of category (4) into aspects concerning the specific *enterprise-internal market* of each organisation [4], and those relevant to *external markets* more generally [5]. This reflects analytical distinctions present in both economic theory and law – for example different sets of legal rules regulating the two spheres. Furthermore, as the overall purpose of the present work is to look at challenges arising from a split of employer functions between different entities, the additional subdivision will allow for a clearer analysis of the resulting challenges.

Before turning to the categories themselves, finally, it is important to focus for a moment on two aspects of the notion of a *multi-functional* concept. The first is its relationship with the main common law tests: while the material in the five categories draws extensively on the same case law, there is no direct overlap with the traditional tests for the classification of an employment relationship. This is primarily due to the fact that any one test can comprise different functional notions, just as all functional notions can be relevant to different tests. The control test provides a straightforward illustration of this, as the functions expressed through it can include control over the inception of a contractual relationship, management in the course of the employment, and duties owed by the employer to its employees.

[111] Freedland (n 5) 40.

A related problem might arise from the fact that some functions appear to fit into multiple categories: the duty to pay employees and provide work for them,[112] for example, could be relevant both to [3] *Providing Work and Pay* and [5] *Managing the Enterprise-External Market*. Upon closer inspection, however, this problem is solved through the use of a typological-functional method, where individual facts matter less than the functions of which they are examples, and according to which they have been characterised. Returning to the payment of wages example, the duty to provide work and pay on an individual transaction basis, will form part of category [3], whereas the 'continuing obligation'[113] to provide work (and thus pay) even if there is no immediate demand for the production output falls within economic risk allocation in [5].

Discussion thus turns to the five functions. In the order set out above, the rationale underpinning each category will be explained, before moving on to illustrative case law examples of the various functions subsumed under it.

1) Inception and Termination of the Contract of Employment

This category includes the power to hire and fire employees, and accessory processes. In functional terms, the emphasis here is on power over the very existence of the contract. The employer has the power to bring about a personal work relationship with the employee, but also the right to terminate it subject to statutory and common law rules on unfair and wrongful dismissal.[114] The 'power of selection',[115] first, covers a range of actions even before an actual contract is concluded, from advertising a

[112] eg *Short v J&W Henderson Ltd* 1945 SC 155 (CS).

[113] *Hellyer Brothers Ltd v McLeod* [1987] 1 WLR 728 (CA) 750E.

[114] The statutory regime is found in the ERA 1996, as amended (Employment Acts 2002 and 2008).

[115] *Short v J&W Henderson Ltd* (n 112).

position, interviewing and selecting applicants, and making a formal offer of employment, to appointing the desired candidate.[116] The right to dismiss[117] as an 'ultimate conduct sanction',[118] is the logic counterpart to this, as are powers of suspension and related disciplinary procedures that could lead up to the termination of the contract.[119]

2) Receiving Labour and its Fruits

This category explains why employers are sometimes referred to as work-takers: the central purpose of being an employer is arguably the power over employees' labour and the resulting products. In cases focussed on the employee's position, this is often framed in terms of 'the principal obligation of an employee: to provide himself to serve.'[120] The duty must be a legal one, as well as exclusive to a reasonable degree.[121] As regards exclusivity, suggestions vary from men not being allowed to sign elsewhere,[122] a rather high threshold, to the case of a skilled artisan working for more than one company, yet always giving priority to his employer.[123] The essence in both cases is the employer's right to demand, and if so to receive, the worker's labour.

[116] *Morren v Swinton and Pendlebury BC* (n 91).

[117] *Narich Pty v Commissioner of Payroll Tax* [1984] ICR 286 (EAT) 295E.

[118] *Cassidy v Ministry of Health* (n 35) 360 (Denning LJ).

[119] *Collins v Hertfordshire CC* [1947] KB 598 (HC).

[120] *WHPT Housing Association v Secretary of State for Social Services* [1981] ICR 737 (HC).

[121] *United States v Silk* (n 95).

[122] *Hellyer Bros Ltd v McLeod* (n 113) 749.

[123] *Lee Ting Sang v Chung Chi-Keung* (n 101).

The employer not only has a right to receive an employee's own work,[124] but also any goods and materials – including intellectual property – produced as a result of this work.[125] Incidental duties, such as confidentiality, owed by employees to their employers, support this.[126] The main function of these duties is to protect the employer's wider economic interests. Finally, there are a range of further common law duties, such as fidelity and obedience, owed to the employer in order to ensure that the overall function can be exercised.[127]

3) Providing Work and Pay

In return for these obligations the employer owes its employees a range of duties, most notably to provide regular work and pay as contractually agreed. In functional terms, this is the reciprocal element to receiving labour and its fruits, placing employees at the wage-taking end of the relationship. Payment of wages is the most frequently referenced aspect,[128] even if there is a relationship of employment only on an hourly basis.[129] The payment of expenses and other allowances can also be a relevant factor.[130] The functional category is considerably wider than this, however. Intimately related to the remunerative obligation is the duty to provide work to the employee – the '*sine qua non*'[131] of the relationship.[132] The obligation to pay an

[124] *Nethermere (St Neots) Ltd v Gardiner* (n 103).

[125] *Stevenson Jordan & Harrison v McDonnell & Evans* (n 94).

[126] *Initial Services v Putterill* (n 33).

[127] *McMeechan v Secretary of State for Employment* [1997] ICR 549 (CA) 565.

[128] *Cassidy v Ministry of Health* (n 35) 360.

[129] *Ferguson v John Dawson Ltd* (n 12).

[130] *Morren v Swinton and Pendlebury BC* (n 91).

[131] *Nethermere (St Neots) Ltd v Gardiner* (n 103) 632F (Dillon LJ).

employee can continue to exist under certain circumstances even if no work is actually being done.[133]

4) Managing the Enterprise-Internal Market

This function is central to the role of the entrepreneur-coordinator: only through the use of directional powers stemming from the contract of employment can management achieve the necessary control over all factors of production. Initial formulations of this built on the power to require both how and what was to be done,[134] even if the right needed not be unrestricted.[135] More recent examples include moving workers from site to site,[136] requiring their presence during certain hours,[137] choosing employees for specific tasks,[138] or even varying the terms of individual engagements.[139] The functional notion underpinning this category is an open-ended right to direct employees, regardless of the actual level of detail of that instruction.

5) Managing the Enterprise-External Market

The final function of the employer is to engage with the market at large. This comprises a number of different aspects, all of which centre on the chance of financial

[132] Although it has also been suggested (Kerr LJ in dissent) that it might not be necessary for the courts to decide if an employer's duty is to provide a reasonable amount of work, or merely to pay an agreed and reasonable sum.

[133] *Clark v Oxfordshire HA* [1998] IRLR 125 (CA).

[134] *Simmons v Heath Laundry Co* [1910] 1 KB 543 (CA) (Hilbery J).

[135] *Ready Mixed Concrete Ltd v Minister of Pensions* (n 34).

[136] *Ferguson v John Dawson Ltd* (n 12).

[137] *WHPT Housing Association v Secretary of State for Social Services* (n 120).

[138] *Cassidy v Ministry of Health* (n 35) 360.

[139] *Calder v H K Vickers* [1988] ICR 232 (CA) 252.

profit and the risk of loss.[140] It is on the employer's account that all business activities take place.[141] The frequently cited ownership of tools[142] stands for all investment in projects and facilities.[143] The obligation to keep paying employees even when the enterprise is not profitable has already been discussed,[144] and stands alongside the risk of bad debt and outstanding invoices[145] for employers' financial buffer function.

The observation that there is nothing in the control, economic risk, and mutuality of obligation tests that demands an inherently singular work-taking counterparty to the contract of employment is thus corroborated by the fact that the notion of the employer is a highly functional one, made up of five overlapping categories of employer functions. At the same time, it stands in potential conflict with the earlier conclusion that the notion is a unitary one.

SECTION IV: AN INHERENT TENSION

Combining the two conceptions of the employer which have emerged is not necessarily an analytical problem: a single entity could after all exercise all employer functions. There are, however, several different modes of exercising the functions of employing individuals under a contract of service. At least three scenarios are possible: functions might be bundled into one entity, shared between two or more entities, or parcelled out between different entities. The first of these modes is the

[140] *Ready Mixed Concrete Ltd v Minister of Pensions* (n 34) 522.

[141] *Market Investigations Ltd v Minister of Social Security* (n 97).

[142] *Montreal v Montreal Locomotive Works* [1947] 1 DLR 161 (PC).

[143] *United States v Silk* (n 95).

[144] *Clark v Oxfordshire HA* (n 133).

[145] *Hall (Inspector of Taxes) v Lorimer* (n 100) 217.

paradigm situation: a single individual or entity exercises all employer functions.[146] There is thus no automatic incompatibility between a *unitary* notion of the employer and a *functional* one.

The same cannot be said of the other two modes. In *shared exercise*, some functions of the employer are simultaneously vested in more than one party. A classic example of this is the case of *Hill v Becket*,[147] where a coal yard employed a foreman to be in charge of a gang of workers. In practice, the foreman was tasked with engaging and dismissing workers under him and the direction of their day-to-day work. The coal yard, however, also reserved a right of general control, as well as the power to procure the dismissal of individual workers. When functions are *parcelled out*, on the other hand, distinct entities fulfil mutually exclusive roles. The best illustrations for this arise in the context of triangular work relationships. In *Dacas*,[148] an agency worker cleaned hostels for a local authority, the end-user. Under the arrangement the agency paid the worker, while day-to-day control over her work was exercised by the authority. Finally, there is the possibility that in the context of a single worker some functions are exercised jointly whilst others are parcelled out – such as in triangular situations where both agency and end-user have the right to procure dismissal.[149] These different distributional models do not sit easily with the paradigm unitary model of the employer.[150]

The problem is further exacerbated by the fact that there is no legal distinction between the potential to fulfil an employer function, and its actual exercise. In *Ready*

[146] Such as the franchisee in *Narich Pty v Commissioner of Payroll Tax* (n 117).

[147] *Hill v Beckett* (n 33).

[148] *Dacas v Brook Street Bureau (UK) Ltd* (n 46).

[149] *Construction Industry Training Board v Labour Force Ltd* [1970] 3 All ER 220 (HC).

[150] M Wynn and P Leighton, 'Will the Real Employer Please Stand Up? Agencies, Client Companies and the Employment Status of the Temporary Agency Worker' (2006) 35 ILJ 301, 303.

Mixed Concrete, MacKenna J held that whether or not anyone had ever attempted to instruct the concrete lorry driver was 'irrelevant: it is the right of control that matters, not its exercise.'[151] Put differently, it is of little relevance whether a party had in fact control over the worker. What matters is 'ultimate authority over [a] man'.[152] That said, there is a clear limit to this fairly extensive approach to the exercise of employer functions: the power or authority must be a legal one (albeit not necessarily stemming from a contract of employment), rather than being social or commercial.[153]

Viewed thus, the multi-functional conceptualisation of the employer poses a direct challenge to the unitary notion, reconcilable only in a small set of paradigm cases. On the other hand, in situations where different functions may be exercised from more than one *locus* of control,[154] the tension quickly comes to the fore. As subsequent chapters hope to demonstrate, the practical implications of this conflict are considerable, from regulatory obligations placed on unsuitable entities to a complete breakdown of employment law coverage.

CONCLUSION

The first chapter of this thesis set out to identify and challenge the unspoken assumptions surrounding the legal notion of the employer in English law. Historically, the language and fact patterns of early cases quickly became a fixed perspective from which future scenarios were analysed, enforcing a unitary view of the employer even

[151] *Ready Mixed Concrete Ltd v Minister of Pensions* (n 34) 515A.

[152] *Humberstone v Northern Timber Mills* (1949) 79 CLR 389 (HCA).

[153] *PA News Ltd v Loveridge* [2003] EAT/0135/03/MAA.

[154] The term *locus* of control is designed to avoid additional complexities arising out of the fact, noted *inter al* by Freedland (n 5) 45-47, that even in traditional companies without external influence management control is often exercised by more than one person amongst a group of relatively senior executives.

where this led to a highly artificial analysis of the relevant facts. This unitary conceptualisation was strengthened by the growing importance of contract as the main framework for personal work relationships, casting the wage-work bargain as a bilateral contract between individual parties. In the subset of corporate employers, the company then became the bearer of this unitary view.

Upon closer investigation, however, it emerged that in the actual cases testing for employment status, a unitary view was rarely *inherent* in the tests used. Instead, the notion builds on a multi-functional classification of employer's rights and duties. There is nothing to suggest that all employer functions ought necessarily to be exercised by the same entity: they can be exercised jointly by several parties, or parcelled out between different *loci* of control. This results in a deep tension between the two conceptions identified.

As subsequent chapters will demonstrate, that inherent tension becomes an acute challenge for regulatory coverage once employment relationships move beyond a narrow bilateral paradigm: the emergence of a second *locus* of control over the worker can render protective obligations inapplicable; in the case of parcelled-out functions it may even place the individual outside the remit of employment law.

CHAPTER II
THE SHARED EXERCISE OF EMPLOYER FUNCTIONS ACROSS MULTIPLE *LOCI* OF CONTROL

In concluding the last chapter, it was suggested that the tension between a *unitary* and a *multi-functional* strand in the notion of the employing entity would come to the fore in multilateral organisational settings. The present chapter explores such setups with multiple entities or *loci* of employer functions, sharing their exercise between or across different entities. This forms the necessary backdrop for chapter three, where the problematic implications for employment law coverage of such multi-entity scenarios will be spelt out.

From a wide range of potential examples, this chapter will focus on two areas in particular: Private Equity (PE) control over portfolio companies, and the relationships arising from a company's use of temporary work or labour agencies. These are prime examples of the challenges to the paradigm notion of the employer as a singular work-taking counterparty in a bilateral relationship, as an additional *locus* of control over the employment relationship emerges: traditional employer functions become exercised by both management and shareholders, or shared between a work agency and its end-user clients.

The two areas are, at first sight, rather different. When a general picture is abstracted from the different fact patterns, several distinctions become apparent: the entities jointly exercising employer functions in the temporary agency worker scenario, for example, are distinct commercial enterprises, usually contracting with each other at arm's length. The economic incentives of Private Equity portfolio companies, on the other hand, are closely aligned with those of the investing fund, as

the profitability of the latter depends to a significant degree on the performance of the portfolio company. In the agency context, on the other hand, there will usually be no such alignment given distinct ownership and management.[1] It is only when looking at the underlying factual cause of the problem in triangular scenarios that the important similarities become apparent: in both agency work and Private Equity transactions, traditional employer functions are exercised by more than one entity.

Furthermore, whilst both factual scenarios have been the subject of academic scrutiny, different labels have traditionally been applied. On the one hand, agency work can be placed in what Fudge has referred to as the 'commercialisation' of employment:

> In developed countries, commercialisation takes many forms. Employment is increasingly project-, task-, or term-limited rather than ongoing, and pay has been individualised. Self-employment—often in the form of 'freelancers'—has increased, and the distinction between employment and self-employment is blurring as employment practices rapidly change. Labour-only subcontracting, franchises, joint ventures, and project employment are examples of the commercialisation of employment.[2]

The Private Equity model to be discussed, on the other hand, can be placed in the context of discussions about the disintegration of the enterprise,[3] where '[t]he boundaries of the firm have proved to be quite porous, "making it difficult to know where the firm ends and where the market or another firm begins"'.[4] Both examples

[1] Though there are also reports of 'in-house agencies': M Aziz and others, 'Hard Work, Hidden Lives: The Full Report' (TUC Commission on Vulnerable Employment 2008) 188.

[2] J Fudge, S McCrystal and K Sankaran, *Challenging the Legal Boundaries of Work Regulation* (Oñati International Series in Law and Society, Hart 2012) 10 (footnotes omitted).

[3] H Collins, 'Independent Contractors and the Challenge of Vertical Disintegration to Employment Protection Laws' (1990) 10 OJLS 353.

[4] Fudge, McCrystal and Sankaran (n 2) 11, citing also W Powell, 'The Capitalist Firm in the Twenty-First Century: Emerging Patterns in Western Enterprise' in P DiMaggio (ed), *The Twenty-*

are brought together for present purposes, however, as they are stark illustrations of the fragmented exercise of employer functions.

The problems discovered in labour agencies and Private Equity are furthermore a good *pars pro toto* illustration of their respective larger areas: agency work problems are mirrored in areas such as sub-contracting, and the use of personal service companies. PE issues in turn are reflected in corporate groups and in other situations of block shareholders exercising control over a company. They are, finally, both numerically significant in the UK labour market. In 2008, the most recent year for which comparable figures are available, an approximate 1.3 million, or 5% of the UK workforce,[5] worked in a triangular agency setting. Private Equity 'employment' numbers ran to approximately three million workers in PE portfolio companies; the equivalent of more than 21% of private sector employees.[6]

In order to explore the shared exercise of employer functions across multiple entities in the Agency Work and Private Equity contexts respectively, this chapter is structured as follows: the analysis of each area begins with a brief overview of the relevant industry and its regulation, primarily in order to show how the crucial issue of employer status is usually left untouched. A subsequent part then turns to a description of key actors and the relationships between them, which condition the emergence of multiple *loci* of control. Drawing on examples from qualitative fieldwork, discussion finally returns to each of the five employer functions identified in the previous chapter to demonstrate their joint exercise.

First Century Firm: Changing Economic Organization in International Perspective (Princeton University Press 2003) 58.

5 EMAR, 'Agency Working in the UK: A Review of the Evidence' (Employment Relations Research Series No. 93, BERR 2008) Table 1.1, drawing on survey of Recruitment Agencies in 2007.

6 IE Consulting, 'The Economic Impact of Private Equity in the UK' (BVCA 2008) 5.

An emphasis on practical detail at this juncture may be surprising. It is however crucial in order to show how multi-entity work settings are a considerably more prevalent phenomenon than generally assumed; indeed in that sense it could be said that there is little left that is 'atypical' about multiple *loci* of employer functions. The practical examples will furthermore be essential in challenging the traditional assumptions that were seen to underpin much of the unitary notion that emerged in chapter one. As Lizzie Barmes has noted,

> [t]he richness of non-legal accounts and analyses starkly contrast with the abstracted, convoluted and, with respect, frequently baffling, reflections of judges in categorising different kinds of workers in order to determine the statutory rights they have (or more typically, especially the more needful of external protection the working person, that they don't have).[7]

In drawing on these practical illustrations, an important factor to keep in mind is the sheer limitless variety of factual scenarios, and therefore, of ways in which the exercise of employer functions can be shared. At least three different scenarios were identified in the previous chapter: employer functions might be bundled into one entity, shared between two or more entities, or parcelled out between different entities. Joint exercise in the multilateral scenarios to be explored will usually involve a combination of all these different modes, with further complexity added by the fact that the courts increasingly refuse to 'ignore practical aspects of control that fall short of direct legal rights'.[8]

Finally, it is important to note that power accrued to investors or end-users is not necessarily power taken away from management. This insight is the key challenge to a unitary notion of the employing entity in the Private Equity and Agency Work

[7] L Barmes, 'Learning from Case Law Accounts of Marginalised Working' in J Fudge, S McCrystal and K Sankaran (eds), *Challenging the Legal Boundaries of Work Regulation* (Oñati International Series in Law and Society Hart 2012) 305.

[8] *Motorola Ltd v Davidson* [2001] IRLR 4 (EAT) [11].

contexts. Only if the power of control within employment, contractual and corporate governance structures were seen as a zero-sum game would this not be the case: the accrual of power to owners or end-users has to lead to a loss of power for management or the agency only if there is a 'finite amount' of control that is constantly reallocated between different actors. Steven Lukes has convincingly demonstrated, however, that for there to be power, control over a situation can be exercised in many ways, 'whether through the operation of social forces and institutional practices or through individuals' decisions'. Thus understood, additional actors gaining power will increase the overall set of influencing factors and 'can occur [even] in the absence of actual, observable conflict'.[9]

The two-way relationships at the basis of concentrated shareholders' control over corporate management or end-users' detailed contracts for the supply of agency labour fits into Lukes' description of power. They are therefore *additional* loci of power within the employment structure, rather than a subsumption of another entity's influence. This is the key challenge to the unitary strand in the notion of the employer in sole control over the employment relationship, as it emerged in chapter one.

SECTION I: TEMPORARY AGENCY WORK

The first illustration of shared employer function exercise is drawn from triangular or agency work settings, where workers are retained by an agency, and then sent out to work for third-party end-users. It stands as a good example of other areas of the 'informalisation' of work, where workers are placed outside employment law

[9] S Lukes, *Power: A Radical View* (Palgrave 2005) 28.

protection because of the 'externalization' of labour.[10] In labour-only sub-contracting or personal service companies, for example, similar issues will arise as there is no direct (contractual) relationship between the worker and the person or entity behind the economic activity. Whilst such situations have traditionally been analysed from the perspective of the insecurity of some of the most vulnerable workers, triangular work settings are by no means limited to those contexts.[11]

SUB-SECTION 1: THE OPERATION OF THE AGENCY WORK INDUSTRY

Whilst the modern form of work agencies has been in existence since the 1950s, there are early reports of labour market intermediaries dating back as far as the 1920s.[12] Indeed, one of the ILO's earliest measures was to call for a legal response to agency work, in the rather radical form of a complete prohibition of employment agencies.[13] In gauging the size of the industry in the United Kingdom today it is rather difficult to obtain accurate data, as agency work is not always distinguished as such in published statistics riddled with curious exceptions,[14] and because issues of classification tend to

[10] T Teklè, 'Labour Law and Worker Protection in the South: An Evolving Tension Between Models and Reality' in T Teklè (ed), *Labour Law and Worker Protection in Developing Countries* (Hart 2010) 3, 20 (as cited by Fudge, McCrystal and Sankaran (n 2) 2).

[11] A Pollert and A Charlwood, 'The Vulnerable Worker in Britain and Problems at Work' (2009) 23 Work, Employment and Society 343.

[12] C Forde and G Slater, 'The Role of Employment Agencies in Pay Setting' (ACAS Research Paper 05/2011) [2.1] citing C Forde, '"You know we are not an employment agency": Manpower, Government and the Development of the Temporary Employment Agency Industry in Britain' (2008) 9 Enterprise and Society 337.

[13] ILO Unemployment Recommendation 1919 (No 1), Art 1; as noted by E McGaughey, 'Should Agency Workers be Treated Differently?' (LSE Working Papers 07/2010) 8. The ILO has softened its stance since.

[14] EMAR (n 5) [1.1], for example, excludes entertainment, modeling, writers and professional sports persons.

lead to significant underestimates.[15] The best current estimates date from 2008, when the number of agency workers was put at a mid-point of 1.3 million, with other sources reporting figures as high as 1.5 million.[16]

Despite these problems in measuring the precise extent of the industry, two things are clear: it has undergone rapid growth,[17] a trend which continued soon after a brief stagnation during recent periods of recession.[18] Second, relative to the overall size of the labour market, the industry is larger in the UK than anywhere else in the European Union (EU), or indeed globally.[19] The lowest estimates of industry size suggest that there are about 6,500 agency work companies, with a total number of branches between 9000 and 15,000[20] and turnover in excess of 28,082 million Sterling.[21] BERR suggests that there are approximately 16,000 agencies across the UK, employing a combined workforce of approximately 225,000 people to match agency workers with assignments.[22]

15 E Markova and S McKay, 'Agency and Migrant Workers: Literature Review' (TUC Commission on Vulnerable Employment 2008) 6. The review extensively covers most of the material cited in the first part of this chapter.

16 EMAR (n 5) Table 1.1.

17 C Forde, G Slater and F Green, 'Agency Working in Britain: What Do We Know?' (Centre for Employment Relations Innovation and Change Policy Report Number 2, CERIC 2008).

18 C Forde and G Slater, 'A Survey of Non Regular Work in the UK' (Report prepared for the Japan Institute of Labour Policy and Training 2010).

19 E Berkhout, C Dustmann and P Emmder, 'Mind the Gap' (International Database on Employment and Adaptable Labour 2007)

20 D Winchester, 'Thematic feature: Temporary Agency Work in the UK' (National Report 2007; available through the EIROnline database at <www.eurofound.europa.eu> (accessed 1 September 2012).

21 J Arrowsmith, 'Temporary Agency Work in an Enlarged European Union' (Office for Official Publications of the European Communities, Luxemburg 2006).

22 EMAR (n 5) [1.3].

Regulatory Context

There are several layers of industry regulation through domestic and European Union measures. In spite of this, the crucial question for present purposes – the actual status of an entity as the employer of temporary workers – is not defined for employment law purposes – in stark contrast, for example, to taxation.[23] The question is therefore left to the common law, the implications of which will be discussed in the first section of chapter three.

In the domestic context, agencies were first regulated by the Employment Agencies Act 1973[24] under somewhat different terminology. The Act drew a distinction between 'employment agencies', businesses who find employment for workers or search workers for companies, and 'employment businesses', enterprises that supply workers to end-user. The latter are however commonly understood to be employment agencies today. The legislation set certain minimum standards, for example, as regards payments by workers and accuracy of advertisements, and crucially, made provisions for a mandatory licensing regime. The latter was however revoked in 1994.[25]

Various Regulations introduced under the Act are in operation today, most notably the Conduct of Employment Agencies and Employment Businesses Regulations 2003,[26] placing a series of general obligations on agencies to avoid particular

[23] S Deakin and G Morris, *Labour Law* (6th edn Hart 2012) [3.35]: Income Tax (Earnings and Pensions) Act 2003, pt II ch 7, and Social Security (Categorisation of Earners) Regulations, SI 1978/1689.

[24] This was at the same time as most other European countries, see eg the *Arbeitnehmerüberlassungsgesetz* 1972 in Germany.

[25] Deregulation and Contracting Out Act 1994.

[26] As amended: Conduct of Employment Agencies and Employment Businesses (Amendment) Regulations 2007, SI 2007/3575.

instances of exploitation:[27] an agency cannot, for example, force workers to use additional services or hire and purchase goods from the agency,[28] and it may not withhold payment for a number of reasons, including 'non-receipt of payment from the hirer.'[29] There is also a prohibition on supplying workers to break industrial action,[30] and the requirement that the parties agree on certain terms before any services are provided.[31] A partial licensing system was reintroduced in 2004 by the Gangmasters (Licensing) Act,[32] limited in its application by a sector-specific focus on areas such as agriculture and food processing.[33] Overall, however, the UK remains one of only five EU countries that do not require a license to operate a temporary work agency.[34]

On the European level, consensus on regulating work agencies proved impossible to achieve over a period of nearly thirty years. A Directive on Temporary Agency Work[35] was eventually enacted in the autumn of 2008, with the primary aim of providing for equality in treatment of temporary agency staff and an end-user's permanent workforce.[36] This is significantly weakened, however, not only because of

27 Conduct of Employment Agencies and Employment Businesses Regulations 2003, SI 2003/3319, pt II.

28 ibid reg 5.

29 ibid reg 12(a).

30 ibid reg 7.

31 ibid pt III; Markova and McKay (n 15) 33.

32 s 7.

33 s 3.

34 M Wynn, 'Regulating Rogues? Employment Agency Enforcement and Sections 15–18 of the Employment Act 2008' (2009) 38 ILJ 64, 69.

35 Directive (EC) 104/2008 of the European Parliament and of the Council of 19 November 2008 on temporary agency work [2008] OJ L 327/9.

36 ibid art 5.

the way the scope of application of the directive is defined,[37] but also given the significant number of carve-outs and exceptions, most importantly as to the minimum length of service provision before the equality duty applies.[38] It is therefore unsurprising that Countouris and Horton conclude that the Directive 'is a regulatory instrument that seeks to remove any remaining stigma, restriction or prohibition, associated with temporary agency work without providing for a sufficiently protective, equitable and fair regulatory framework.[39] The United Kingdom's implementation in 2010[40] reluctantly gave effect to the basic rights set out in the Directive, for example as regards the use of joint facilities and the provision of information about job vacancies from the start of the employment.'[41] As already suggested, however, there are significant carve-outs, most notably in the form of a 12-week threshold,[42] which end-users will frequently explicitly contract around by limiting the length of any individual assignment to an 11-week period.[43] Liability for breach of various obligations is apportioned between the agency and its end-user client, subject to the latter's ability to invoke a series of defences.[44]

The overall weakness of the combined domestic and European regulatory efforts is compounded by a glaring lack of enforcement, primarily due to a lack of significant

37 N Countouris and R Horton 'The Temporary Agency Work Directive: Another Broken Promise?' (2009) 38 ILJ 329, 330.

38 ibid 333.

39 ibid 338.

40 Agency Workers Regulations 2010, SI 2010/93.

41 ibid regs 12 and 13.

42 ibid reg 5.

43 Eversheds LLP, 'Terms and Conditions for the Supply of Services from an Employment Business to an End-User Client' (PLC Employment and PLC Commercial, Practical Law Company, London 2012) 2.10.

44 Agency Workers Regulations (n 40) reg 14.

numbers of inspectors and the division of responsibilities between overlapping bodies such as the Employment Agencies Standards Inspectorate (EASI) and the Gangmasters Licensing Authority (GLA).[45] The Employment Act 2008 brought some improvements in this regard,[46] but commentators continue to note a 'disturbing picture of variations in enforcement activity across the UK recruitment industry'[47] as a result of weak enforcement mechanisms.[48] It is not surprising, then, when Markova and McKay conclude that 'in practice it is possible for agencies to open for business without having to meet any regulatory standards.'[49] Despite individual examples to the contrary, high levels of non-compliance are reflected in qualitative studies across the board.[50]

In conclusion, it should briefly be noted that some existing statutory regulation, for example in the areas of health and safety or anti-discrimination, can extend into the operation of work agencies. The actual status of workers or employers for employment law purposes is not defined, however; an omission that is in clear violation of ILO norms.[51] The specific industry regulation seen here will therefore be mostly excluded from future chapters,[52] as it merely tinkers 'at the edges of the problem rather than dealing with the matter at the heart of this area of law [*viz*, …] the

45 McGaughey (n 13) 12.

46 eg Employment Act 2008, s 16 (increased EASI inspection powers).

47 Wynn (n 34) 72.

48 Equality and Human Rights Commission (EHRC), 'Inquiry into Recruitment and Employment in the Meat and Poultry Processing Sector' (EHRC 2010) 31.

49 E Markova and S McKay, 'Understanding the Operation and Management of Employment Agencies in the UK Labour Market' (TUC Commission on Vulnerable Employment, London 2008) 8.

50 Aziz (n 1) 127.

51 ILO Private Employment Agencies Convention 1997 (No 181).

52 Notably the Employment Agencies Act 1973 and the Conduct Regulations 2003 (n 27).

issue of the employment status and protective employment rights of agency workers.'[53]

SUB-SECTION 2: A MULTIPLICITY OF ENTITIES

Discussion thus turns to the first step in the practical illustration: the following paragraphs will look at agencies and end-users as key actors in the triangular setup, briefly explore the potential motivations for the use of agency labour, and analyse how the multi-partite relationship is structured through contracts for the supply of labour.

Employment Agencies

Employment Agencies recruit workers on an on-going basis in order to provide labour to clients on individual 'assignments'. In a highly fragmented market, over half of the temporary work agencies in the United Kingdom are very small operations, directly employing less than five people; less than one per cent have staff exceeding 200.[54] The majority of agencies operate from a single establishment.[55] Forde and Slater have identified at least three different typologies,[56] beginning with agencies' geographical span: whilst some operate only in a limited area, others have branches across the country. Second, whilst some large firms operate as general workforce providers, most agencies have a specific occupational and sectoral focus. Finally, agencies vary as regards the nature of their contractual relationships with end-users, from one-off

53 P Leighton and M Wynn, 'Temporary agency working: is the law on the turn?' [2008] Company Lawyer 7, 8.

54 EMAR (n 5) [1.3].

55 ibid.

56 Forde and Slater (n 12) 10ff.

short term hires to 'in-house' labour agencies at large corporations.[57] Qualitative fieldwork reports confirm this high degree of factual variation.[58] It is also mirrored in the broad range of different jobs done by agency workers,[59] from providing cleaning services to piloting commercial passenger aircraft.[60]

End-Users or Clients

Nearly one fifth of workplaces in the United Kingdom rely on the services of temporary agency workers,[61] with a fairly clear concentration in larger enterprises: over 50% of temporary agency workers are seconded to work in enterprises with more than 50 employees.[62] BERR figures suggest that production industries (including, for example, agriculture, construction, and manufacturing) make up 25% of agency clients, and private sector service companies 33-45%.[63] Other sources suggest a different makeup, leaving the overall picture rather unclear.[64] The role of the public sector in procuring the services of labour agencies should also not be underestimated: several of the leading cases to be discussed in subsequent chapters involve public

57 Aziz (n 1) 188.

58 See eg the list of different agencies reviewed by McKay and Markova (n 49) 16-21.

59 EMAR (n 5) 11-12.

60 See eg the agency recruiting for Ryanair: <www.stormmcginley.com/p/h/Home/Job_Details/29/?lang=&rcv_id=339&fromrss=yes> accessed 1 September 2012.

61 B Kersley and others, *Inside the Workplace: First Findings from the 2004 Workplace Employment Relations Survey* (Routledge, London 2005) (as cited in Forde and Slater (n 12) [2.1].

62 EMAR (n 5) 4-5.

63 ibid 3-4.

64 Markova and McKay (n 15) 17.

authorities, and fieldwork reports give numerous examples such as a London local authority which sources nearly 20% of its staff from agencies.[65]

When enquiring into the motivations behind the use of agency work,[66] different studies have uncovered a wide range of potential reasons, with considerable divergence between the answers offered by end-users and agencies. Users' arguments range from numerical flexibility to meet peaks and troughs in demand to obtaining specific skills or ensuring temporary leave and maternity cover.[67] Markova and McKay summarise these reasons under a series of categories.[68] Flexibility is considered to be of prime importance, though it is not always clear to what extent this is limited to complementarity, ie the use of agency workers in situations where required staff numbers rise temporarily, or whether there is an increasing move towards substitution of permanent employees and the long-term hiring of a workforce through agencies. Cost savings are a second factor frequently identified, though a considerable number of end-users suggest that there are little, if any, overall savings. Legal factors, finally, also loom large. Some studies suggest that employers' primary motivation is not the avoidance of employment law regulation as such, but rather the possibility of shifting liability for immigration law violations, with the agency in charge of organising work permits, checking workers' documents and ensuring on-going compliance.[69] Other studies, however, have found that up to a quarter of end-

65 Markova and McKay (n 49) 18.

66 See also S McKay, 'Employer Motivations for Using Agency Labour' (2008) 37 ILJ 296.

67 See eg EMAR (n 5) Table 4.1.

68 Markova and McKay (n 15) 19ff, drawing on L Gramm and J Schnell, 'The Use of Flexible Staffing Arrangements in Core Production Jobs' 2001 (54) Industrial and Labour Relations Review 245; K Hakansson and T Isidorsson, 'Flexibility, Stability and Agency Work: A Comparison of the Use of Agency Work in Sweden and the UK' in B Furaker, K Hakansson and J. Karlsson, *Flexibility and Stability in Working Life* (Palgrave 2007) 123; P Allan, 'The Contingent Workforce; Challenges and New Directions' (2002) American Business Review 103.

69 Markova and McKay (n 49) 24-25.

user firms rely on agency labour specifically in order to avoid incurring employment law obligations.[70]

Contractual setup

The formal relationship between agencies and end-users can be structured in myriad ways,[71] from on-the-spot contracting to increasingly common long-term relationships between a particular agency and end-user.[72] Some agencies have preferred or even sole supplier status with individual clients; others rely on framework agreements to standardise individual one-off hires.[73] A more recent development is temporary work agencies that act as third party vendors to coordinate other agencies organising external workforces for clients, without providing any workers directly. Greenwich London Borough Council, the defendant in the now infamous case of *James*,[74] for example, employed more than 10% of agency workers at the time of the litigation, and had to retain the services of a large national employment agency to manage its various supplier agencies.[75]

The analysis of an anonymised sample contract used as the basis for negotiations between agencies and end-users[76] suggests that key terms between agency and end-user will usually go beyond the legally required minima, such as fee calculation and

70 EHRC (n 48) 22.

71 Forde and Slater (n 12) 11-14.

72 See K Purcell, J Purcell and S Tailby 'Temporary Work Agencies: Here Today, Gone Tomorrow?' (2004) 42 BJIR 705; Markova and McKay (n 49) 30-31 offer practical illustrations.

73 I Kirkpatrick and others, 'Professional Agency Working in Health and Social Services: Implications for Management' (CERIC Policy Report Number 3, CERIC 2009).

74 *James v Greenwich LBC* [2008] EWCA Civ 35, [2008] ICR 545.

75 McGaughey (n 13) 26.

76 Eversheds (n 43).

termination procedures.[77] The agencies' duties may be set out in great detail, including as to where and how workers should be recruited, which background and immigrations checks are to be completed, any additional licences, authorisations and references that may be required, and the details of information about each temporary worker to be supplied to the end-user.[78] These information provisions are generally mutual, ie the end-user's obligations will cover provision of information about what workers are required and when.[79] There are, however, also reports of situations where end-users have little knowledge of the terms and conditions offered by agencies to workers.[80] Both parties will usually enjoy strong termination rights,[81] and be subject to confidentiality, audit, record-keeping and indemnity requirements. The contractual agreements, finally, will include detailed arrangements for fee and transition payment and tax structures, as well as the already referenced clause limiting the length of any individual assignment in order to avoid the application of the 2010 Agency Workers Regulations.[82]

SUB-SECTION 3: THE SHARED EXERCISE OF EMPLOYER FUNCTIONS

In moving from a summary of the organisational and regulatory setup of the employment agency industry to a detailed account of how the five employer functions under scrutiny are jointly exercised, discussion in the present sub-section will draw on a broad range of sources that document the day-to-day operation across different

77 Conduct Regulations 2003 (n 27) reg 17.

78 Eversheds (n 43) cl 2.

79 ibid cl 3.

80 Markova and McKay (n 49) 8.

81 Eversheds (n 43) cl 5.4.

82 Eversheds (n 43) cl 2.10 'The Employment Business shall not provide any Temporary Worker for a period in excess of 11 weeks without the prior written consent of the Client.'

sectors. There is, first, a considerable body of litigation concerning the status classification of temporary worker, which frequently summarises the relevant involvement of different entities.[83] As Lizzie Barmes has noted, however, even where such summaries can be found in reported decisions, they are usually limited to a small cross-section of the actual factual scenario, and can present a very abstract image. [84] It is therefore necessary to rely on additional field studies in scrutinising the five functions. A range of such sources has recently become available, most notably in the form of a report by Sonia McKay and Eugenia Markova on the Operation and Management of Employment Agencies in the UK Labour Market,[85] a sector-specific study on Working Conditions in the Meat Processing Industry,[86] and several profile-based case studies found throughout the Full Report of the Commission on Vulnerable Employment.[87] One interesting effect of relying on these sources can be noted at the outset: while the case law frequently suggests a clear parcelling out of functions between different entities, the qualitative field work reports show a much more diffuse picture, with agencies and end-users both involved (albeit to different degrees) in the exercise of the full range of employer functions.

1) Inception and Termination of the Contract of Employment

As regards the first function, this will usually be the primary task of the employment agency: a worker is taken on its books, and contracted out to end-users at the agency's

[83] Barmes (n 7).

[84] ibid 314.

[85] Markova and McKay (n 49).

[86] EHRC (n 48).

[87] Aziz (n 1).

discretion. [88] Agencies can also shortlist and select candidates on the end-user's behalf,[89] and be in charge of organising work permits and checking other qualifiations and documents.[90] End-users are however also sometimes involved in the selection of individual workers, and there are reports of instances where they do so for illegal purposes, for example by specifying a particular race or nationality of the agency worker to be supplied.[91]

As regards influence over the setting of terms, there is again a wide variety of different models, though end-users generally seem to have only 'limited knowledge of agency workers' terms and conditions'.[92] At least one report suggests that end-users 'found that they had no influence on changing terms and conditions, and indeed agency workers had been forbidden [by their agencies] from even talking to the [clients] about their pay rates.'[93] Public sector users are an exception in this context, with most local authorities insisting on direct control over agency workers' terms and conditions.[94]

General Human Resource (HR) functions including appraisals will usually be exercised by the agency.[95] Termination and replacement is likewise via the agency

88 Markova and McKay (n 49) 39ff.

89 Markova and McKay (n 15) 20; citing C Stanworth and J Druker, 'Human resource solutions? Dimensions of Employers' Use of Temporary Agency Labour in the UK' (2006) 35 Personnel Review 175.

90 Markova and McKay (n 49) 24-25.

91 EHRC (n 48) 8.

92 Markova and McKay (n 49) 40.

93 ibid 42.

94 ibid.

95 Forde and Slater (n 12) 12.

itself, [96] usually upon the end-user's request, [97] and without significant notice periods.[98] Some clients, however, may retain a direct right to dismiss the employee,[99] again with several reports of this function being exercised for inappropriate reasons, such as dismissing a female line worker.[100]

2) Receiving Labour and its Fruits

While it could be suggested that agencies' profit margins are a result of the workers; labour,[101] the second function rests firmly with the end-user; indeed this is usually the very reason for the triangular relationship. The extent to which this is an actual legal duty owed directly to the client varies, however,[102] as the agency will not normally rely on the worker to provide services for its own purposes. Indeed, some end-users increasingly report concerns about the quality of work received, with some linking it to a lack of temporary workers' loyalty to the client.[103]

3) Provision of Work and Pay

The division of this third employer function is amongst the more difficult to analyse, as it varies drastically across different scenarios. Looking first at the obligation to

96 Aziz (n 1) 189.

97 Leighton and Wynn (n 53) 9.

98 McGaughey (n13) 2.

99 *Muschett v HM Prison Service* [2010] EWCA Civ 25, [2010] IRLR 451, 14.

100 EHRC (n 48) 11-12.

101 Forde and Slater (n 12).

102 Suggested to exist in *Tilson v Alstom Transport* [2010] EWCA Civ 1308, [2011] IRLR 169; cf *James* (n 74), where no duties were owed to the employer.

103 Aziz (n 1) 190.

provide work, the agency will normally not be under any obligation to do so. Leighton and Wynn cite the following sample contractual clause:

> We, the agency, will do our best to find you work that suits you and you, the temp, will in turn agree not to unreasonably refuse suitable work when offered.[104]

The situation of the end-user is less clear. While an obligation to provide work is rarely found on the facts,[105] there have been decisions to the contrary, especially where the employee was deeply integrated in the end-user's undertaking, up to and including managerial control over the end-user's permanent employees.[106] Whilst the provision of day-to-day work is therefore clearly a role of the end-user, for example in choosing the allocation of particular jobs,[107] such findings will be rare. In reality, workers will frequently turn up at an end-user's site in the morning only to find that on that particular day no work is available.[108]

The provision of pay, on the other hand, is usually a function exercised by the agency, together with general payroll and tax services. Suggestions that an employment agency merely acts as the end-user's agent in this regard no longer seems to feature in the most recent case law.[109] While wages are nearly always paid to workers by their agency or a payroll company associated with it,[110] the question as to who actually determines the levels of remuneration yields a much more mixed

[104] Leighton and Wynn (n 53) 12.

[105] See eg *James* (n 74).

[106] *Alstom* (n 102).

[107] EHRC (n 48) 10.

[108] Aziz (n 1) 14 (John's story).

[109] Though cf Munby J's dissent in *Cable & Wireless Plc v Muscat* [2006] EWCA Civ 220, [2006] ICR 975.

[110] EHRC (n 48) 16.

response, as a recent report for ACAS shows. The traditional assumption, backed up by early empirical studies, was that pay levels were driven primarily by how much the end-user paid the agency.[111] In *James*, on the other hand, it was pointed out that different agencies sometimes offer distinct pay levels for identical jobs: the claimant was found to have 'changed agencies rather then employers in order to obtain a higher wage.' [112]

It has also been suggested that during positive economic climates agencies will have more power to set pay levels[113] as well as additional benefits, such as holiday pay.[114] Any suggestions of a clear overall picture, however, betray immense factual variation and complexity. This is frequently illustrated in situations where problems arise once an end-user has paid its fees to an agency, without workers ever receiving their wages,[115] or being paid late and only after incurring much hassle.[116]

4) Managing the Enterprise-Internal Market

The facts of most reported cases suggest that function four rests firmly with the end-user. In *James*, for example, the council conceded at the outset that it had exercised full control over the claimant.[117] In *Alstom*, counsel for the end-user went even further in agreeing with the court that on the basis of a 'significant degree of control', there had been 'a direct contractual relationship between Alstom and the appellant, [and it

[111] Forde and Slater (n 12) 19.

[112] *James* (n 74) [41], [15].

[113] Forde and Slater (n 12) 30.

[114] ibid 35.

[115] Aziz (n 1) 133 (Michael's story).

[116] ibid 116 (Pietr's story).

[117] *James* (n 74) [12].

would have been characterised] as a contract of service.'[118] But agency involvement frequently goes further than these reports suggest. The starkest illustrations of this are agency offices on the client site as seen in *Astbury v Gist*.[119] Other reports suggest that this was by no means an isolated incident,[120] and that some local authorities even have more than one agency physically represented on their premises.[121]

Agencies may also sometimes influence what work is done and how, for example when a cleaning agency instructs its workers how to prepare and apply certain chemicals.[122] Agency involvement may even go as far as the selection of employees for specific tasks or other clients, to the potential frustration of the original end-user where 'the agencies […] "skim off" the best workers or move them on, even when the company was keen to keep them.'[123] As regards time worked, it will usually be the end-user who sets the hours where workers' presence is required, with control exercised right down to when toilet breaks may be taken.[124] Again, however, there is also evidence of agency involvement, for example where workers are forced to leave their accommodation and go to work in the morning, or the case of the 'agency managers standing at the factory exit and turning back agency workers to force them to work overtime when they tried to leave the factory after their shift had ended.'[125]

[118] *Alstom* (n102) [4].

[119] *Astbury v Gist Ltd* [2007] UKEAT/0619/06/DA.

[120] Including the public sector: K Hoque and others, 'New Contractual Relationships in the Agency Worker Market: the Case of the UK's National Health Service' (2008) 46 BJIR 389.

[121] Aziz (n 1) 14.

[122] Aziz (n 1) 18 (Angela's story).

[123] Markova and McKay (n 49) 29.

[124] EHRC (n 48) 11.

[125] ibid 14.

Working-time opt-out signatures under the Working Time Regulations 1998[126] are usually required by both agency and end-users.[127]

Wynn and Leighton suggest that agencies will rarely be involved in managing their client's internal affairs, on the basis of a distinction between operational and transactional control (the former falling under category [1] in the present classification).[128] As the present discussion has demonstrated, on the other hand, agencies may frequently be involved in a client's enterprise-internal market, with examples reaching as far as the reported requirement by an agency that its end-user client install on-site washing machines and shower facilities.[129]

5) Managing the Enterprise-External Market

The allocation of the final function is likewise distributed in myriad ways: when measured against the common law criterion of undertaking an economic activity in return for potential profit whilst also under the risk of direct exposure to loss, it can be seen as, in some sense, shared between end-user, agency, *and the worker himself*. In *Alstom*, for example, the claimant had repeatedly refused to be engaged under a contract of employment with the end-user directly, as 'he was on a significantly higher rate of pay under the agency arrangements' and 'also perceived there to be tax advantages'.[130] The oft-cited provision of tools, including health and safety equipment and relevant training is sometimes seen as the task of the agency,[131] and at other times

[126] SI 1998/1833, reg 5.

[127] EHRC (n 48) 12.

[128] Leighton and Wynn (n 53) 9.

[129] Markova and McKay (n 49) 34 (Food Company G).

[130] *Alstom* (n 102) [5].

[131] Markova and McKay (n 49) 33 (Food Company A vs. Food Company G)

as that of the end-user, who may even force workers to share particular items.[132] There are also frequent reports of workers having to provide their own uniforms and protective equipment.[133] Specific training will usually be provided by the end-user,[134] though generally at a lower level than for permanent staff,[135] whereas some agencies also provide broader skills training.[136]

The chance of making profits or incurring losses, for example due to a contractual obligation to keep paying workers even when there is no work available, will usually be born by *neither* agency nor end-users, thus shifting the risk directly onto individual workers who will not get paid when no work has been offered.[137]

In conclusion, then, it has been seen how extremely 'varied and variable'[138] the arrangements between different *loci* of employer functions in the triangular agency work context can be. It should also be remembered that the joint exercise of employer functions takes place on a spectrum ranging from complete parcelling out, where different entities have exclusive competence in certain areas, to a high degree of overlap. A single triangular setting will usually involve a combination of these. A good illustration of this arose on the facts of *Dacas v Brook Street Bureau (UK) Ltd*,[139] where the claimant was an agency worker employed to clean hostels for a local

[132] Aziz (n 1) 22 (Victor's story).

[133] ibid 27 (Imran's story).

[134] eg Markova and McKay (n 49) 34 (Local Authority B); 26 (Food Company A).

[135] Aziz (n 1) 188.

[136] *Heatherwood and Wexham Park Hospitals NHS Trust v Kulubowila* [2006] UKEAT/0633/06/LA; Forde and Slater (n 12) 36.

[137] J Hacker, *The Great Risk Shift: the New Economic Insecurity and the Decline of the American Dream* (OUP 2008).

[138] Leighton and Wynn (n 53) 8.

[139] [2004] EWCA Civ 217; [2004] ICR 1437.

authority (the end-user). Under the arrangement, the agency paid the worker (function [1]), while day-to-day control over her work (function [4]) was exercised by the local authority. An example of shared exercise, on the other hand, can be found in situations were both agency and end-user have the right to terminate the worker's engagement,[140] or indeed the many diffuse situations encountered above.

SECTION II: PRIVATE EQUITY

Discussion thus turns to a second example of multi-entity employer function exercise: the Private Equity industry. As the traditional model of dispersed shareholdings has increasingly come under pressure,[141] industry analysts have noticed a strong trend towards concentrated ownership, from block holdings to outright subsidiary ownership. Private Equity funds are a prime example of this shift towards relational, or 'insider',[142] systems of corporate governance. Concentrated share ownership is particularly challenging in the employment context, as it leads to multiple parties potentially exercising traditional employer functions. Once the majority, or at least a significant proportion of, voting rights are vested in a single shareholder, it will be able to exert considerable power over management. Gospel and Pendleton, drawing on research by Holland,[143] describe this power as the result of a two-way relationship:[144] through individual, usually private, meetings with senior management, detailed

[140] Muschett (n 99); see also *Construction Industry Training Board v Labour Force Ltd* [1970] 3 All ER 220 (HC).

[141] H Gospel and A Pendleton, 'Markets and Relationships: Finance, Governance, and Labour in the United Kingdom' in H Gospel and A Pendleton (eds), *Corporate Governance and Labour Management: An International Comparison* (OUP 2005) 71.

[142] ibid 62.

[143] J Holland, 'The Corporate Governance Role of Financial Institutions in Their Investee Companies' (Research Report No. 46, Chartered Association of Certified Accountants 1995) 19.

[144] Gospel and Pendleton, 'Markets and Relationships: Finance, Governance, and Labour in the United Kingdom' (n 141) 75.

information about the company flows to its owners. This information covers both matters of long-term strategic planning, and daily operational details (thus covering all elements of the employment relationship), and forms the basis of investors' control, in 'a clear break with the traditional view of investor passivity in corporate governance'. [145] The firm's management will pay close attention to investors' opinions, even if not voiced expressly, as this 'network of relationships […] provides an effective means […] for investors to force changes on management'.[146] This is an important addition to the more traditional company law tools of control, such as replacing directors on the corporation's board – another example of controlling action that is available to majority shareholders.

In a strict technical sense, Private Equity refers to an asset class that comprises the entirety of equity investments not quoted on public exchanges. [147] In commercial reality, on the other hand, there is consensus that the meaning of the term is much more limited – even if its exact boundaries remain unclear. PE financiers are said to 'provide capital to invest in unquoted companies including public companies that are de-listed as part of the transaction. These investments may take the form of a purchase of shares from an existing shareholder (a buy-out if control is acquired) or an investment in new shares providing fresh capital to the investee company (development capital).'[148] The value of these equity stakes in high risk / potentially high reward projects is protected by undertaking careful due diligence before making

[145] ibid.

[146] ibid 79.

[147] T Jenkinson, 'Private Equity' in European Economic Advisory Group (ed) *Report on the European Economy* (CESifo 2009) 124.

[148] J Gilligan and M Wright, *Private Equity Demystified: An Explanatory Guide* (2nd edn ICAEW Corporate Finance Faculty 2010) 16.

the investments and retaining powerful oversight rights afterwards.[149] The industry is further divided between funds providing capital to companies in their early life, with a focus on growth and expansion (venture capital) and investments in mature companies, usually in form of a buy-out: the meaning of Private Equity that is most relevant for present purposes. Mature companies are acquired by PE funds directly from public markets in so-called Public to Private (P2P) transactions, from private ownership, or increasingly from other investment funds through secondary buyouts. The same interest groups usually represent both branches of the industry;[150] in economic terms, however, buy-out activity is significantly more important than venture capital. A range of other alternative investment funds are sometimes mistakenly characterised as, or equated to, Private Equity partnerships. Confusion arises most frequently as to the relationship between hedge funds and PE. The main difference here is that the former focus on an infinite variety of relatively liquid trading strategies, moving quickly in (usually) public markets.[151] While some activist hedge funds do seek to influence company managers, they usually do so with only a small stake in the company, and their influence is never *contractual*: the primary way of putting formal pressure on management is by divesting shares. As Private Equity management companies seek to build larger investment portfolios and hedge funds move into less liquid investment strategies there is considerable room for convergence between different types of alternative investment funds;[152] for present purposes, however, the focus remains on 'traditional' PE management companies involved in the acquisition and restructuring of mature companies.

[149] P Gompers and J Lerner, *The Venture Capital Cycle* (MIT Press 2004) 1.

[150] The British Venture Capital and Private Equity Association (BVCA) on a national level; a member of the EVCA (European Private Equity and Venture Capital Association).

[151] For a taxonomic overview, see P Myners, *Institutional Investment in the United Kingdom: A Review* (HM Treasury 2001) 157-8.

[152] J Bevilacqua, 'Convergence and Divergence: Blurring the Lines between Hedge Funds and Private Equity Funds' (2006) 54 Buffalo Law Review 251, 253.

The underlying economic rationale of this industry can be summarised in three main strands. The first of these rejects traditional models of firms built on managerial discretion and shareholder deference to professional managers,[153] focussing on the agency costs that arise from a misalignment of owners' and managers' interests.[154] Private Equity, it is suggested, can overcome this problem by giving senior management a significant equity stake in the enterprise, thus closely aligning the interests of all parties.[155] The sharp incentive structure thus set up is usually reinforced by considerable levels of debt, requiring optimisation rather than maximisation of the underlying business.[156] Second, a clearly defined and closely monitored obligation to service creditors[157] settles what could otherwise be a constant struggle between owners and managers over the allocation of free cash-flow;[158] thus removing further inefficiencies that are said to result from the public corporation's split between ownership and control. Finally, the much more detailed and regular provision of information about the company to investors considerably reduces the price of financing operations by overcoming the 'lemons market' problem, where uncertainty about the true quality of a product impedes otherwise beneficial market transactions.[159] As traditional retail banks lack the institutional capacity for this sort of

153 A Berle and G Means, *The Modern Corporation and Private Property* (Macmillan 1939).

154 A Alchian and H Demsetz, 'Production, Information Costs, and Economic Organization' (1972) 62 The American Economic Review 777; W Meckling and M Jensen, 'A Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 Journal FE 4.

155 I Clark, 'The Private Equity Business Model and Associated Strategies for HRM: Evidence and Implications?' (2009) 20 International Journal of Human Resource Management 2030, 2033.

156 Jenkinson (n 147) 132.

157 M Jensen, 'The Eclipse of the Public Corporation' (1989) 67 HBR 61, 64; 1997 revision 18.

158 Gilligan and Wright (n 148) 84.

159 G Akerlof, 'The Market for "Lemons": Qualitative Uncertainty and the Market Mechanism' (1970) 84 Quarterly Journal of Economics 488.

monitoring oversight, the Private Equity industry has come to fill the niche role.[160] There are three ways for Private Equity investments to create returns in practice.[161] First, business performance can be improved, specifically by increasing the free cash flow of the enterprise.[162] This in turn is necessary to fund the second driver of increased returns, financial leverage: as long as the overall price of an asset remains stable, the value of its equity is set to increase as debts secured against it are being paid off. Finally, operational changes and new business environments can increase the overall value of a company, by increasing the multiple at which it can be sold on.[163] The following chapters focus on the first of these value drivers, as it is here that *management* skills are at the core of what PE management companies do. Business performance has traditionally been improved by focussing on revenue growth, consolidation, and cost reduction;[164] with the latter not necessarily as the primary driver of efficiency gains.[165]

Before turning to a detailed examination of the industry and the resulting joint exercise of employer functions, it should be noted that Private Equity is a good example, *pars pro toto*, in the present context of inter-corporate control of corporate groups more generally. The key challenge for present purposes, *viz* the involvement of external shareholders in detailed management as an example of multiple loci of control, comes out most starkly in Private Equity context. The relationships that will

[160] Gompers and Lerner (n 149) 4-5.

[161] T Franklin, 'What Private Equity Investors Look For: Investments, Managers, Advisers and Professionals' in M Soundy, T Spangler and A Hampton (eds), *A Practitioner's Guide to Private Equity* (City & Financial 2009) 13-14.

[162] The financial measure for this is usually EBITDA.

[163] One way of valuing businesses is by multiple of EBITDA.

[164] Franklin (n 161) 20.

[165] Ernst & Young, 'How Do Private Equity Investors Create Value? A Study of 2006 Exits in the US and Western Europe' (2006).

be discussed sit on a particularly salient point along different axes of inter-corporate relationships,[166] combining each relevant facet in its strongest possible instantiation. The key points of subsequent findings will therefore also hold true for corporate groups. As regards the allocation of control between insider and outsider models of corporate governance, for example, Private Equity is identical to corporate groups in a strong focus on insider control, drawing on a range of sources from company law and contractual agreements to commercial pressure. As regards the incentive alignment between management and shareholder, there are similar parallels. The intensity, purpose, and actual exercise of a shareholder's control over an underlying entity, finally, can be strategic or operational. In corporate groups this will depend on different areas of the business, individual management structures and sometimes even historical accident. The hands-on approach of control-oriented Private Equity management companies, on the other hand, provides the clearest possible example of external control.

Operations in the PE industry therefore provide a particularly salient subset in which to illustrate the conceptual tension in the notion of the employer. Given the financial and reputational constraints prevalent throughout the industry, however, there has been comparatively little litigation on which an exploration of practical implications in the following chapter could draw. On the basis of the foregoing observation, however, the relevant subset will be extended in chapter three to include corporate groups more generally, by carefully moving along the various axes just identified, thus ensuring that any differences are of degree, rather than of kind.

Despite a range of differences between Private Equity funds and the corporate group as economic entities – for example, as regards the longevity of the involvement,

[166] E Berglöf, 'Reforming Corporate Governance: Redirecting the European Agenda' (1997) 12 Economic Policy 91; B Cheffin, 'Corporate Law and Ownership Structure: A Darwinian Link?' (2002) 25 University of New South Wales Law Journal 346.

or the extent to which some functions are centralised in the parent entity – there are two key similarities that warrant comparative treatment for present purposes: the external decision making powers of a sole, or at least majority, shareholder, and a close economic incentive alignment. As regards the former, a central group (or holding) company will normally own all the shares in its subsidiaries, either directly or through a chain of other companies, thus being able to exercise close control over its boards. This is mirrored in the PE partnership's control, albeit usually via a sophisticated chain of SPVs headed by a Private Equity management company, of the portfolio company's board and senior executives. Subject to the temporal limitations of PE ownership over a three- to ten-year cycle, the economic incentive alignment is equally powerful in corporate groups and portfolio companies. Traditional shareholders suffer considerable agency cost losses due to their inability to act collectively.[167] As block- or single shareholder, the fund or central group company has direct control over an entity that shares its economic aims, and may therefore be able to generate substantial additional value from the underlying entity. Corporate Groups therefore share with Private Equity key features, such as the exercise of employer functions at multiple levels and close economic incentive alignment. As a result, examples can be drawn from both areas, with relevant links explained at the appropriate juncture in subsequent chapters.

SUB-SECTION 1: THE OPERATION OF PRIVATE EQUITY INVESTMENTS

The oft-reported picture of Private Equity value creation has not gone unchallenged. Froud and Williams, for example, argue that the returns achieved by PE firms are

[167] For analysis in the company law context see Kraakman et al, *The Anatomy of Corporate Law* (OUP 2009) 36.

based on the capture and extraction of existing value.[168] They argue that funds rely on financial engineering to rearrange 'ownership claims for value extraction, particularly for the benefit of the few who are positioned as private equity principals or senior managers in the operating businesses.' The legacy effect of this is said to be a 'cultural shift which normalises value capture insofar as it helps to institutionalise and normalise value extraction for the few as a practice and motivation for investors and managers within and beyond the Anglo-Saxon economies.'[169] A detailed engagement with these competing arguments is beyond the scope of the present work; the following paragraphs will nonetheless briefly survey the outlines of the Private Equity Industry in the United Kingdom.

It has been suggested that this has existed since the 1930s,[170] with the earliest leading institutions – the Industrial and Commercial Finance Corporation (ICFC) – founded in 1945.[171] Today, the majority of UK-based funds specialise in the buy-out market for mid-cap enterprises, comprising a substantial part of Mergers and Acquisitions activity.[172] The BVCA estimates that three million workers, the

[168] J Froud and K Williams, 'Private Equity and the Culture of Value Extraction' (2007) 12 New Political Economy 405.

[169] ibid 407. The authors suggest that his is not necessarily on the back of workers alone, but rather through financial engineering such as re-financings, where debt can be used to pay dividends to PE investors. This is reminiscent of the idea, that in hostile takeovers, value comes from shareholders' reneging on implicit contracts with stakeholders, with the resulting gains cast as redistributions from stakeholders to shareholders: A Shleifer and L Summers, 'Breach of Trust in Hostile Takeovers' (1987) NBER Working Paper No. 2342.

[170] A full historical overview is given in Myners (n 151) [12.22] – [12.34].

[171] Today the fund is known as 3i.

[172] Gilligan and Wright (n 148) 19-20.

equivalent of 21% of private sector employees, are employed in British companies that have PE backing.[173]

In the mid-2000s, the UK Private Equity industry, along with the rest of Europe (and indeed the world), enjoyed extremely benign economic and regulatory conditions, leading to record investments in 2006.[174] The demise of this rapidly maturing industry has been predicted by economic and academic commentators,[175] and current statistics do show a contraction of the Private Equity sector in line with the retreat of global financial markets: overall, BVCA members' investment in the United Kingdom fell from £12bn in 2007 to £8.2bn in 2008.[176] More recent figures for total global investment of UK-based firms show an even more drastic decline, from £20bn in 2008[177] to 4.6bn in 2009.[178]

By dealing exclusively with large, sophisticated investors, Private Equity funds are only subjected to a limited array of general financial markets regulation on both national and EU levels.[179] This is justified by the policy idea that major institutional investors are capable of bargaining for their own protection, and supported by very

[173] IE Consulting (n 6). This report was compiled on the basis of just over 1000 companies surveyed by IEC and the BVCA. By comparison, House of Commons Treasury Committee, *Interim Report on Private Equity* (10-I, 2006-07) puts the figure at 8% of the UK workforce being employed in Private Equity-owned companies.

[174] K Raade and C Dantas Machado, 'Recent Developments in the European Private Equity Markets' 319 European Commission Economic Papers 27.

[175] eg B Cheffins and J Armour, 'The Eclipse of Private Equity' (2008) 33 The Delaware Journal of Corporate Law 1.

[176] PriceWaterhouseCoopers, 'PE and VC Performance Measurement Survey' (BVCA 2008) 12.

[177] PriceWaterhouseCoopers, 'Private Equity and Venture Capital Report on Investment Activity 2008' (BVCA 2008).

[178] BVCA, 'February Briefing' (2010) 26.

[179] S Firth and O Watkins, 'The Regulatory Environment for Funds and Private Equity Houses' in M Soundy, T Spangler and A Hampton (eds), *A Practitioner's Guide to Private Equity* (City & Financial 2009).

few reports of investor problems in the PE industry.[180] The only recent exception to this hands-off regulatory stance are pension funds belonging to investee company employees.[181] Following a Pensions Regulator investigation in 2008, the PE house Duke Street Capital contributed £8m to the Focus DIY pension scheme, despite having sold the company on to another fund, Cerberus Capital, in the previous year.[182]

The Regulatory Context

Domestic Regulation is primarily self-imposed. *The Walker Guidelines* for increased industry transparency were published in November 2007. Their scope is reasonably limited,[183] covering less than 15% of the industry in the United Kingdom, given that reporting obligations only apply to investee companies if more than 50% of revenues stem from the UK, there are in excess of 1000 employees, and the enterprise value at acquisition exceeded £500m, or £300 in the case of P2P transactions. As regards substantive obligations, a first set lies directly with the portfolio company:[184] in a public annual report, it has to identify its PE shareholders, as well as their senior executives or advisers in the UK who have oversight of the company on behalf of the fund or funds. There must furthermore be disclosure on board composition, a business review along the lines of public companies,[185] and financial reviews that cover risk-management objectives. Investing funds are equally obliged to produce public

[180] Jenkinson (n 147) 136.

[181] G Brafman and J Wheeler, 'Due Diligence - Management / Employees' in M Soundy, T Spangler and A Hampton (eds), *A Practitioner's Guide to Private Equity* (City & Financial 2009) 158.

[182] Linklaters, 'Hot Topic: Duke Street Capital's £8m Pension "Hit"' (2008).

[183] ibid V3.

[184] ibid V4.

[185] Companies Act 2006, s 417.

reports,[186] describing their basic structure and investment approach, listing UK portfolio companies, management, and LP investors categorised by type and geography. Finally, all parties are to provide the BVCA with detailed data covering their financial and business activities,[187] and are subject to supervision by an external Monitoring Group.[188]

Responses to the Guidelines were critical, with Jack Dromey of Unite (T&G) voicing the fear that self-regulation was 'worse than useless'.[189] Other commentators questioned whether the benefits of limited additional disclosure would outweigh the costs of producing materials 'on average […] about as interesting as the glossy annual reports from public companies that are often assigned rapidly to the re-cycling bin.'[190]

On a European level, attacks on the industry were considerably more vehement, ranging from a critical report of the European Parliament[191] to more explicit attacks equating Private Equity firms with 'locusts'.[192] In 2009, the European Commission presented draft proposals for a Directive on Alternative Investment Fund Managers, aimed primarily at the regulation of 'significant systemic risk in financial markets'.[193]

[186] D Walker, 'Guidelines for Disclosure and Transparency in Private Equity' (2007) V 7.

[187] ibid V6 (portfolio company) and V9 (Private Equity firms).

[188] In early 2010, the WGMG made a recommendation to lower this threshold to £350m and £210m in case of P2P. The BVCA has accepted this recommendation, and will implement changes accordingly: BVCA, 'February Briefing' (n 226) 23.

[189] HC Treasury Committee (n 173) [76].

[190] Jenkinson (n 147) 137.

[191] P Rasmussen, 'Report of the European Parliament with Recommendations to the Commission on Hedge Funds and Private Equity' (A6-0338 2008).

[192] Anon, 'Locust, pocus – German Capitalism' (The Economist, 7 May 2005).

[193] Commission (EC), 'Proposal for a Directive of the European Parliament and of the Council on Alternative Investment Fund Managers and amending Directives 2004/39/EC and 2009/.../EC' COM(2009) 207 final ['AIFM Draft Directive'].

The Directive was finally adopted in late 2010 and published in the Official Journal on July 1, 2011.[194]

As regards PE funds' operational aspects, the major focus is on increased transparency and the prevention of asset stripping.[195] Chapter V, Section 2 of the Directive sets out new obligations for Alternative Investment Funds (AIFs) acquiring controlling influence in non-listed companies,[196] which is defined as holding more than 50% of voting rights,[197] even if as part of a club deal.[198] Funds must notify the acquisition of such control to the investee company and its shareholders,[199] and disclose the acquisition to a wider stakeholder group including to employees or their representatives via the investee's board.[200] Information on operational and financial developments must be included in firms' annual reports.[201] Article 30 of the Directive sets out a list of distribution requirements designed to avoid asset stripping within the first 24 months following the acquisition of control.

The directive's regulatory design is interesting, as certain obligations do not rest with individual investee companies but are to be born centrally by the PE management

[194] Directive (EU) 61/2011 of the European Parliament and of the Council on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 [2011] OJ L 174/1 ['AIFM Directive'].

[195] AIFM Directive, preambles (58), (89).

[196] ibid art 26–30.

[197] ibid art 26(5). This changed from 30% in the AIFM Draft Directive, art 26(1)(a).

[198] ibid art 26(5)(b).

[199] ibid art 27(1).

[200] ibid art 28(4).

[201] ibid art 29(2).

company.[202] The extent to which this approach addresses actual issues within the industry is, however, questionable. As Jenkinson notes, any 'push to increase transparency […] is likely to have a limited impact'.[203] The asset stripping provisions are equally unlikely to have a significant impact, as Private Equity income is increasingly structured via the repayment of debt, which, professional advisers suggest, is likely to fall outside the Directive's scope.[204]

SUB-SECTION 2: THE EMERGENCE OF MULTIPLE *LOCI* OF EMPLOYER FUNCTIONS

In order to demonstrate the distribution of employer functions amongst different entities inherent in the Private Equity business model, the present chapter turns to a detailed technical analysis of buy-out transactions. It introduces the key parties involved before focussing on the legal structures behind a buy-out transaction. This is the backdrop against which multiple employer function *loci* emerge, specifically through PE management companies' legal control rights and operational oversight.

Variations in the Private Equity Business Model

Two important caveats remain to be made: first, as to the range of issues under consideration, and second, as to the practical relevance and consistency of the specific model used. Private Equity investments have come to be analysed in various stages of a cycle spanning the life period of an investment from acquisition to divestment, yet the following discussion will be centred on the management of portfolio companies in between those points, including only those acquisition issues, such as company

[202] ibid art 29(1). It is however unclear to what extent this cross-portfolio view is a deliberate regulatory strategy: Interviews with Officials at DG Market (Brussels 23 March 2010).

[203] Jenkinson (n 147) Executive Summary, 139.

[204] Clifford Chance, 'AIFM Directive and Private Equity' (Client Briefing, January 2011) 1.

structuring and debt covenants, that continue to overshadow the operational phase. This focus means that a lot of other contentious issues related to the PE industry will not be scrutinised,[205] ranging from tax-transparent fund structures, leverage, and systemic risk to the incentives and remuneration of fund managers and their interaction with institutional investors such as major pension funds. This limitation is analytically justified: it is during the active management stage that the relationship with a Private Equity management company has its strongest impact on investee companies. As one of the leading business school casebooks puts it, 'interactions between PE investors and the entrepreneurs they finance […] are at the core of what PE investors do.'[206]

Finally, it is important never to forget the limitless variety within the Private Equity industry – both as regards the orientation of funds in general, and their specific structuring of individual transactions. As regards the former, PE transactions where only a minority stake in an enterprise is acquired, or where several funds share a single acquisition (so-called club deals), are examples of different approaches to essentially the same business model. The organisational chart below is drawn up on the basis of an existing fund; there are however no two funds exactly like one another. As structural differences are primarily driven by tax and securitisation considerations, such distinctions are of little relevance in the practical control aspects.

The use of financial jargon in the Private Equity industry can be bewildering,[207] and while most terms will be addressed as discussion evolves, three terms surrounding the concept of buy-outs warrant immediate explanation. The first of these is the LBO,

[205] Jenkinson (n 147) 128 ff.

[206] Gompers and Lerner (n 149) 7.

[207] Extensive explanatory lists can be found at <www.evca.eu/toolbox/glossary.aspx> accessed 1 September 2012; Gilligan and Wright (n 148) Glossary Section; Myners (n 151) 152.

or leveraged buy-out. In a leveraged (geared) transaction, a majority of the purchase price does not come from the fund itself, but is provided by banks in various forms of debt. Whilst not all PE transactions have to be leveraged, and levels of debt have indeed been falling recently, this is very much the norm in buy-out transactions today. Where a business, or part thereof, is acquired by the existing management team with the backing of external investors, reference is made to an MBO (management buy-out); if a new team of managers is brought in, the same transaction will be classified as an MBI (management buy-in).

Key Actors [208]

The most significant parties to a buy-out deal are equity capital providers, *viz* the limited partnership between fund managers (General Partners, or GPs) and investors (Limited Partners, or LPs); [209] debt capital providers, *viz* banks and the debt syndication markets; the acquisition fund and its associated special purpose vehicle (SPV) structure; and professional advisors including accountants and lawyers.[210]

The lifetime of the *Limited Partnership* is limited to a fixed duration of usually ten years.[211] Its key terms are set out in a partnership agreement concluded between the GP and LPs. The parties' obligations include the personal service of key GP

[208] Gilligan and Wright (n 148) 30 and T Spangler, 'Private Equity Fund Structures' in M Soundy, T Spangler and A Hampton (eds), *A Practitioner's Guide to Private Equity* (City & Financial 2009) 31ff.

[209] Technically speaking there are normally *several* limited partnerships in place, eg the GPs themselves are often organised as a Partnership, which in turn forms part of the Partnership with LPs.

[210] Financial Services Authority, *Private Equity: a Discussion of Risk and Regulatory Engagement* (Discussion Paper 06/6, 2006) [2.16] and [2.28] respectively.

[211] A reasonably long period in financial industry terms.

employees,[212] basic economic terms, such as fees and management remuneration (the 'carry'), indemnities and other limits on the GP in relation to investment activity in other funds. Other investment vehicles, such as direct investment [semi-]'captive funds' and investment trusts exist, but their market penetration is comparatively low.[213] A final investment variant are listed Private Equity trusts, with considerably lower minimum commitments – the price of a single share, and ready liquidity over the course of the investment cycle.[214]

A fund's *General Partner* is the legal entity representing the interests of the Private Equity house, with detailed management roles often devolved into a separate management company, which in turn also serves as the regulated entity.[215] GP remuneration is based on a 2/20 structure: two percent of assets under management are charged annually to cover fees and other expenses of the fund; this number has increasingly come under pressure as larger and larger funds are raised. Once an exited investment has exceeded a minimum rate of return (the so-called 'hurdle rate'), GPs receive 20% of any remaining profit as carry, taxed as capital gains.[216]

The *Limited Partners*, on the other hand, are usually large institutional investors[217] looking for long-term, illiquid assets for their investment portfolios.[218] A potential for somewhat ironic incentive structures has been noted in this connection where

[212] So-called 'key-man' provisions: Spangler (n 208) 44.

[213] Myners (n 151) [12.12]-[12.21].

[214] HgCapital Trust plc, *Annual Report and Accounts* (2009) 9.

[215] L Gullifer and J Payne, *Corporate Finance Law: Principles and Policy* (Hart 2011) 658.

[216] Memorandum of Understanding between the BVCA and Inland Revenue on the Income Tax Treatment of Venture Capital and Private Equity Limited Partnerships and Carried Interest (2003).

[217] Gilligan and Wright (n 148) 45. This is to limit investment to eligible counterparties. Sources of investment are discussed in detail by Myners (n 151) [12.64]-[12.75].

[218] Gompers and Lerner (n 149) 1.

workers' pension funds are at stake.[219] At fund closure, limited partners will commit considerable amounts of capital – minimum investments in excess of £10m are not unheard of – without however transferring any money other than advance fees. The bulk of invested sums are received only once the GPs issue draw-down notices in order to fund a specific investment.[220] In legal terms, LP liability for the partnership's actions is capped at the initially contributed amount.[221] However, it is interesting to note that this protection can be lost if an LP becomes too closely involved in the management of the partnership's investment,[222] for example through close monitoring or control.[223] A final source of equity is the direct investment expected of both PE principles and investee company senior management. The latter's 'hurt equity' is usually the equivalent of a year's salary, or 50% of the personal gains from a previous sale of the company. Considerably higher management stakes are equally possible.[224]

Banks provide the debt element in a purchase; before the 2008 crisis in bond markets, this often constituted 70% or more of the overall price.[225] A lead bank would syndicate the loan, packaged into a variety of collateral debt obligations (CDOs), amongst several financial institutions and hedge funds,[226] thus increasing overall amounts of liquidity. Debt financing is coupled with a host of obligations, going well

[219] Jenkinson (n 147) 126, quoting Phillip Jennings (UNI Global Union): 'Unions need to be aware that the money they are paying into pension funds is feeding the beast that may devour them.'

[220] Spangler (n 208) 37.

[221] Limited Partnership Act 1907, s 4(2).

[222] ibid s 6(1).

[223] Spangler (n 208) 33.

[224] E Rigby and A Felsted, 'Pessina to Boost Alliance Boots Skincare Brands' (Financial Times, 28 April 2010): CEO investment of £1.27bn in a £12.4bn deal.

[225] Froud and Williams (n 168) 407. The equity/debt ratio in an average UK FTSE company was the opposite.

[226] Gilligan and Wright (n 148) 54. Several PE firms have benefited from the financial crisis by repurchasing these loan packages at significant discounts from distressed debt funds.

beyond prioritised repayment: through so-called covenants, banks can closely monitor a portfolio company's ability to repay its debts.[227] Indeed, monitoring compliance with bank covenants quickly becomes a CEO's primary goal following a leveraged buyout.[228] If covenants are breached, the bank has several options, from renegotiating loan terms with the shareholder fund to stepping in and selling the remaining assets of the investee.

The interaction between these various groups is organised and supported by a large amount of *External Professional Advisors*.[229] Industry studies suggest that close to 15,400 service industry professionals are engaged in Private Equity-related activities in the United Kingdom.[230]

Fund Structure

The model Private Equity fund arrangement on the next page shows the operation of a variety of relationships between the parties identified above. Whilst developed on the basis of an existing fund, it has been modified both in order to maintain investor and investee anonymity, and to remove more complex arrangements relevant only for tax and debt securitisation purposes.

[227] ibid 88.

[228] Interview with former Investee Company CEO (Oxford 23 February 2010).

[229] Franklin (n 161) 26.

[230] AS Associates, 'The Impact of Private Equity as a UK Financial Service' (BVCA 2008) 7.

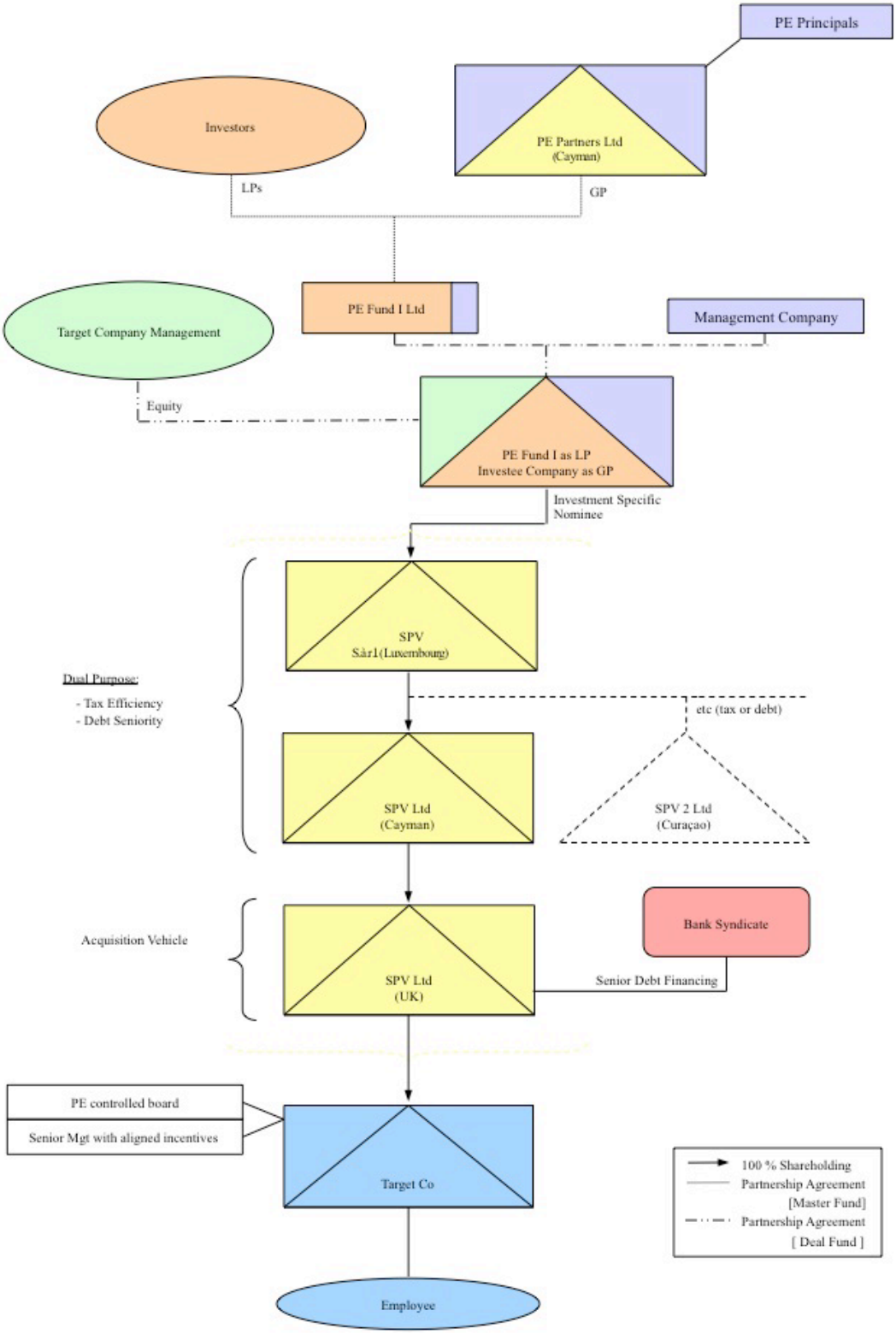
PE Principals
Investors
PE Partners Ltd
(Cayman)
LPs
GP
Target Company Management
PE Fund I Ltd
Management Company
Equity
PE Fund I as LP
Investee Company as GP
Investment Specific
Nominee
SPV
Sàr1(Luxembourg)
Dual Purpose:
- Tax Efficiency
- Debt Seniority
etc (tax or debt)
SPV Ltd
(Cayman)
SPV 2 Ltd
(Curaçao)
Acquisition Vehicle
Bank Syndicate
SPV Ltd
(UK)
Senior Debt Financing
PE controlled board
Senior Mgt with aligned incentives
Target Co
Employee
100 % Shareholding
Partnership Agreement
[Master Fund]
Partnership Agreement
[Deal Fund]

Figure 1 Fund Structure

The life cycle of a PE investment commences when the Limited and General Partners come together in a partnership that owns and controls the *Master Fund*, PE Fund I Ltd.[231] This fund then enters into further partnerships, specific to each investment project, with a management company and other investment-specific co-investors, most notably the target company's senior management team. PE Fund I Ltd and the co-investors are LPs in this partnership; with the management company taking on the GP's operational duties. Together they set up the *Deal Fund*, nominally controlled by an investment specific nominee. It is this entity which then sits on top of a long chain or web of Special Purpose Vehicles (SPVs).

These companies, sometimes also referred to as Alternative Investment Vehicles (AIVs) are created by the GP in order to give security to the holders of more junior debt and mezzanine facilities, and structure the transaction as tax efficiently as possible.[232] Shareholdings across multiple jurisdictions, and cross-holdings amongst different SPVs are common. Control over each entity is exercised through majority shareholding, usually as a single member. Offshore trust companies in the relevant jurisdictions will provide the necessary board facilities; in most cases (again dictated primarily by tax considerations), an employee of the PE management company is also represented on the SPV board.

At the end of this arrangement sits the Acquisition Special Purpose Vehicle (ASPV). Usually incorporated in the target company's jurisdiction, its purpose is the acquisition of a controlling (or exclusive) stake in the enterprise.[233] The consideration for this is raised from two sources – the deal fund (via the various SPVs), and public

[231] The numbering of Funds traditionally refers to previous successful ventures by the GPs.

[232] This is a power explicitly laid down in the Master Fund Partnership Agreement.

[233] Gilligan and Wright (n 148) 76.

debt markets (via the syndicate leader bank). In the ASPV, all streams of funds are united for the first time: neither the fund nor the partnerships take on any debt directly.

Management Control

Two aspects of management control will be discussed in the remainder of this sub-section: its legal organisation through the company's constituent documents, and the various tools for its practical exercise. It is in this context that the specific examples to be explored are set, thus illustrating the serious challenges posed by the Private Equity model to the common law's traditional notion of the employer: a second entity exercises employer functions, up to and including control over the supposedly singular counterparty to the contract of employment itself.

Management control is the unique selling point of the Private Equity industry: in order to ensure the success of their investments, GPs must carefully work with and oversee entrepreneurs and portfolio companies.[234] There is some disagreement about this hypothesis – some argue that profits were driven for a long time by leverage and multiple growth, with operational improvements becoming more and more important only in the 21st century,[235] while other commentators place the shift from a 'hands-off, eyes-on' approach to an involved management style and sector specialisation as early as the 1980s.[236] Today, there is a clear consensus that even funds that traditionally specialised in the financial aspects of buy-out deals are taking a strong interest in management control. In fact, nearly all funds surveyed employ a dedicated team of

[234] Gompers and Lerner (n 149) 70.

[235] Interview with Partner in City Law PE practice (London 10 March 2010).

[236] Gilligan and Wright (n 148) 17.

professional managers and consultants, or are in the process of setting up specific portfolio interaction teams.

From a legal perspective, the relationship between investors and senior company management is regulated by the investee company's constituent documents; specifically the investment or shareholders' agreement, and the company's articles. In the Private Equity context, there will usually be extensive management undertakings given to both the investee company and the PE management company; these are analytically distinct from the company's key documents and will accordingly be discussed as illustrative examples in the next chapter. The investment or shareholders' agreement sets out key terms of the subscription arrangement, followed most importantly by governance details. These include the structure of the company board and its various sub-committees (eg for remuneration, risk, and compliance), and the procedures for replacing directors and the appointment of additional ones. A detailed schedule attached to the agreement will specify key decisions which cannot be taken without the formal approval of the Private Equity management company, give ample information rights to investors, and list a series of warranties and restrictive covenants given by the management team. The company's articles, on the other hand, focus on the target's capital structure and various classes of equity and debt. It is nevertheless an important control tool due to the share transfer rules laid down in it: management can be forced to exit an investment at any moment chosen by the investors (drag-along provisions), may loose its investment (bad leaver clauses) or gain additional equity stakes at the fund's discretion (ratchet).

Legally speaking, the portfolio company board is therefore a major location for the exercise of investor control. In addition to a public company board's normal function as decision-making and strategy-setting authority, boards in Private Equity backed

enterprises become one of the major interfaces between investors and management.[237] Executive directors are supplemented by PE-appointed non-executives in order to represent investor interests: whilst this might be legally different from reporting lines in group-subsidiaries, for example, it is not far off in practice: [the alternative governance arrangement] 'does not mean that the [management] team does not have a 'boss' […] ultimately, the investor will have the authority to make major changes in the interests of shareholders or the company as a whole.'[238] In practice, Private Equity funds and their board representatives deploy a series of specific governance tools at board level and beyond, four of which will now be examined more closely.[239]

Board Setup

As a first step, a PE management company will normally 'consider carefully the composition of the [investee company] board, and the ability to control it'. This specifically refers to using the appointment and removal of directors 'in the event of a disagreement with the executives and other non-executive directors'.[240]

Information Access

This is regulated both through formal arrangements and management practice. As regards the former, both the shareholders' agreement and loan covenants will set out a series of reporting requirements (cash-flow statements, balance sheets, executive reports) due at regular intervals anywhere between daily and monthly set points and

[237] G Sharp, *Buyouts: A Guide for the Management Team* (Montagu Private Equity 2009) 102.

[238] ibid 104.

[239] A Hampton, 'Corporate Governance / Risk Management' in M Soundy, T Spangler and A Hampton (eds), *A Practitioner's Guide to Private Equity* (City & Financial 2009), on which the following paragraphs draw for basic structure.

[240] ibid 331.

when certain key events arise. Informal arrangements, however, are considerably more important: 'directors appointed by a PE house will spend a significant amount of time with the company and its managers, discussing strategy and performance issues.' [241] This is further supported by 'a steady flow of e-mail and telephone exchanges',[242] allowing analyst teams within the investing fund constantly to monitor each investment.

Veto Rights

It has already been noted that the shareholders' agreement will normally include a schedule setting out an extensive list of issues on which the board of directors, or sometimes even the Private Equity management company itself, must be consulted by the management team and consent before a proposed course of action can be taken. Examples of such events range from material business plan changes and major financial decisions, including new loans, the payment of dividends, or a change of accounting policies to the hiring of individuals paid more than a certain amount.[243] A liability risk can arise from these veto rights, however, as a PE management company could conceivably be found to have become a shadow director of the investee company – an especially challenging issue in the insolvency context, where conflicting interests between shareholders and other stakeholders crystallise.[244] Under section 251 of the Companies Act 2006, an individual or entity can acquire this status if they become a 'person' in accordance with whose instructions the directors of [the

[241] ibid 332.

[242] Sharp (n 237) 104.

[243] £50,000 seems to be the most frequent threshold.

[244] D McCahill and S Willcock, 'Restructuring Issues for Private Equity Houses' in M Soundy, T Spangler and A Hampton (eds), *A Practitioner's Guide to Private Equity* (City & Financial 2009) 397.

portfolio] company are accustomed to act. Sophisticated PE management companies therefore make sure that the veto schedule is kept to exceptional items only, and that any other guidance is phrased as advice, which 'the directors are free to consider […] and adopt […] or alter […] as they think best for the company.'[245]

Direct Interventions

A combination of the above factors enables Private Equity investors to spot potential issues arising in investee companies early on, and provides them with a full range of powerful remedies, from giving general advice and challenging particular decisions to a complete renewal of the management team. It is important to remember that interaction goes well beyond formal board sessions or sporadic meetings: there is a strong culture of 'regular [investor representative] attendance at ad hoc meetings to address specific issues'.[246]

In summary, management are certainly not left alone in their core tasks following the buy-out, be it an increase in post-tax profits by upping gross margins, volumes and sales or by reducing overheads.[247] Academic studies have found a very high level of investor interaction with executives through active boards and beyond. Whilst specific details might vary between different funds or even investment teams,[248] the overall difference from traditional models is striking: an intense leadership of management strategy leads to a focus on value creation rather than more general compliance and

[245] Hampton (n 239) 334.

[246] Sharp (n 237) 104.

[247] Gilligan and Wright (n 148) 83.

[248] F Cornelli and O Karakas, 'Private Equity and Corporate Governance: Do LBOs Have More Effective Boards?' in J Lerner and A Gurung (eds), *The Global Impact of Private Equity Report 2008* (World Economic Forum 2008) for example find that as a PE fund becomes more experienced, its post-LBO board size decreases significantly.

risk management issues.[249] Whereas executives in public companies act more or less autonomously, Private Equity shareholders wield 'significant influence over aspects of the running of the business such as budget approvals, capital investment decision and management appointments; […] such control [being] one of the defining elements of PE ownership.'[250] Indeed, economic analyses[251] show that performance change in investee companies results not only from additional financial constraints imposed by high debt levels,[252] but from economically more effective management,[253] and increased reliance on control systems that help the buy-out team to meet business plan targets and stay within financial covenants.[254] Global studies show overall efficiency improvement in management,[255] especially where PE funds specialise in the relevant industry.[256] Ian Clark has presented two sets of findings at the firm level that could explain this increased economic efficiency: considerably less managerial discretion once executives' decisions are driven by quantifiable measures such as improved

[249] V Archarya, C Kehoe and M Reyner, 'Private Equity vs PLC Boards: A Comparison of Practices and Effectiveness' (2009) 21 Journal of Applied Corporate Finance 45.

[250] Franklin (n 161) 25.

[251] See Gilligan and Wright (n 148) Appendix Table 11 and 12 for a full overview of studies.

[252] J Franks and C Mayer, 'Governance as a Source of Managerial Discipline' (2002) National Bank of Belgium Working Paper 31, 2.

[253] S Green, 'The Impact of Ownership and Capital Structure on Managerial Motivation and Strategy in Management Buy-Outs: A Cultural Analysis' (1992) 29 Journal of Management Studies 513.

[254] C Jones, 'Accounting and Organizational Change: An Empirical Study of Management Buy-Outs' (1992) 17 Accounting, Organizations and Society 151.

[255] N Bloom, J van Reenen and R Sadun, 'Do Private Equity-Owned Firms Have Better Management Practices?' in J Lerner and A Gurung (eds), *The Global Impact of Private Equity Report 2008* (World Economic Forum 2008).

[256] R Cressy, F Munari and A Malipiero, 'Creative Destruction? Evidence that Buyouts Shed Jobs to Raise Returns' (2011) 13 Venture Capital: An International Journal of Entrepreneurial Finance 1.

cash-flows or reduced head counts, and the 'more overtly aggressive management of Human Resources'.[257]

SUB-SECTION 3: THE SHARED EXERCISE OF EMPLOYER FUNCTIONS

Having thus seen the emergence of a second *locus* of managerial control, especially as regards traditional employer functions, in the specific context of Private Equity-led leveraged buy-outs, discussion now returns to the inherent tension identified in the conclusion to the first chapter: what if various employer functions are no longer exercised by a single entity? To illustrate this tension in the present context, the final sub-section will draw on a range of case studies from London-based PE houses. The emerging picture – of employer functions shared between different entities, parcelled out to various parties, or exercised jointly in a host of different ways – confirms the observation that different facets of the notion of the employer, whilst not problematic in the unitary paradigm of single employer cases, may stand directly opposed to each other in scenarios where control is exercised by more than one entity.

The Case Studies

In order to demonstrate the division of traditional employer functions in practice, it is necessary to identify various *loci* of control, and then look in detail at their interaction. The first of these tasks is relatively straightforward in the Private Equity setting: following a buy-out, a fund management team representing investor interests joins the investee company management in directing the portfolio enterprise. The second step, on the other hand, is rather more challenging: there is little, if any, detailed qualitative research on the actual modes of interaction between funds and their investee companies. Aggregate data is of limited use, as each fund deploys different strategies,

[257] Clark (n 155) 2044.

sometimes even varying them as between different investments. Finally, even practical analyses in practitioners' handbooks focus more or less exclusively on the technicalities of *legal* mechanisms of control in company law. This perspective ignores the majority of less formal interactions between the two *loci* of control, which are crucial in illustrating the day-to-day division of employer functions.

In order to obtain the relevant information, therefore, several case studies were conducted amongst London-based Private Equity funds.[258] In a series of semi-structured interviews, participants were asked first to explain the basic financial and legal structure of their fund, before focussing on the list of employer functions identified in the first part. In this context, interviewees identified how various functions were exercised in practice. Relying on illustrations from current or recently divested investments, this function-by-function analysis explored the roles and incentives of the various participants in the two *loci* of control.

In order to obtain as accurate a picture as possible, at least one interviewee was chosen from each group of key parties in a typical Private Equity transaction: investors, PE funds, portfolio company management, legal advisers, and investment banks. Different funds were chosen to reflect the breadth of the industry, both in terms of investment vehicle choice (limited partnerships and public investment trust funds) and management strategy (strong focus on operational improvements versus a more traditional hands-off approach based on financial engineering skills). The 'private' aspect of the Private Equity industry was felt insofar as it was reasonably challenging to identify individuals willing to provide information. All interviewees insisted on strict anonymity, and none of the funds or investee companies will be identified in the

[258] This initial fieldwork was approved by the Social Sciences and Humanities Inter-Divisional Research Ethics Committee (IDREC) on January 20, 2010: SSD/CUREC1/10-285.

discussion, below.[259] Whilst the overall sample size therefore had to remain reasonably small, especially when considering the variety of structures and strategies within the industry, the examples below are nonetheless highly useful in illustrating the key argument put forward in this thesis: tensions inherent in different aspects of the traditional notion of the employing entity come to the fore as soon as various employer functions are exercised from more than one *locus* of control.

(1) Inception and Termination of the Contract of Employment

The first employer function was summarised earlier in functional terms as all aspects of power over the very existence of an employment relationship under a contract of service. There are four areas where this function is exercised in practice: actions before an actual contract is concluded, such as the advertisement of a post, selection of potential candidates and negotiations over their terms of employment; the actual hiring; powers of suspension and over disciplinary procedures more generally; and the termination of employment relationships. In the PE context, all of these functions are shared between the investee company management and its financial backers. The various case studies on this first function show the full variety of different modes of interaction between the two *loci* of control – from direct contractual arrangements and formal voting on the company board to investor veto rights and more informal discussions.

As regards actions even before an actual contract is concluded, several PE management companies maintain rosters of executives specialising on specific management tasks, from divisional restructuring to supply chain reorganisation. If a portfolio company decides to hire employees in any of these fields, the fund will

[259] Full interview notes, including names and fund information for all interviews, and samples of contractual documents have been deposited with the supervisor of this thesis in accordance with IDREC-notified procedures. No market-sensitive data was collected.

'assist' its efforts by selecting an executive from its database, or sometimes even propose one of its own senior partners as an appropriate (temporary) manager.[260] These candidates will normally be interviewed and selected directly by the PE management company team, who are also often tasked with negotiating further particulars of employment. Other funds maintain a much smaller stock of experienced executives, but nevertheless retain the power to direct the investee company's hiring choices.[261] The actual conclusion of employment contracts with lower-tier employees is usually left to the portfolio company itself. It is not unusual however to see explicit veto provisions reserved for the Private Equity management company: one common provision demands explicit fund approval for new employment contracts where the total value of annual remuneration and additional benefits exceeds £50,000.[262]

Whereas general Human Resource management in solvent companies is left to portfolio company executives on a day-to-day basis,[263] the PE investors usually retain powers of suspension and related disciplinary procedures for more senior employees through two distinct routes: executive directors can always be ousted by shareholder representatives' votes on the company board. Second, there are contracts concluded directly between individual senior employees and the PE management company. In consideration for participatory drawing rights in the carry vehicle,[264] these agreements subject employees to both general underperformance clauses and more specific disciplinary procedures run by the Private Equity management company. The latter

[260] Telephone Interview with Senior PE Operations Executive (15 February 2010).

[261] Interview with PE Business Development Partner (London 19 February 2010).

[262] Interview with PE Partner (London 10 March 2010).

[263] Interview with former Investee Company CEO (Oxford 23 February 2010).

[264] And ratchet provisions (management equity increase triggers when performance targets are met).

can extend as far as an individual's personal behaviour, such as an obligation to report even minor traffic offences.[265]

The right to terminate employment relationships is equally shared between both *loci* of control. Portfolio company management and investing funds can usually initiate redundancies, albeit through different processes. The former will retain the formal power to terminate most employment contracts, subject to key personnel clauses. Nonetheless, even minor terminations are usually discussed in informal phone calls between the PE operations team and the company's Chief Executive Officer (CEO) or Head of Human Resources.[266] If analysts within the Private Equity management company have identified potential redundancies, the next steps will depend on the fund's investment strategy: while some firms only initiate 'general conceptual discussions' with management,[267] others will provide detailed instructions on where and how changes to the workforce are to take place.[268] Investee company executives are fully aware that in the case of disagreement with PE investors, their contracts can be terminated more or less immediately.[269] Some funds regularly invoke the underperformance clause set out above to this end, containing potential employment law litigation through compromise undertakings given in return for the retention of small equity stakes in the investment.[270]

[265] Interview with former Investee Company CEO (Oxford 23 February 2010).

[266] Interview with former Investee Company CEO (Oxford 23 February 2010).

[267] Telephone Interview with Senior PE Operations Executive (15 February 2010).

[268] Interview with PE Partner (London 10 March 2010).

[269] Interview with former Investee Company CEO (Oxford 23 February 2010).

[270] Interview with PE Partner (London 10 March 2010).

(2) Receiving Labour and its Fruits

The essential element underlying both aspects of this second function of the employer was identified earlier as the employer's ability to demand, and if so receive, the workforce's personal labour. In the vast majority of cases, this function will be exercised exclusively by the portfolio company itself: there is little scope for Private Equity investors' involvement in the actual day-to-day execution of work processes, as even traditional factory visits are an increasingly rare sight.[271] The right to receive any goods and materials resulting from the work processes was noted to include incidental benefits, such as intellectual property rights. In practice, however, it appears again that fund managers are in most cases content to leave such issues to the investee company.[272]

Two exceptions to this general observation should be noted: first, the direct contracts between senior management and Private Equity managements companies, as already discussed in the first function. Through these arrangements, the investors are arguably entitled to demand and directly receive a considerable share of management employees' labour: regular reporting, both through formal documents and informal meetings and phone conversations, on cash-flows, covenant stress-testing, and divisional performance are a key part of executives' work, and have to be delivered directly to the relevant analyst teams within the management company.[273] A second area where Private Equity investors can sometimes get involved in the receipt of labour and its fruits is in troubleshooting operations for specific sections of the business. An example of this is the collection of receivables, particularly in overseas operations, where funds might rely on direct involvement to ensure that materials or

[271] Interview with PE Business Development Partner (London 19 February 2010).

[272] Interview with former Investee Company CEO (Oxford 23 February 2010).

[273] Interview with PE Business Development Partner (London 19 February 2010).

services provided to customers are turned into stable incoming cashflows within a reasonable timeframe. [274]

(3) Providing Work and Pay

This third category is underpinned in functional terms by the work-taking party's reciprocal obligations to those of wage-takers in category (2). The provision of regular work is usually parcelled out to the investee company – with the exception of senior management contracts just discussed. In general, the Private Equity managers do not consider it their duty to provide work to employees. This becomes particularly evident when portfolio companies are on the brink of bankruptcy: whilst holding discussions on business strategy and employment level changes, or at least a sale as a going concern to a trade buyer or another Private Equity fund, to ensure the future viability of the enterprise some funds will simultaneously retain professional advisors to prepare the winding down of the company.[275]

When it comes to the payment of wages, expenses and other allowances, on the other hand, both company and PE *loci* of control will normally be involved, be it directly or indirectly. On one end of the spectrum there is the direct payment of regular wages by the Private Equity management company, usually for key employees of the portfolio company (on top of any eventual proceeds from the sale of equity stakes).[276] Most funds, however, avoid such direct links: operational partners have formally to relinquish their partnership in the investment vehicle before taking up executive management roles within the investee enterprise, the latter also agreeing to

[274] Interview with former Investee Company CEO (Oxford 23 February 2010).

[275] Interview with Investment Banking Associate (London 10 March 2010).

[276] Interview with PE Business Development Partner (London 19 February 2010).

pay the partner's wages and expenses during that period.[277] When it comes to the payment of external non-executive directors that represent the interests of the PE fund and its mangement company on the company board, there is a fairly even split between remuneration coming from the portfolio company and the funds. One regularly used technique to avoid direct cashflows between the Private Equity management company and its appointees is the payment of monitoring fees in the range of £15,000 to £50,000 from company funds.[278]

A final control tool over payment of wages is the board subcommittee on compensation. Several Private Equity management companies staff this entity exclusively with its analysts or their representatives, preferably the 'toughest guys around'.[279] By setting the criteria along the lines of which management and sometimes even employees at large are evaluated, and deciding on the corresponding levels of pay and other benefits, the fund here exercises a crucial employer function, regardless of the actual accounts linked to payroll. Any discretionary bonuses management want to award as incentives to more junior employees will equally have to be considered and approved by the Private Equity management company, acting through the compensation committee.

(4) Managing the Enterprise-Internal Market

It will be recalled from the discussion in chapter one that this function is central to the role of the entrepreneur-coordinator: only through the constant use of the directional powers founded on the employees' contractual obligations can management achieve the necessary control over all factors of production. The functional notion

[277] Telephone Interview with Senior PE Operations Executive (15 February 2010).

[278] Interview with Partner in City Law PE practice (London 10 March 2010).

[279] Telephone Interview with Senior PE Operations Executive (15 February 2010).

underpinning this category is an open-ended right to direct employees, regardless of the actual level of detail of that instruction. As set out earlier, the idea at the very core of the Private Equity business model is that as single majority shareholder, funds can seize control over their investment companies *in addition* to the existing management. Control over the enterprise-internal market is not shared in the sense expounded, for example, in the first function. Rather, the same sets of functions are in fact exercised at different levels in the PE context: the investing fund will traditionally focus on business plans and development, leaving more detailed execution to the company's executives. The precise levels of this stratification vary dramatically from fund to fund, and can in some instances even be inverted.

In nearly all investment agreements there is a clear list that sets out which strategic matters can only be initiated and in some cases even executed by the PE firm. This will cover decisions on senior management, group structures and financing, from repayment priorities to additional loans.[280] Changes to the overall business plan, or any significant acquisitions or disposals of individual business units will equally be within the exclusive domain of the management company.[281] Depending on the latter's internal operations team, the target company's management may be tasked with drawing up detailed action plans: in one case, the fund simply provided executives with target employment figures 30% below the existing level, and then approved management's suggestions as to how this should be achieved. Whilst strategic change is often addressed at formal board meetings there are other, more opaque, methods of communication between the two *loci* of control: the investors can, for example, request mere attendance rights at board meetings, with the minutes clearly reflecting that all decisions were made by the executive directors alone. In

[280] Interview with PE Partner (London 10 March 2010).

[281] Interview with Partner in City Law PE practice (London 10 March 2010).

other scenarios, particularly when it comes to reductions in employment levels, information is conveyed as informally as possible, from telephone calls to lunch conversations.[282]

Other funds take an even more active approach to managing the enterprise-internal market. The employment of operating partners as senior management has already been discussed; another frequently used technique is a direct secondment of junior analysts at all levels of the target company,[283] for example as chief of staff to key executives, in order to get 'very close to the operations' and deliver the strategic changes decided by the fund.[284] For large funds, this can involve up to thirty of its employees acting as 'consultants' within a recently acquired business.[285] More regularly occurring management functions, such as ensuring that health and safety controls are in place and dealing with vicarious liability claims following accidents or deaths at work in hazardous environments will often be delegated to the investee company despite board information and approval requirements.[286]

(5) Managing the Enterprise-External Market

The final function of the employer that emerged in the first part of this work was engagement with markets at large. Put differently, it is a key function of being an employer to enjoy the chance of financial profit and carry the risk of loss from investing in ventures undertaken by the enterprise. At a first glance, it might be assumed that it is on the investee company's account, and on this account alone, that

[282] Interview with PE Partner (London 10 March 2010).

[283] Interview with PE fund General Counsel (London 11 March 2010).

[284] Telephone Interview with Senior PE Operations Executive (15 February 2010)

[285] Interview with Partner in City Law PE practice (London 10 March 2010).

[286] Interview with former Investee Company CEO (Oxford 23 February 2010).

all business activities take place. This is true insofar as – subject to what has just been said about the division of management functions in the enterprise-internal market – it is the company which has to sell its products and services on the open market. The key element, however, was investment in projects and facilities, as seen historically in the provision of tools and equipment. In the Private Equity context it is the investing fund that provides, or arranges for the external provision via debt markets, of all such investments through downstream cashflows, and enjoys the financial gains from upstream payments, or the risk of financial loss if the investee company is not profitable enough. The following paragraphs take a closer look at these cashflows, building on the fictional fund structure set out above.

Financial movements take place in two directions within that investment structure: investments move downstream initially, when cash flows from the master fund via the deal fund and its SPVs into the acquisition vehicle, and from there onwards to the target company vendors and the portfolio enterprise itself. During and at the end of the investment cycle, money moves back upstream, when the investee company's cash flow is distributed along similar pathways. Downstream financing is initiated by the General Partner's capital calls under the terms of the original Master Fund partnership agreement. The GP will then set up the Deal Fund (including the nominee company and subordinated entities) and start diffusing capital into the structure. In return, each SPV issues a mix of equity (shares), debt (especially in the form of loan notes) and hybrid securities. Only a relatively small part of the fund's investment is in the form of equity, however, as its amount is limited by the proportion of management investment. The majority of funds will therefore be structured as loans,[287] with tiered repayment priorities during the course of the investment. Once subordinated debt providers have injected their share of investment the fund will arrange for the

[287] Gullifer and Payne (n 215) 665.

syndicate leader bank to transfer the most senior loan tranches directly to the acquisition vehicle, securing its interest on the target company's assets.[288] Using these funds, the Private-Equity controlled ASPV then acquires shares in the target company.

Upstream cash flows commence as soon the investee company's balance sheet meets or exceeds local dividend payment (DR) requirements. The board declares a dividend on the company's shares, which are duly paid to its sole shareholder, the ASPV, in order for it to meet its financing obligations to debt holders (banks) and loan note bearers (the PE fund). Capital is then moved up through the structure as various SPVs declare dividends, repay their debts, and redeem various hybrid securities. Once profit targets in the partnership agreement are met, 20% of profits are paid out to the GP's carry vehicle, with the remainder distributed proportionally amongst LPs. A similar process, albeit on a much larger scale, takes place at investment exit: the ASPV sells its shares in the investee company, repays any outstanding debts, and returns the remaining investment and profits to the master fund.

The final employment function, risk of loss and chance of gain associated with the equity investment, is therefore more or less exclusively parcelled out to the investing fund: even as regards engagement with the market, it will usually be the fund managers rather than portfolio company executives who negotiate loans and restructure the company's debts when covenants have been breached.[289] The portfolio company will not normally reinvest any of its positive cashflows in the business, declaring dividends and repaying existing debts instead. Any expansion or additional investment will usually be funded through drawdowns from new or existing lines of credit.

[288] The precise timing of this depends on the target jurisdiction's financial assistance laws.

[289] Interviews with Partner in City Law PE practice and Investment Banking Associate (London 10 March 2010).

CONCLUSION

Chapter one of this thesis suggested that the notion of the employer in English employment law suffers from an inherent tension. The traditional unitary vision of the employer as a singular entity is firmly built on historical language and fact patterns, reinforced by contractual doctrines of bilateral relationships and, in the context of corporate employers, in line with economic theory as embodied in company law. Upon closer inspection, however, this orthodoxy is challenged by the fact that all tests traditionally used to determine the status of dependent workers, other than the enterprise integration test, do not command a unitary vision of the employer as a matter of logical necessity. Moreover, this orthodoxy is further challenged by the multi-functional approach prevalent in the case law. In concluding it was suggested that the resulting tension might not be an issue in single employer scenarios where all functions are exercised by one party; but that the notion could face serious challenges in situations beyond this narrow paradigm.

Chapter two then turned to two such scenarios that are particularly challenging to the unitary element in the traditional notion of the employer: Temporary Work Agencies, and Private Equity portfolio companies. Following a brief introduction to each industry, discussion focussed on two major aspects – how additional entities emerge as a second *locus* of control; and how this in turn leads to a joint exercise of nearly all of the employer functions identified in chapter one.

These arrangements bring the contradictions inherent in the notion of the employing entity to the fore: the assumption that only a single entity, the counterparty to the contract of employment, can exercise employer functions is incongruent with their continuous joint exercise by two *loci* of control in the contexts surveyed. It is to the practical implications of this tension for employment law coverage to which the second part of this thesis now turns.

PART II
THE IMPLICATIONS OF A NOTION UNDER PRESSURE

The first part of this thesis identified a deep tension inherent in the notion of the employer in English law: it is a multi-functional, yet unitary concept. It then demonstrated that the resulting conflict between the two strands is brought to the fore in situations beyond a narrow single-entity employer paradigm, with triangular work relationships and Private Equity controlled firms providing notable examples of situations where multiple entities exercise employer functions. The goal of the third and final part will be to respond to this problem, addressing the issue through a reconceptualisation of the notion of the employer.

Introduction

Before this task can be attempted, however, several intermediary steps have to be taken in order to explore the implications of the notion under the pressure. This is the dual purpose of the second part: to illustrate practical instances of the tension, and to collect evidence for the eventual construction of a reworked notion of the employer. In doing so, the chapters to follow form a logical link between parts one and three.

Evidence that the identified tension is not merely an abstract theoretical problem, but one of the key causes of an on-going crisis in Labour law's fundamental concepts,[1] will support the claim that the problems identified are grave enough to warrant a reconsideration of the employer notion. The various examples explored in

[1] A term coined in K Wedderburn, R Lewis and J Clark (eds), *Labour Law and Industrial Relations: Building on Kahn-Freund* (Clarendon Press 1983) vi.

order to advance this argument will furthermore form the initial elements of a framework in which this reconceptualisation is to take place. The previous part extensively trailed through case law and academic material in search of different aspects of the functioning of the employer, operating on the assumption that it was in difficult borderline scenarios that the notion could best be teased out; this exercise is now, in a certain sense, to be repeated at a different level in order to prepare an investigation of the broader function or purpose of the employer.

Defining the Relevant Case Law

Having thus set out the main aim of part two, two preliminary points remain to be made: explaining the subsequent discussion's move onto a broader plain in order to be able to look at the issue from multiple angles in different contexts, and elaborating on how this seemingly fragmented effort is nonetheless driving at a single notion of the employer. As regards the former point, there is a crucial dimension in which the material analysed moves beyond the thesis' general focus on multi-entity employment in English law, in which discussion has taken place thus far, by turning to a comparative excursion into German law.

This comparative analysis will be particularly fruitful due to that legal system's long-standing tradition of regulating block shareholdings and complex cross-holdings in corporate structures. Home to one of the largest European Private Equity industries outside the United Kingdom,[2] research in Germany has also allowed for the collection of illustrative fieldwork material where necessary. [3] German company and employment law have developed a series of legal mechanisms to address the

[2] Chris Hale and Emma Watford, BCL Seminar (Oxford, 7 February 2012).

[3] Approved by the Social Sciences and Humanities Inter-Divisional Research Ethics Committee (IDREC) on December 21, 2010: SSD/CUREC1/10-451.

challenges arising from multiple *loci* of control over subsidiary undertakings, for example, as regards the protection of different stakeholders in the subordinated entity; up to and including specific mechanisms for the protection of employees other than as wage creditors.

Two particular sets of employees will be generally excluded from further consideration: employees of Private Equity partnerships such as financial analysts or management advisors, and senior management at investee companies. As regards the former group, litigation has been brought directly against the management company for a wide range of issues, for example, to settle questions as to a redundant analyst's entitlement to a profit share in the carry vehicle.[4] From an analytical perspective such cases fall outside the current framework, however, as there is no tension in the traditional notion where the Private Equity fund exercises all employer functions in regard of the claimant. The litigation options of senior management at investee companies, on the other hand, are usually limited by contractual agreements and economic incentives. In the case of dismissal, for example, executives' primary motivation is to bargain with the management company to retain at least a small portion of their equity entitlements in consideration of comprehensive compromise and non-disclosure agreements.[5]

A Single Notion of the Employer

The second preliminary point to be discussed concerns the development of a single notion of the employer through an analysis of different contexts. Given the wide range of sources to be analysed, it might be thought that at least two analytical

4 *Aymard v SISU Capital Ltd* [2009] EWHC 3214 (QB).

5 Furthermore, it might even be open to question whether senior management could be considered as being partners in the original fund: *Tiffin v Lester Aldridge LLP* [2012] EWCA Civ 35, [2012] IRLR 391.

juxtapositions arise: the notion of the employer at common law, as opposed to that in statute, and a domestic concept differing from one developed in the case law of the European Court of Justice and other Union-level legal developments. This is not the case, however. None of the above categories are watertight compartments with distinct notions of the employer. While such developments have been called for in other areas such as Tort[6] or Intellectual Property law,[7] the notion of the employer is implicitly assumed to be identical across all areas covered in the following chapters.

This may be so in part because the apparently separate domains of statute and common law at domestic and European levels are in reality in constant interaction with each other, mutually shaping a unified notion of the employing entity. They are closely linked infra- and superstructures, each adding particular aspects to the overall notion. At points, this linkage becomes very explicit, with amalgamations both in substance and in a jurisdictional sense.[8] Statutory legislation will normally rely directly on common law concepts such as the contract of employment in defining key terms such as employee and employer,[9] and the existence of statutory legislation will in turn influence the development of the common law.[10] As regards the relationship between common law and statute, it is therefore 'increasingly difficult to view [the two domains] as separate streams whose waters "do not mingle"'.[11]

6 E McKendrick, 'Vicarious Liability and Independent Contractors: A Re-Examination' (1990) 53 MLR 770.

7 J Pila, '"Sewing the Fly Buttons on the Statute": Employee Inventions and the Employment Context' (2012) 32 OJLS 265.

8 M Freedland, *The Personal Employment Contract* (OUP 2003) 3.

9 Employment Rights Act (ERA) 1996, s 230.

10 See, most notably, L Hoffman in *Johnson v Unisys Ltd* [2001] UKHL 13, [2001] 1 AC 518.

11 S Deakin and G Morris, *Labour Law* (6th edn Hart 2012) 138.

The relationship between domestic and European law operates along similar lines, both in employment law generally and as regards the specific notion of the employer. Concepts of European Union law are to be uniformly applied by all member state courts under principles of EU constitutional law.[12] Their precise nature, however, is frequently shaped by practices in the member states. The Acquired Rights Directive[13] to be discussed in section two serves as an illustration of this approach: key concepts are defined in direct reference to domestic law. The meaning of the term 'employee' (and thus in turn the notion of the employer) covers 'any person who, in the Member State concerned, is protected as an employee under national employment law.'[14] The Directive furthermore explicitly operates 'without prejudice to national law as regards the definition of contract of employment or employment relationship.'[15]

Considered in the light of this dual purpose, the different contexts are all equally relevant. As regards the first task, it will be helpful to be able to show problems from across the employment law spectrum. As regards the second goal, the *functional notion* of the employer to be developed is not necessarily bound to a single area of regulation. Indeed, to some extent this is even true for the comparative enquiry, contributing to different aspects of the present discussion from distinct legal systems in order to provide additional external insights to the development of a unifying approach.

To put this second preliminary point rather differently, one can think of the idea of a stone, which needs to be rolled around and inspected from different angles in order

12 P Craig and G de Burca, *EU Law* (5th edn OUP 2011) ch 7.

13 Council Directive (EC) 23/2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses [2001] OJ L82/16 (ARD).

14 ibid art 2(1)(d).

15 ibid art 2(2).

to be scrutinised.[16] As different facets of the notion of the employer come under strain in various contexts it is only by looking at a selection of issues in each area that an understanding of the implications of the notion under pressure can emerge. Indeed, the problems with the received notion could in this way be analysed as resulting precisely from a one-dimensional, contractual, analysis of a multi-dimensional issue.

Structure

In order to develop the steps thus outlined, the material in this section is structured as follows: chapter three addresses specific problems in the United Kingdom and European Union context, with chapter four dedicated to an exploration of German labour law in corporate groups (*Arbeitsrecht im Konzern*). With minor variations as expedient (such as a brief excursion into comparative methodology) the chapter is generally structured to first set the scene and point out the problems that can arise from a split of employer functions before analysing potential responses within existing frameworks, and drawing tentative conclusions that will become guidelines for the reconceptualisation of the notion of the employer in part three.

[16] The author is grateful to Mr Sebastian Butschek for this point.

CHAPTER III
THE FRAGILE SCOPE OF EMPLOYMENT LAW COVERAGE

Turning first to illustrations in domestic law (as significantly influenced by EU measures in certain areas), discussion will focus on two particular implications of the inherent tension: the complete breakdown of employment law coverage in triangular (agency work) scenarios, and the incomplete and incoherent extension of employee voice mechanisms, as illustrated in the context of consultation with employee representatives in collective redundancies and transfers of undertakings. This selection is necessitated primarily by limitations of scope: the tension arises, and is significant, in employment scenarios across the board. The examples are chosen *pars pro toto* to highlight a series of different types of problems, and enable discussion of a core group of issues from a variety of angles. Ideally, the contexts should cover several parts in the lifecycle of the employment relationship and draw on a wide variety of labour market regulation tools, including common law and statutory provisions of domestic and European Union origin. The two areas chosen meet this requirement, and have the additional advantage of considerable amounts of recent litigation which can be drawn on to illustrate key arguments.

The tension characterising the notion of the employer makes employment law coverage fragile in multi-entity employment scenarios: it becomes unclear, incoherent, and open to easy manipulation. This is because the identification of the employer is driven by two conflicting strands with the potential to point in different directions. In multilateral employment relationships, the multi-functional aspect of the notion

instinctively points towards the identification of several relevant entities, whereas various elements identified as parts of the unitary strand in chapter one insist on a single entity conceptualisation. The contractual aspect of this effect will be demonstrated in the context of parcelled-out employer functions in the triangular agency employment in sub-section one; sub-section two focuses on the joint or shared exercise of employer functions across different entities.[17] As a direct consequence of the notion's underlying tension, no employer can be identified in the former scenario; in the latter identification is limited to a small subset, which may frequently be an inappropriate counterparty, or only one of several relevant entities.

The challenges arising from multiple employing entities to the very existence of a contract of employment have already been the subject of extensive scrutiny in litigation and scholarship. Discussion of the second set of implications will therefore be significantly more extensive in this chapter, particularly in order to demonstrate the importance of a coherent notion of the employer even in areas where significant problems may not have been readily perceivable to date.

SECTION I: THE BREAKDOWN OF EMPLOYMENT LAW COVERAGE

Section one of chapter two illustrated the different ways in which the five employer functions are in fact shared or parcelled out between agency and end-user in the temporary agency work context. This joint exercise of employer functions is a clear illustration of the 'profound difficulties' posed by complex triangular or multilateral employment relationships:[18] it challenges the very existence of a contract of employment, thus leaving individual workers without recourse to the majority of

[17] As noted previously, these different modes of exercise are not a clear-cut distinction; rather, they serve as a convenient sub-division for the purposes of the present analytical exposition.

[18] Freedland (n 8) 36ff.

domestic employment protective legislation. The complete breakdown of employment law coverage is a consequence of 'contractual arrangements that split, on the one hand, day-to-day control of work processes and, on the other hand, day-to-day securing and paying of people to work, [thus] prima facie prevent[ing] those working from being legally classified as anyone's "employees".'[19] The present section sets out to explore the mechanisms behind this outcome, tracing it back to the inability of the traditional common law tests for the existence of the contract of service to cope with the joint exercise of multiple functions: as the inherent tension between the multi-functional and the unitary strands of the notion of the employer is brought to the fore, no responsible employer can be identified.

The existence of a contract of employment is a necessary precondition for the claimant's success in employment tribunal cases, most notably in unfair dismissal claims;[20] the absence of any contract at all, however, can also have an impact in wider areas such as discrimination claims.[21]

Given the large number of possible factual variations as seen in the previous chapter, it is important to note that there is nothing *prima facie* to exclude the existence of a contract of employment under all circumstances, be it with an employment agency (some major industry players explicitly make a point of providing

[19] L Barmes, 'Learning from Case Law Accounts of Marginalised Working' in J Fudge, S McCrystal and K Sankaran (eds), *Challenging the Legal Boundaries of Work Regulation* (Oñati International Series in Law and Society, Hart 2012) 308.

[20] The issue at stake in the majority of cases to be discussed, below, including *James v Greenwich LBC* [2008] EWCA Civ 35, [2008] ICR 545; *Tilson v Alstom Transport* [2010] EWCA Civ 1308, [2011] IRLR 169; *M&P Steelcraft Ltd v Ellis* [2008] IRLR 355 (EAT).

[21] *Muschett v HM Prison Service* [2010] EWCA Civ 25, [2010] IRLR 451: in addition to unfair dismissal, a claim was brought under the wider definition of employment (including contracts for services) under anti-discrimination legislation; the absence of any contract at all with the end-user was lethal to the applicant's claim.

their workers with such contracts)[22] or end-users.[23] As discussion in the following section will show, however, this is still not a guarantee for complete regulatory coverage. The same point applies to various kinds of specific statutory interventions to be discussed extensively in chapter five.

Deirdre McCann has suggested[24] that workers' exclusion from key employment rights, triggered by the absence of a contract of employment, can be traced back to two dimensions of triangular agency work's divergence from standard employment. The first dimension revolves around the multilateral nature of the work setup. Indeed, in early cases such as *Construction Industry Training Board v Labour Force Ltd*, this seemed to lead the courts to the conclusion 'that there is much to be said for the view that, where A contracts with B to render services exclusively to C, the contract is not a contract for services, but a contract sui generis, a different type of contract from either of the familiar two.'[25] While this *sui generis* analysis is generally no longer considered appropriate today, a second dimension, *viz* the fact that the worker's relationship with the agency is a casual working arrangement has become increasingly important. For present purposes, discussion is therefore broken down into analyses of the two potential relationships involved: that between the temporary worker and the agency, and that between the temporary worker and the agency's client or end-user.

SUB-SECTION 1: NO CONTRACT WITH THE AGENCY

In their analysis of the relationship between worker and employment agency, Wynn and Leighton suggest that '[i]t is clearly understood that the agreement between a

22 *McMeechan v Secretary of State for Employment* [1996] EWCA Civ 1166, [1997] IRLR 353.

23 *Motorola Ltd v Davidson* [2001] IRLR 4 (EAT).

24 D McCann, *Regulating Flexible Work* (OUP 2008) 147.

25 [1970] 3 All ER 220 (QBD) 225 (Cooke J).

temp who is on the books of an agency is essentially a pre-contractual or collateral one.'[26] This result is borne out in some early cases such as *O'Sullivan*,[27] where the court held that there was no contract at all between agency and worker. With respect, however, this will no longer be the case in most scenarios today: a contract is frequently in place between the parties, and there is nothing in principle to stop it from being characterised as a contract of employment; indeed, the Court of Appeal so found in *McMeechan*.[28]

In reality, however, it is unlikely 'that many agency contracts will turn out to be contracts of employment [even if] the possibility should not be overlooked'.[29] Instead, while a contract with the agency will be found, it will usually be characterised as one for services. In *Wickens*,[30] for example, it was held that the claimant could not bring an unfair dismissal claim, as temporary agency workers were not engaged under contracts of employment, and that the relevant business size threshold had therefore not been met.

The explanation behind these findings can be found in the traditional common law tests as set out in chapter one; in particular the tests of control and mutuality of obligation.[31] As the previous chapter has demonstrated, the employer functions most relevant under these criteria are usually exercised jointly, or by the end-user rather

[26] M Wynn and P Leighton, 'Will the Real Employer Please Stand Up? Agencies, Client Companies and the Employment Status of the Temporary Agency Worker' (2006) 35 ILJ 301, 319.

[27] *O'Sullivan v Thompson-Coon* (1972) 14 KIR 108 (DC).

[28] (n 22).

[29] HMRC, *Employment Status Manual*, ESM2002, <www.hmrc.gov.uk/manuals/esmmanual/ESM2002.htm> accessed 1 September 2012.

[30] *Wickens v Champion Employment* [1984] ICR 365 (EAT).

[31] The latter one being especially important since *Carmichael v National Power Plc* [1999] 1 WLR 2042 (HL).

than the agency. The Court of Appeal's decision in *Bunce v Postworth*[32] neatly illustrates this point. The applicant was a welder on the books of an employment agency, Skyblue. While the vast majority of engagements were for one particular end-user, a railway company, the relationship there was not exclusive, and the Employment Tribunal's decision as to the absence of an employment contract with any particular end-user was never appealed. The employment agency exercised a range of employer functions, including payment, training and the provision of certification materials and tools.[33] Once at the actual job sites, however, the welder worked directly under the control of each client. As Keene LJ put it '[t]hat is really fatal to [the claimant's] case'.[34] The mutuality of obligation test can play a similarly lethal role, as the decision in *Montgomery v Johnson Underwood* shows:[35] an agency-supplied receptionist was not an employee working under a contract of service because of the absence of mutually reciprocal obligations.

Despite exceptions on the facts of specific cases[36] or in the practice of individual agencies that explicitly 'employ' their temporary workers,[37] it is therefore unlikely that temporary workers will come within the protective scope of a contract of employment with their agency.

32 *Bunce v Postworth Limited t/a Skyblue* [2005] EWCA Civ 490, [2005] IRLR 557.

33 ibid [9].

34 ibid [29]-[30]. For lack of control over day-to-day work see also *Dacas v Brook Street Bureau (UK) Ltd* [2004] EWCA Civ 217, [2004] ICR 1437.

35 [2001] EWCA Civ 318, [2001] ICR 819; confirmed in *Bunce* (n 32).

36 *McMeechan* (n 22).

37 C Forde and G Slater, 'The Role of Employment Agencies in Pay Setting' (ACAS Research Paper 05/2011) 14; K Ward, 'Making Manchester "Flexible": Competition and Change in the Temporary Staffing Industry' (2005) 36 Geoforum 223.

SUB-SECTION 2: NO CONTRACT WITH THE END-USER

The situation as against end-users is similar, if not even more difficult. There is generally no direct contractual arrangement in place between the parties, although factual exceptions are again possible.[38] The traditional tests for employment status are the by now familiar starting point, as seen for example in Elias J's decision in *Stephenson v Delphi Diesel Systems Ltd*.[39] There, an employee's previous service under an agency arrangement was held not to have been under a contract with the end-user, thus negating the possibility of an unfair dismissal claim. In so doing, Elias J's focus was firmly on mutuality of obligation as the test for the existence of a contract: '[t]he significance of mutuality is that it determines whether there is a contract in existence at all.' [40] Given the absence of a duty to pay the assigned worker continuously or provide any future work there could therefore be no contract of any kind; the issue of control, in this analysis, having been relegated to the classification of any contract that may be found to exist.

At the time of Elias J's judgment in the EAT, however, a crucial development had already come underway, with courts initially surprisingly willing to explore other ways of establishing a contractual relationship with the end-user. The absence of a written contractual document between the parties has never been a problem in this context, as section 230 of the Employment Rights Act 1993 explicitly provides that a

[38] *Dacas* (n 34): contract with client; *Motorola* (n 23): very high level of end-user control, including training and sanctions; worker is employee.

[39] [2003] ICR 475 (EAT).

[40] ibid [11]. Picked up by Munby J dissenting in *Dacas* (n 34).

contract of service can be 'express or implied, and (if it is express) […] oral or in writing'.[41]

In *Dacas v Brook Street Bureau*,[42] a Court of Appeal led by Mummery LJ had picked up earlier foundations in cases such as *Franks v Reuters*[43] and developed the use of implied contracts in triangular work scenarios. On the facts of the case, this aspect of the decision was strictly *obiter*, as the claimant had never appealed the employment tribunal's finding that there was no contract of employment with the end-user, Wansborough Council. Nonetheless, in overruling the EAT's finding that the cleaner had been employed by the agency, the court found that as a matter of law, an implied contract between parties was a possibility that tribunals ought to have considered.[44]

The majority opinion in *Dacas* was approved in 2006 by the Court of Appeal in *Muscat*.[45] The most important thing to note about the latter decision, however, is the court's explicit linking of previous *dicta* that a contract could only be implied where necessary[46] to the business reality test of necessity as espoused by Bingham LJ in *The Aramis*.[47, 48] This was an early sign of a shift in focus – soon to be driven along by

41 ERA 1996, s 230(2).

42 (n 34).

43 *Franks v Reuters* [2003] EWCA Civ 417, [2003] ICR 1166.

44 The case law surrounding implied contracts will be discussed extensively in chapter five.

45 *Cable & Wireless Plc v Muscat* [2006] EWCA Civ 220, [2006] ICR 975 [45].

46 *Dacas* (n 34) [16].

47 *The Aramis* [1989] 1 Lloyd's Rep 213 (CA).

48 *Muscat* (n 45).

Elias J in the EAT,[49] and culminating in the Court of Appeal's ruling in *James v Greenwich London Borough Council*.[50]

In that case, the applicant had been seconded by her agency to the respondent council as a housing support worker for nearly three years. When Ms James attempted to return to work after an extended period off for health reasons, she found that her function had been filled by another temporary worker. There was no contention for a contract of employment directly with the agency.[51] Mummery LJ took the opportunity to review the existing case law on employment relations in triangular setups,[52] and made it clear that the threshold for implication was a high one: as the council's exercise of employer functions over Ms James could be explained by the parties' 'respective contracts with the employment agency, […] it was not necessary to imply the existence of another contract in order to give business reality to the relationship between the parties.'[53]

The resulting difficulty in establishing a contract of employment with end-users is evident in a series of subsequent EAT decisions,[54] and was confirmed by the Court of Appeal two years later in *Alstom*.[55] Whilst the Employment Tribunal in *Alstom* had analysed the agency arrangements as merely a payment mechanism and therefore

49 *National Grid Electricity v Wood* [2007] UKEAT/0432/07.

50 See also *Cairns v Visteon UK Ltd* [2007] ICR 616 (EAT).

51 *James* (n 20) [18]. There usually is a contractual nexus between worker and agency, but it will rarely be one of service: *Wickens v Champion Employment* (n 30).

52 *James* (n 20) [46] - [52]. Agency worker cases at the tribunal stage had been stayed in anticipation of the decision.

53 ibid [42].

54 For example in *East Living Ltd v Sridhar* [2007] UKEAT/0476/07/RN (carer not employed as other explanations for work negate necessity test) or *Vidal-Hall v Hawley* [2007] UKEAT/0462/07/DA (social worker in relationship with charity, no need to also imply relationship with HM Prison Service).

55 *Alstom* (n 20).

implied a direct contract with the end-user, Elias LJ in the Court of Appeal held that the other contractual relationships in the multi-agency arrangement were a sufficient explanation of Mr. Tilson's service; consequently, no contract of employment could be implied.[56] The implications and possible interpretations of this line of cases will be discussed extensively in chapter five; suffice it to note for the moment that it is increasingly unlikely that a contract of employment would readily be implied between an agency worker and the end-user of the agency's services.

The starkest implication of shared exercise across multiple *loci* has thus become visible: a worker can find herself without recourse to the most significant employment protective rights in triangular settings, as neither the arrangement with the agency nor the relationship with the end-user are classified as a contract of employment. This situation is not infrequently exacerbated by the fact that many individuals in non-standard employment relationships have little understanding of their legal status.[57]

SECTION II: INCOMPLETE AND INCOHERENT COVERAGE

The second set of implications will be discussed in a different regulatory context, with examples chosen from statutory provisions that facilitate and protect employee voice in the work place. The section will draw in particular on employers' duties to consult employees before specific events in a company's life cycle, with a view to influencing the exercise of related employer functions: collective redundancies, and the transfer of undertakings. Whilst consultation duties have today been extended to a more general

[56] ibid [49].

[57] B Burchell, S Deakin and S Honey, 'The Employment Status of Individuals in Non-Standard Employment' (1999).

plane,[58] these areas are closely linked[59] examples of two such duties that continue to draw litigation at the highest levels. A multi-functional notion of the employer would point to all entities that are actual decision makers under such circumstances. In corporate groups, however, the distinct legal personality of each entity confines the identification of the employer to the immediate contractual counterpart alone.

In line with the overall design of part two, this section is organised as follows. A first sub-section outlines the basic regulatory motivation and frameworks, before looking at the difficulty of identifying the relevant employer in the two contexts: the person or persons taking the decision leading to collective redundancies, and the transferor entity in the transfer of undertakings. The discussion's initial focus will be on the difficulty of identifying the employer for purposes of collective redundancy consultation. As the two areas are reasonably similar for present purposes this is then followed by an analysis of recent important developments concerning the notion of the employer in the context of the Acquired Rights Directive. Sub-section two continues an exploration of that context, with a view to demonstrating why the corporate veil may continue to operate so strongly in shaping a unitary notion and denying a successful multi-functional identification of the employer, as well as showing up the deep flaws of such analyses. This material then provides the basis for section three, which sets out the key conclusions to be drawn from this chapter.

[58] Directive (EC) 14/2002 of the Council and the European Parliament of 11 March 2002 establishing a general framework for informing and consulting employees in the European Community [2002] OJ L80/29.

[59] ibid, pr 5: '[…] Information, consultation and participation for workers must be developed along appropriate lines, taking account of the practice in force in the various Member States. Such information, consultation and participation must be implemented in due time, particularly in connection with restructuring operations in undertakings or in cases of mergers having an impact on the employment of workers.'

SUB-SECTION 1: EMPLOYEE CONSULTATION IN COLLECTIVE REDUNDANCIES AND TRANSFERS OF UNDERTAKINGS

Discussion thus turns to the substantive areas under review: the information and consultation of employees in cases of collective redundancies and transfers of undertakings. The principal goal of statutory regulation in the former area is to avoid or reduce the need for redundancies or, failing that, to limit the impact of layoffs. The economic idea underpinning an obligation on employers to consult with employees is that the party taking a restructuring decision will be able to identify the overall most efficient choice only in dialogue with directly affected individuals. In order to ensure this, all stakeholders must be able to signal correctly their range of preferences, which in turn is only possible if their representatives have access to all the relevant information.

As regards the motivation underpinning the second area, changes in the structure and composition of enterprises were one of the key economic consequences envisaged by the creators of the European Single Market.[60] With the changes in economic activity there was to come an increase in productivity and wealth – but also an increase in the uncertainty faced by individual workers: as new shareholders and management took over, implicit bonds between the existing owners and employees were bound to break down.[61] The (then) Community therefore saw a need to provide for the protection of employees' rights in the resulting organisational changes,[62] primarily through 'the principle of the retention of employment contracts despite a

[60] ARD (n 13), pr (2).

[61] A Shleifer and L Summers, 'Breach of Trust in Hostile Takeovers' (1987) NBER Working Paper No 2342. The same is said to be true in Private Equity transactions today: D Hall, 'Methodological Issues in Estimating the Impact of Private Equity Buyouts on Employment' (Public Services International Research Unit, UNITE 2007).

[62] ARD (n 13) pr (3).

change in the legal personality of the employer'[63] and by imposing a range of related obligations such as information and consultation with employees affected by a reorganisation.[64] The relative weight accorded by the Community to the policy goal of safeguarding employees' rights in enterprise restructuring from early on was significant, thus justifying the imposition of 'a major limitation on […] the power of employers to arrange their commercial and corporate affairs in such a way as to minimise or fragment their employment law liabilities.'[65]

These goals will be defeated by problems in identifying the employer: in the transfer of undertakings, the crucial question is as to whether the transferor of the undertaking was also the worker's employer, as the protective regime is otherwise inapplicable. In the context of redundancy consultations, wrong identification places obligations on parties other than those who are contemplating dismissals and will eventually take the relevant decisions. As the European Court of Justice itself has pointed out, one cannot comply with the Directive and avoid or reduce the number of terminations if consultation of workers' representatives comes subsequent to the redundancy decision.[66]

The Regulatory Frameworks

While the policy considerations and general context are therefore reasonably similar, the regulatory frameworks must be set out separately. The duty to consult with

63 Commission Report on Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses (Brussels, 18 June 2007) COM(2007) 334 final [6].

64 ARD (n 13), ch III.

65 Deakin and Morris (n 11) 234. A summary of substantive provisions can be found at [3.67]ff.

66 Case C-188/03 *Junk v Kühnel* [2005] ECR I-885 [38].

employee representatives in the case of collective redundancies, first, is found in section 188 of TULRCA 1992,[67] which implemented the Collective Redundancies Directive (98/59/EC).[68] Where more than 20 employees are to be made redundant at an establishment within a period of 90 days, the employer has to commence negotiations, 'with a view to reaching agreement', on ways of avoiding the dismissals, reducing the numbers of employees to be dismissed, and mitigating the consequences of the dismissals.[69] In so doing, relevant information needs to be provided to the employees' representatives, including details about the reasons for redundancies and the proposed method of selecting those to be dismissed;[70] these requirements have increasingly been interpreted as encompassing broader economic reasons for the employer's decision.[71] If an undertaking is found to have breached these obligations, the employees can apply for a protective award.[72]

The regulation of transfers of undertakings, on the other hand, stems from the Acquired Rights Directive 1977,[73] as implemented in the United Kingdom four years thereafter.[74] A series of politically controversial amendments and re-enactments followed;[75] the provisions in force today are set out in the Acquired Rights Directive

67 Trade Union and Labour Relations (Consolidation) Act (TULRCA) 1992, pt IV ch II: Procedure for Handling Redundancies (s 188-198).

68 Council Directive (EC) 59/1998 on the approximation of the laws of the Member States relating to collective redundancies [1998] OJ L225/16 (Collective Redundancies Directive).

69 TULRCA 1992, s 188(2).

70 ibid ss 188(4)(a) and (d) respectively.

71 *UK Coal Ltd v NUM* [2008] IRLR 4 (EAT) [84, 87] (Elias J).

72 Which is of penal rather than compensatory nature: *Susie Radin Ltd v GMB* [2004] IRLR 400 (CA).

73 Directive (EC) 187/1977. Today consolidated in the ARD (n 13);

74 Transfer of Undertakings (Protection of Employment) Regulations 1981, SI 1981/1794 (TUPE).

75 S Hardy and R Painter, 'Revising the Acquired Rights Directive' (1996) 25 ILJ 160, 165.

of 2001 on a European level,[76] to which the 2006 TUPE Regulations give domestic effect.[77] The Regulations apply if there is a relevant transfer of an undertaking, business or part thereof, 'where there is a transfer of an economic entity which retains its identity'.[78] The precise scope of this requirement has been the subject of extensive litigation and academic writing. As the issues under discussion there are not specific to the PE or Corporate Group setting, the application of TUPE to a subsection of the scenarios under discussion (management buy-out of a unit in a larger, solvent business) will be assumed for present purposes. Once TUPE applies, there are two crucial consequences, the latter of which is particularly relevant for present purposes: contracts of employment will not terminate in a transfer of the business (or part thereof), having effect 'as if originally made between [the employee] and the transferee'.[79] The same general principle applies to collective agreements[80] and trade union recognition.[81] The parties are furthermore subject to a reasonably wide range of duties, including the provision of information on 'the fact that the transfer is to take place, the date or proposed date of the transfer and the reasons for it; the legal, economic and social implications of the transfer for any affected employees; [and] the measures [to be taken] in connection with the transfer';[82] and a duty to 'consult the

76 ARD (n 13).

77 P Davies and M Freedland, *Towards a Flexible Labour Market: Labour Legislation and Regulation since the 1990s* (Oxford Monographs on Labour Law, OUP 2007) 92.

78 Transfer of Undertakings (Protection of Employment) Regulations 2006, SI 2006/246, reg 3(1)(a).

79 ibid reg 4(1).

80 ibid reg 5.

81 ibid reg 6.

82 ibid reg 13(2)(a) – (d).

appropriate representatives of [the employees to be made redundant] with a view to seeking their agreement to the intended measures.'[83]

SUB-SECTION 2: WHICH ENTITY IS THE RELEVANT EMPLOYER?

The existence of a second *locus* of control gives rise to two potential issues in the context of collective redundancy consultation: first, where the most appropriate entity may not be under an obligation to consult with employee representatives. If this obligation is placed on an investee company alone, for example, the scope of consultation would become vastly under-inclusive in the Private Equity context: it is at, or more precisely in the run-up to, the decision-making stage that consultation will be at its most effective, by making a broad range of information available to the decision maker, and challenging him or her to come up with a plan that takes all stakeholders' interests into account. The PE analyst team preparing the redundancy decision will frequently have access to the company's financial and strategic data, but not always a lot of information beyond that. Its decision, which will frequently be final, may therefore be inefficient, both in terms of its impact on employees and the financial performance of the fund, as there was no obligation to consult with worker representatives. The second potential issue arises in relation to the contractual employer (*viz*, the portfolio company), who may attempt to use superior but formally external decisions as a defence to excuse its non-compliance with the consultation regime: the CEO of a portfolio company may not have contemplated redundancies until informed thereof by the PE management company, but nonetheless has to give effect to these orders as a clear expression of shareholder interest. As subsequent discussion will show it is only the latter of these issues (the 'defence question') that is successfully addressed by the current redundancy consultation regime.

[83] ibid reg 13(6).

The issue of external influence is clearly addressed in the Directive's preamble, where the Community institutions note that

> it is necessary to ensure that employers' obligations as regards information, consultation and notification apply independently of whether the decision on collective redundancies emanates from the employer or from an undertaking which controls that employer.[84]

This desire is reflected in article 2(4), which decrees that the Directive's obligations 'shall apply irrespective of whether the decision […] is being taken by the employer or by an undertaking controlling the employer,' ie even in circumstances where the latter has not provided the relevant information to its subsidiary. At first sight these provisions appear to give effect to the goals of the Directive – the obligations 'apply' even where decisions are not taken by the employing entity's executives or board of directors. The wording of the preamble covers two distinct problems: first, that a company could rely on external decisions imposed on it as a defence to avoid consultative obligations; and second, that no meaningful consultation with the appropriate decision-making body takes place at all.

Upon closer inspection it becomes apparent that while the provisions may be successful in addressing the first problem, they fail to attain the Directive's goals, as the second issue is not considered. *Ex-ante* consultation with the relevant decision maker is considerably more important than the *ex-post* imposition of a punitive award.[85] There are several sources of this limitation: a particularly narrow transposition of Article 2(4) in section 188(7) TULRCA 1992 in the United Kingdom and, on both domestic and Union levels, an unduly restrictive interpretation of the Directive and its implementing provisions.

[84] Collective Redundancies Directive (n 68) [11].

[85] *Susie Radin Ltd v GMB* (n 72).

The consultative obligations in Article 2(4) of the Directive are transposed in the United Kingdom as section 188(7) TULRCA 1992. This provision sets out a defence available to the employing entity if special circumstances make it not reasonably practicable for it to have informed and consulted the workforce before the collective redundancies took place: it will only have to take such steps as are reasonably necessary. It is not difficult to envisage how binding orders from a superior company (acting if necessary as a sole shareholder) could be invoked as such a special circumstance, in effect negating the section 188 duties. Subsection (7) goes on to decree, however, that '[w]here the decision leading to the proposed dismissals is that of a person controlling the employer (directly or indirectly), a failure on the part of that person to provide information to the employer shall not constitute special circumstances rendering it not reasonably practicable for the employer to comply with such requirement.'

It is not immediately obvious where this 'special circumstances' defence and the exceptions to it are grounded in the Directive; it appears to be a uniquely British approach to transposition.[86] The key problem for present purposes is the fact that the section 188(7) arrangement will only ever address the defence point, which was identified as one of two problematic issues in the Directive's preamble: there is nothing to guide consultative efforts towards the party best placed to discharge this duty. As regards the defence question, repeated decisions have emphasised that 'special circumstances' is a high threshold indeed: the events in question need to be something out of the ordinary; even a very significant event such as insolvency, which may regularly occur in the business world, is not enough.[87] The futility of consultation

[86] Deakin and Morris (n 11) 936.

[87] *Clarks of Hove Ltd v The Bakers' Union* [1978] IRLR 366 (CA).

(an argument at hand in most PE situations) will likewise not constitute a special circumstance by itself.[88]

Even where a court heeds the legislation's worker-protective purpose and attempts to look beyond this reductive interpretation towards effective consultation, however, there is very little space to manoeuvre within that framework. In *GMB v Beloit Walmsley*,[89] the UK subsidiary of a US paper conglomerate had ceased trading following the parent entities' surprise collapse; two separate rounds of redundancies consequently took place. A breach of the section 188 consultation requirements was conceded before the court, the focus of the argument thus shifting onto the special circumstances defence. The Employment Tribunal held that the unexpected announcement had indeed constituted such special circumstances, and that the second part of section 188(7) was not applicable as the decision leading to the dismissals had not been that of the American parent company, nor had the latter failed to provide relevant information.

The Employment Appeal Tribunal, having noted that this was the first time it had been asked to interpret these particular provisions, first turned to the Directive's preamble to discover the purposes of consultation. With this in mind, it proceeded to construe widely the requirement of 'information' to be provided, and held that the parent companies' actions may well have been decisions with 'the causal effect of requiring dismissals by reason of redundancy by the employers, and that the person or persons who made them must have contemplated that they would have that consequence'.[90] Seen through the narrow perspective of the defence question, this

88 *Iron & Steel Trades Conferedation (ISTC) v ASW Holdings plc* 2004 WL (EAT); *Middlesborough BC v TGWU* [2002] IRLR 332 (EAT); but cf *Amicus v GBS Tooling Ltd (in administration)* [2005] IRLR 683 (EAT).

89 *GMB (AEEU & MSF) v Beloit Walmsley Ltd* [2003] ICR 1396 (EAT).

90 ibid [23].

decision is to be welcomed: it ensures that the general high threshold (which excludes economic events such as insolvency) is equally applied in group settings. Towards the end of the tribunal's judgment, however, Mitting J suggested that it was 'delay in communicating [the redundancy] decision which is the mischief at which the exception to the special circumstances defence in section 188(7) is aimed.'[91] It is submitted, with respect, that this constitutes far too narrow an interpretation of the provision, particularly in light of the material extensively cited in the earlier parts of the appeal tribunal's judgment.

At the European Union level, the first opportunity to clarify the application of Directive 98/59 to situations where decisions are taken by entities other than the undertaking's management arose in *Fujitsu Siemens*.[92] Here, control was exercised by Fujitsu Siemens Computers (Holding) BV, a company incorporated and resident in the Netherlands, over manufacturing plants in Kilo, Finland and various locations in Germany. On December 7, 1999 the executive team of the parent company held a telephone meeting to discuss the potential disengagement from the Kilo plant, and resolved to propose the measure to the parent company's board. The latter supported the proposal on December 14 without, however, deciding on a specific plan of action. Local management in Kilo consulted with employee representatives from 20 December 1999 to 31 January 2010, before ceasing activity on February 1 and terminating the employment of 350 workers from February 8 onwards. The trade unions representing the claimants alleged that these steps meant that Fujitsu Siemens had failed to comply with the Directive's obligations as transposed in Finnish law.

91 ibid [22].

92 Case C-44/2008 *Akavan Erityisalojen Keskusliitto AEK ry and Others v Fujitsu Siemens Computers Oy* [2009] ECR I-8163 AG[50].

At first instance it was held that consultation amongst Kilo employees had been genuine. Upon appeal, several questions were referred to the ECJ, including (questions 3 and 4) whether the obligation to inform and consult originated at the point in time when the controlling parent undertaking discussed a general need for action, or only once collective redundancies were contemplated specifically in the subsidiary company; and (questions 5 and 6) whether consultation needed to be finalised before the parent took general commercial or strategic specific decisions that might lead to redundancies, or only before the need for dismissals was certain.

AG Mengozzi's opinion started with a detailed examination of the scope *ratione personae* of the Directive, asserting that this was firmly restricted to the employing entity itself.[93] Whilst the Advocate General then conceded that compliance with the information requirement might be impossible without assistance from the controlling entity, he nonetheless went on to suggest that this could not be read as a duty on the latter to hold direct consultations. Indeed, the *travaux préparatoires*[94] to the directive had made it clear that its provisions were not to be used as a 'bypass' mechanism.[95] In following this line of reasoning, the Court affirmed that the Directive's obligations were squarely based on the 'employer, in other words a natural or legal person who stands in an employment relationship with the workers who may be made redundant'.[96] An undertaking, even if capable of controlling the employer through binding decisions, did not have that status. The Directive's goal was not to restrict the commercial freedom of corporate groups to choose their organisations' management

93 ibid AG[35].

94 European Commission, *Explanatory Memorandum to the Proposal for a Council Directive amending Directive 75/129* COM(91) 292 final OJ 1991 C310, 5 [16].

95 *Fujitsu Siemens* (n 92) AG[40], AG[42].

96 ibid [57]-[58].

structures, and none of its provisions could be interpreted as imposing any obligations on the controller.[97]

The Court then turned to its comparatively brief answers to the specific questions referred. A duty to start consultation, first, only arose once the specific subsidiary had been identified. If that company had not been immediately and properly informed by the controlling entity this would constitute a breach of the Directive's provisions, with the consequences to be born by the subsidiary alone.[98] As regards the timing of the final decision to dismiss workers, on the other hand, 'in the context of a group of undertakings [… the] decision by the parent company which has the direct effect of compelling one of its subsidiaries to terminate the contracts of employees [… could] be taken only on the conclusion of the consultation procedure within that subsidiary.' These answers express an unease in dealing with the issue at stake: while the Court was mindful of not rendering the duties fictional, it nonetheless refused to give the information and consultation obligations full effect by including in their scope the party best placed to discharge them.

It should be noted that the wording of the decision throughout, and especially in answer to the questions referred, is relatively unclear, as the recent Court of Appeal decision in *US v Nolan* shows:[99] here, the respondent had made some 200 civilians redundant as a consequence of the decision to close RSA Hythe, a military base in Hampshire, in September 2006. Ms Nolan alleged that the USA had failed to consult with representatives of the civilian workforce, in particular by not consulting before, and about, the operational decision to close the base.[100] In November 2010, the Court

97 ibid [59], [68].

98 ibid [63], [69].

99 *The United States of America v Christine Nolan* [2010] EWCA Civ 1223, [2011] IRLR 40.

100 ibid [3].

of Appeal referred a series of questions to the ECJ, in particular as to the distinction between the adoption of business and operational strategies and consequent redundancy decisions. In March 2012, AG Mengozzi suggested that consultation was to begin as soon as a strategic decision compelled the contemplation of collective redundancies;[101] at the time of the final editing of this thesis the Courts' opinion had not yet been handed down.

In the Private Equity context (and indeed many forms of corporate groups), several of the distinctions drawn by the ECJ in *Fujitsu Siemens* may be entirely fictional: as opposed to the board of holding companies, fund teams will always take decisions directly for each investment – identifying the relevant subsidiary will rarely be a distinct step.[102] Applying the wording of the answer to questions 5 and 6 in the judgment,[103] therefore, it would appear that a fund's decision to dismiss a group of employees would be in direct contravention of section 188 TULRCA 1992. This conclusion holds true even if the decision was transmitted informally to portfolio company management, as the tests focus on the 'factual level' of control exercised.[104] While the fact that the resulting protective award can only be made against the investee company might matter in certain groups of companies with distinct accounts and liabilities, it is of little relevance to the Private Equity operator whose returns are directly linked to cashflows from the portfolio company.

The law's inability to identify the appropriate employing entity or combination of entities where there has been a split of employer functions across multiple

[101] Case C-583/10 *Nolan* (ECJ, pending) [AG Opinion of 22 March 2012]. The 'compelling force' of individual decisions is to be determined by the Member State courts: AG[49].

[102] Essentially only where the investee itself is a group of companies.

[103] *Fujitsu Siemens* (n 92) [71].

[104] Jan Heinsius, 'Commentary on the EU Court's Decision in *Fujitsu*' (2010) 7 European Company Law 165, 168.

corporations is a result of the two competing strands of the notion of the employer. Its problematic consequences extend to both employees and management, as the most appropriate entity may be under no duty to be involved in dialogue with employee representatives. As regards PE management companies, there is the potential of liability where fund-internal procedures mean that 'workers would be presented with a fait accompli, and the provision would be deprived of any practical effect.'[105] For employees, on the other hand, there is little chance that their representatives will be able to engage in meaningful consultations as to the workforce's future.

Potential Solutions

The issue thus identified exists at both Community and domestic level: the problems that can arise from complex corporate setups in informing and consulting employees are twofold, yet only the reliance on external (shareholder) instructions as a potential defence is successfully addressed. The differences shown up at the different regulatory levels are, however, not ones of degree, but of kind. In the ECJ, a broad interpretation of the Directive's provision would be feasible, whereas given the UK implementation in section 188(7) the possibilities for an effective solution within the existing framework are few. For the information and consultation duties to operate effectively in subsidiary-parent or portfolio company-PE fund circumstances, the very duties created by the collective redundancy regime would need to be able to identify the relevant counterparty as the employer: the obligations have to rest on the body from which the decision to effect collective redundancies emanates, regardless of whether parent and subsidiary entities are acting independently or jointly.

Within the existing domestic framework, there is but one potential route to achieving this result: a challenge to the proper transposition of the Directive under EU

[10] *Junk* (n 66) AG[60].

law principles. It has long been established that the UK government showed particular reticence in the transposition of various employee consultation Directives;[106] the European Commission first instituted infringement proceedings in 1992.[107] These were primarily focussed on the consultative mechanism and the remedial regime, however, and did not address the peculiarity of section 188(7). The same is true for another series of judicial discussions, this time on the temporal element of the consultative requirement, a decade later.[108] It is therefore unlikely that such an avenue for reform will be pursued.

Before the European Court of Justice, on the other hand, there is at least some possibility that *Fujitsu Siemens* may not be followed in its narrow confinement of the consultative obligation to the subsidiary entity and formal counterparty to the contract of employment. The court's general approach in the area of employee consultation has frequently been a purposive one, both generally to achieve the proclaimed harmonisation goals of various Directives,[109] and specifically in order to support their worker-protective stance.[110] In the present context, this general stance would suggest a functional approach to the interpretation of the Directive's requirements; that is a finding of consultative obligations resting on whichever entity will in fact take the eventual redundancy decision. It is against this backdrop that the judgment in *Fujitsu Siemens* must be evaluated.

[106] P Davies and M Freedland, *Labour Legislation and Public Policy* (OUP 1993) 576 ff.

[107] Case C-383/92 *EC Commission v United Kingdom (collective redundancy infringement)* [1994] ECR I-2479.

[108] See eg *MSF v Refuge Assurance plc* [2002] 2 CMLR 27 (EAT).

[109] Case C-242/09 *Albron Catering BV v FNV Bondgenoten* [2011] All ER (EC) 625.

[110] See eg Case C-55/02 *EC Commission v Portuguese Republic* [2004] ECR I-9387 [50]; Case C-449/93 *Rockfon A/S v Specialarbejderforbundet i Danmark* [1996] ECR I-4291.

The relevant sections of Advocate General Mengozzi's opinion, endorsed by the court, begin with an examination of the 'scope *ratione personae* of Directive 98/59, and in particular the question […] whether that Directive lays down obligations incumbent not only on the employer but also on the undertaking controlling that employer.'[111] This question is answered primarily by reference to the actual wording of the provisions, with a major emphasis on the practicality of needing a *single* entity on whom the various duties (information, notification, consultation) in the run-up to the proposed redundancies rest, which is to discharge them and accept liability for the failure so to do. This last part of the AG's argument is not necessarily contentious – indeed, it harks back to the defence point already discussed at length: in a multi-entity scenario it is crucial to avoid the exploitation of the corporate group in order to escape regulatory obligations. In cases where the redundancy decision is shared between two entities, it will always be possible for an employment tribunal to decide on the facts which company was the primary *locus* of decision making – or impose AG Mengozzi's solution as a default outcome unless displaced by factual evidence.

The case for the single entity on which the obligations are imposed always to be the subsidiary, on the other hand, is a much weaker one, even if constructed purely on the wording of the Directive: whilst this might be the appropriate solution in the majority of cases, there is nothing to suggest an inherent need for a focus on any particular entity. Indeed, the Advocate General concedes that 'the fact remains that, if the parent company takes the decision leading to collective redundancies, it is required to provide the necessary information to the relevant employer under its control'[112] thus directly contradicting the later assertion that 'the fulfillment of [the consultative

[111] *Fujitsu Siemens* (n 92) AG[35].

[112] ibid AG[40].

obligation] falls exclusively on the employer even if the parent company controlling that employer takes the decision leading to collective redundancies.'[113]

A second set of reasons offered for the narrow confinement of the consultative obligation to the contractual work-taking employer is traced back to a quote from the *travaux préparatoires*, giving the impression that the Commission's original focus was to protect corporate groups' freedom to organise their management structure internally. Upon a detailed reading of the cited document, however, this is not the case.[114] Instead, it states explicitly that the Directive is designed to 'ensure that the information, consultation *and* notification requirements are met *whatever the identity of the undertaking* which takes the relevant decisions leading to the collective redundancies.' [115]

The defence question is merely seen as an addendum to this:

> The main changes [in the consolidated version] are to fulfil the aim of ensuring the enforcement of the existing directive […]. Thus, it is provided that the information and consultation requirements laid down by the directive apply irrespective of whether the decisions entailing collective redundancies are taken by the employer himself, by a controlling undertaking or by the central administration of a multi-establishment undertaking. *In order to reinforce* this central obligation it is *also* established that an employer's failure to comply with the directive's requirements can not be condoned on the ground that the undertaking taking the decision leading to collective redundancies failed to inform the employer in due time.[116]

[113] ibid AG[42].

[114] Even though it had become, somewhat ironically, the Commission's position by the time of *Fujitsu Siemens* (n 92) [59].

[115] European Commission (n 94) 6 [15]. Emphasis supplied.

[116] ibid 6 [14]. Emphasis supplied.

While the AG is therefore correct to suggest that the Directive 'does not directly impose any obligation on controlling undertakings *as such*,'[117] the conclusion that no obligation must be imposed under any circumstance is, with respect fallacious. Indeed, the Commission's explanatory notes seem to support the development of a functional approach by emphasising that all obligations are to apply substantively regardless of the corporate structure in question – the opposite of the reductive view emerging from *Fujitsu Siemens*.[118]

A final strand of reasoning, prevalent particularly in the Court's decision, focuses on the Directive's repeated use of the word 'employer' in the singular. The ECJ goes on to suggest that this ought to be construed as 'a natural or legal person who stands in an employment relationship with the workers who may be made redundant. An undertaking which controls the employer, even if it can take decisions which are binding on the latter, does not have the status of employer.'[119] This narrow definition of the employer has not been a consistent element in the court's jurisprudence, as the court's recent decision in *Albron*[120] shows. There, the court interpreted the notion of the employer in complex group scenarios very widely indeed, by seeing it as independent of direct contractual arrangements.[121] When looking for potential solutions within the existing framework, therefore, it may be possible to read *Fujitsu Siemens* as a case confined in its larger impact to a reasonably narrow set of facts – which may of course in turn inform the member state courts' duty of compliant

[117] ibid 5 [16] as cited by the AG; 6 [16] in the version available to the author. Emphasis supplied.

[118] Indeed, the Commission's main concern with imposing liability seem to have been the difficulties arising from extraterritorial regulation; this is no longer considered as a serious obstacle to legislative harmonisation.

[119] *Fujitsu Siemens* (n 92) [57] - [58].

[120] *Albron* (n 109).

[121] A decision in the context of the ARD (n 13), which is similar enough for present purposes: Deakin and Morris (n11) 913.

interpretation in a possible challenge to the UK's highly limited transposition of the Directive.

The much more flexible approach to identifying the employer arose in the context of a question as to which party in a large multi-entity group was the relevant transferor for ARD purposes. In *Albron*,[122] the court applied a very purposive interpretation to the definition of the transferor under Dutch ARD implementation measures and found that a service company without direct contractual links to the employees could nonetheless be an employer and thus a relevant transferor.

The claimant Mr Roest had been an employee of Heineken Nederlands Beheer BV (B), a staff service company within the Dutch beer brewing group, for over twenty years. He was permanently assigned to Heineken's catering entity (H). In early 2005, H's activities were taken over by Albron Catering BV (A), and Mr Roest commenced employment with A. With the support of his trade union, he subsequently claimed that this change had fallen within the remit of the Dutch ARD provisions, and that he was therefore entitled to the same contractual terms as before the outsourcing.

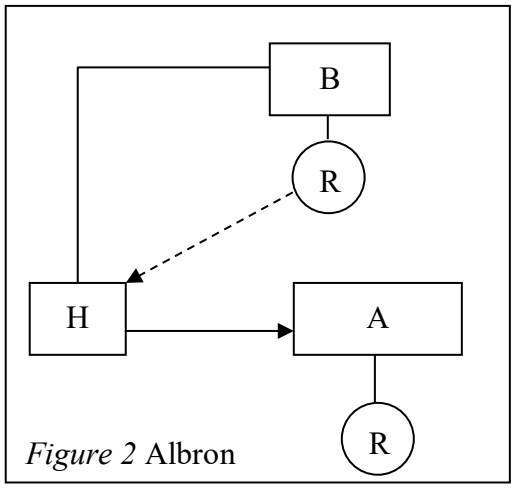

Figure 2 Albron

The national court referred the question to the ECJ whether H could be regarded as a transferor under the Directive despite the absence of a direct contractual relationship of employment with Mr Roest, given the context of a group of companies.

[122] *Albron* (n 109).

The Court of Justice, following the AG's opinion,[123] answered the question in the affirmative. It arrived at this result having considered the purpose and wording of Directive 23/2001, finding that whilst the transferor was the party losing the capacity of employer, 'in the mind of the Union legislature, a contractual link with the transferor [was] not required in all circumstances for employees to be able to benefit from the protection conferred by [the Directive's provisions].'[124] In complex group situations with a 'plurality of employers', there was nothing to suggest that 'the contractual employer must systematically be given greater weight.'[125] Indeed, as the transfer regime was designed to 'protect employees in the event of a change of 'employer', 'a change in the legal or natural person […] responsible for the economic activity' could be a relevant transfer despite the absence of direct contractual relationships, 'even [where] there exists within [the corporate] group an undertaking with which the employees concerned were linked by […] a contract of employment.'[126]

This finding that the meaning of 'transferor' was not necessarily limited to the claimant's contractual employer, but also extended to a third party exercising economic control over the worker, led to a considerable flurry of practitioner comment.[127] Its precise impact remains unclear, especially given the apparent focus

123 ibid [AG opinion of 3 June 2010].

124 *Albron* (n 109), [24].

125 ibid [25].

126 ibid [28], [30] and [32] respectively.

127 See, eg DLA Piper, 'TUPE: *Albron Catering BV v FNV Bondgenoten*' (2010); Freshfields Bruckhaus Deringer, 'Simplifying the Application of the Acquired Rights Directive to Complex Corporate Structures?' (2010); Allen & Overy, 'ECJ Confirms its Broad Interpretation of the Scope of Transfer of Undertakings Protection' (2010) and Thompsons Solicitors, 'An Acquired Taste: *Albron Catering BV v FNV Bondegenoten*' (2010).

on the permanent nature of Mr Roest's assignment to H,[128] and the court's emphasis on the corporate veil's protection of internal group structures in other contexts.[129] The position in the United Kingdom after *Albron* is equally unclear: as has been seen, the courts have traditionally refused to pierce the veil in TUPE transfers.[130] Depending on the context of future cases, it is possible to envisage a split between the private (where the employment tribunal is under a strong interpretative obligation, but no more) and public sectors (where an employee could attempt to rely on the direct effect of the Acquired Rights Directive).

The crucible of a potential solution lies in the court's recognition that parties other than a contractual counterparty to the contract of service can be responsible for employees' sphere of economic activity, and therefore the regulatory consequences attached to it, and that the status of 'contractual employer' does not automatically take precedence over such external control. There is little in the judgment to suggest that this purposive interpretation of the ARD is limited to the transferor concept. Even in that case, however, it may have an impact in the present context: where a PE fund divests a portfolio company, for example in a secondary sale to another investor, it could be seen as a transferor, in addition to or instead of the investee enterprise. The primary benefit to employees of such an extension would be unlikely to relate to the existence of the contract of employment (as, unlike in *Albron*, this issue would not arise), but rather would consist of the additional information and consultation duties contained in TUPE. Going beyond this narrow impact, the principles espoused by the

[128] Though this aspect is much more pronounced in the AG's reasoning, eg *Albron* (n 109) AG[61], than in the Court's final judgment.

[129] *Fujitsu Siemens* (n 92).

[130] *Brookes v Borough Care Services Ltd and CLS Care Services* [1998] ICR 1198 (EAT); *Clifton Middle School Governing Body v Askew* [2000] ICR 286 (CA).

Court may in addition mean that the strict separation of shareholders and contractual employers as seen in *Fujitsu Siemens* is now open to serious questioning.

SUB-SECTION 3: SHAREHOLDERS AS EMPLOYERS?

The tension underpinning the notion of the employer is thus increasingly coming to the fore: while its multi-functional strand implicitly recognises that relevant employer functions are exercised by multiple parties, the strong unitary assumption limits the imposition of duties to a singular entity. One particularly strong instantiation of this assumption is the idea that shareholders must generally be kept clearly distinct from employers. The transfer of an undertaking provides a salient illustration of how the identified tension creates the resulting problems in identifying the employer. As the precondition for triggering the operation of the protective regime is a *change in employer*, the unitary strand of the notion leads to very arbitrary distinctions as to when a relevant event takes place.

This significant limitation to the scope of TUPE protection has already been briefly touched upon: the definition of relevant transfer in Regulation 3 does not encompass situations where the legal personality of the target company is unaffected, such as for example a change of its members. This has the effect of '[p]aradoxically […] exclud[ing …] the most important kind of change of ownership in our system of company law, namely takeover by share purchase.' [131] The following paragraphs explore this exclusion in terms of its statutory origin and application in the common law, and contrast it with situations where TUPE does apply. Against this background, a discussion of PE transactions highlights a further problem in defining the employer: the current notion leads to an entirely arbitrary application of particular norms. In the

[131] P Davies and M Freedland, 'The Effects of Receivership upon Employees of Companies' (1980) 9 ILJ 95, 109.

present context, the justifications given for the share transfer exclusion are incongruent with its effect where the shareholder is a Private Equity fund.

In its initial proposals of 1973, the European Commission explicitly included share transfers within the ambit of the (then draft) Acquired Rights Directive.[132] The protective regime was designed to apply 'also to concentrations by which control was acquired in an undertaking, so affecting the most common form of share mergers, without a change in the identity of the employer, in Great Britain.'[133] This was to be achieved by including in its scope transactions where control was acquired, which in turn was defined very widely, including the 'power to influence the composition, voting or decisions of the organs of an undertaking'.[134] Pressure exerted by the United Kingdom and other Member State governments,[135] however, succeeded in excluding share transfers from the ARD's scope; and the UK did not make use of its power to enact a higher level of protection (which would have been far more intrusive than the existing common law position) in the 1981 transposition.[136]

The exclusion's operation is strict.[137] In *Brookes*,[138] a large group of care home workers who had previously been employed directly by a local Council were transferred to a limited company operated by the latter in 1992. Several years later, the

[132] [1973] OJ C104 (as cited by S Hardey, *Understanding TUPE – A Legal Guide* (Chandos 2001) 12).

[133] B Hepple, 'Recent Legislation: European Economic Community' (1977) 6 ILJ 106.

[134] B Hepple, 'Workers' Rights in Mergers and Takeovers: The EEC Proposals' (1976) 5 ILJ 197, 205.

[135] Davies and Freedland (n 106) 579.

[136] B Hepple, 'The Transfer of Undertakings (Protection of Employment) Regulations (1982)' 11 ILJ 29, 31.

[137] Though note the potential departure in *Millam v Print Factory (London) 1991 Ltd* [2007] EWCA Civ 322, [2007] IRLR 526.

[138] *Brookes* (n 130). Similarly *SI (Systems and Instrumentation) Ltd v Grist* [1983] ICR 788 (EAT).

Council decided to sell its care homes to a provident society. The purchaser was aware of the (then) recent decision in *Wilson*,[139] and decided that the only way it could modify the employee's terms and conditions was if the transaction were structured as the equivalent of a share sale, rather than a transfer of the undertaking. Despite this explicit intention to avoid the application of TUPE, the EAT held that the Regulations had not been triggered. Relying on *Adams v Cape Industries plc*,[140] the tribunal found that as the company's arrangement had not been a mere façade, the corporate veil could not be pierced. Similarly, in *British Nursing v Peterson*[141] the applicant had worked for Goldsborough (G), a subsidiary company of health care provider BUPA. In 2001, the entire share capital in G was sold to BNA (B), itself a subsidiary of another major company in the industry, Nestor. Mr Peterson was made redundant following a reduction in the number of field manager positions. In somewhat unclear proceedings, the tribunal at first instance found that the transaction had not merely been a share sale, but that following it there had been a separate transfer of G's undertaking to B.[142] The Employment Appeals Tribunal relied on *Brookes* in holding that the first instance tribunal had erred in law. The idea that a change in factual control over the enterprise could be sufficient was rejected in explicit terms:

> [B] acquired the means to influence and control [G]'s policies and decisions as to the employment and retention of staff. [G] had, by reason of the share purchase, become a part of the [B] stable. However, of course, the fact that by reason of the share transfer [B] had become the owner of the shares in [G] and had thus acquired the ability to decide, in effect, whether [G] carried on in business did not have the effect that [G]'s undertaking was transferred to [B] and, if it did, how it would carry on its business. […] None of that control indicates that

[139] *Wilson v St. Helen's Borough Council* [1995] ICR 711 (EAT).

[140] *Adams v Cape Industries Plc* [1990] Ch 433 (CA).

[141] *British Nursing Co-operations Ltd v Peterson* (unreported, 16 January 2004) (EAT).

[142] ibid [33].

> [G]'s business or part of it (as opposed to the ability to control that business) had been transferred to [B].[143]

The basis of the share transfer exception, therefore, is the argument that a change of shareholder does not change the nature of the employer. This idea, however, conflates a change of identity with a change of legal personality, as the juxtaposition of two examples from the Private Equity context shows. A change in the employer's identity is frequently what PE management companies hope to achieve in a buyout transaction. Where the target company is part of a larger corporate group, and is acquired via a share sale from the target parent to the domestic acquisition special purpose vehicle (ASPV), TUPE will not apply.

Another common way for Private Equity funds to source new deals is to work with the management of a particular department within a large company, such as R&D or particular services,[144] towards a spin-off into a new company. Contrary to the share sales discussed above, TUPE does apply in such situations. The sale of a part of an undertaking falls within the definition of an economic entity as 'an organised grouping of resources which has the objective of pursuing an economic activity, whether or not that activity is central or ancillary.'[145] The ECJ held in *Botzen* that 'the decisive criterion regarding the transfer of employees' rights and obligations [was] whether or not a transfer takes place of the department to which [the employees] were assigned and which formed the organizational framework within which their employment relationship took effect.' [146] Put differently, while the group of individuals transferring is reasonably limited, there is no doubt that TUPE will apply

[143] ibid [21].

[144] Interview with former Investee Company CEO (Oxford 23 February 2010).

[145] TUPE (n 78) reg 3(2).

[146] Case C-186/83 *Arie Botzen and Others v Rotterdamsche Droogdok Maatschappij BV* [1985] ECR 519 [15].

to the core group of the departmental employees. This is true even if no assets are transferred, as long as the activity is of the application of TUPE in a PE-backed management buy-out.

This 'arbitrary impact of the Directive'[147] and the resulting incongruence between regulatory aims and the effects of the relevant provisions is by no means confined to a Private Equity subset of cases: in *Brookes*,[148] for example, the applicants were in fact subject to two changes in the structure of their employing entity. The first was a transfer of the care homes from the Council to BCS Ltd. While the factual identity of the employer remained unaffected, BCS Ltd was a new legal entity (a company limited by guarantee), and TUPE therefore applied. The subsequent share transfer to CLS Care Services Ltd, an entity harbouring intentions of changing the nature of the employer, on the other hand, was not capable of triggering the employee-protective regime.[149] In the PE context the distinction is even starker, especially where various kinds of transactions are economically identical from the fund's perspective. The split of employer functions between the buyout firm and its portfolio company management is equally applicable, regardless of how a fund acquired a particular investment. The structure of the investment (P2P or a spin-off transaction), on the other hand, will expose the fund to very different levels of potential employment law liability.

From the employees' perspective, the joint exercise of employment functions which comes into existence following a Private Equity investment is therefore a prime example of the situation envisaged by Elias and Bowers where workers 'may be

147 P Davies, 'Transfers – The UK Will Have to Make Up Its Own Mind' (2001) 30 ILJ 231, 234; there criticising the impact of the ECJ's decision in Case C-172/99 *Oy Liikenne* [2001] ECR I-475.

148 *Brookes* (n 130).

149 ibid 1201G-H.

significantly affected by a change in the control of the company in which they work.' The incongruence in identifying the relevant employer, however, 'has the effect that employees have no right to be informed or consulted about most takeovers even though the nature of the new controllers may be of great importance to their working lives.'[150]

Despite these problems, as long as the notion of the employer is characterised by the strong influence of the elements constituting the unitary strand, effective change is unlikely. As noted by the UK government's consultation paper on TUPE in 2001, 'the scope of the legislation is the most extensively debated and litigated aspect of the current regulations.'[151] Indeed, public stances on the share exclusion continue to be divided across the spectrum: a House of Lords Select Committee in 1995, for example, found in favour of extending TUPE's scope to cover share transfers; a 2001 DTI consultation paper, on the other hand, suggested that the government's opposition to an extension remained unchanged.[152] The most recent discussion of the issue at the European level is found in the Commission's impact report pursuant to Article 10 of the ARD. After a survey of Member States and consultation with relevant interest groups, it clearly affirmed the status quo, suggesting that

> [t]he transfer of ownership of the majority of the shares in an undertaking or a change in the majority of shareholders does not constitute a transfer because the legal personality of the employer is unchanged. The Commission considers that a revision of the Directive, extending the definition of 'transfer' to include a change of control, as

[150] P Elias and J Bowers, *Intelligence Report. Transfer of Undertakings: The Legal Pitfalls* (6th edn FT Law & Tax 1997) 33 [2.4.1]

[151] Employment Relations Directorate, 'Transfer of Undertakings (Protection of Employment) Regulations 1981: Government Proposals for Reform. Detailed Background Paper' (DTI 2001) [5].

[152] House of Lords Select Committee on the European Communities, Fifth Report, Session 1995-96: *Transfer of Undertakings: Acquired Rights* (HL Paper (1995-96) No 38, 11 July 1995); Employment Relations Directorate (n 151). For full discussion of these sources, see J McMullen, 'An Analysis of the Transfer of Undertakings (Protection of Employment) Regulations 2006' (2006) 35 ILJ 113, 119.

> proposed by the European Confederation of Trade Unions […], is not justified at this stage. Although a change of control can lead to changes in the undertaking, the employees' legal position vis-à-vis the employer is unchanged. [153]

Significant change to the regulatory provisions on a domestic level is equally unlikely. In early 2008, John Heppel MP introduced a Private Equity (Transfer of Undertakings and Protection of Employment) Bill. [154] Having noted the potential impact of PE takeovers on employees and the fact that transactions structured as share sales would fall outside the scope of the existing TUPE provisions, the Bill sought to extend the TUPE regime to the acquisition, transfer or disposal of substantial shareholdings by PE funds. The latter terms were not explicitly defined in the Bill, with 'Private Equity Company' to be accorded such meaning as prescribed by the Secretary of State in a statutory instrument, [155] and 'Substantial Shareholding' linked to the definition of controlling undertakings in Regulation 3 of the Transnational Information and Consultation of Employees Regulations 1999. [156]

The Bill then targeted the incongruence just set out: by widening the relevant definition of the employer, PE controlled transactions are brought within the scope of TUPE, and employees and their representatives are accorded most information, consultation and protection rights directly against the controlling Private Equity shareholder in addition to the employing enterprise. Some natural limitations apply, for example as there is no need to transfer or novate contracts of service in the case of

153 COM(2007) 334 final, [2.2.1].

154 Private Equity (Transfer of Undertakings and Protection of Employment) Bill, Bill 28/07-08: 'A Bill to extend the application of the Transfer of Undertakings (Protection of Employment) Regulations 2006 to the acquisition and disposal of substantial shareholdings by private equity companies; and for connected purposes.' (Bill).

155 Bill, cl 1(4).

156 SI 1999 / 3323.

a share sale.[157] The rights accorded to employees go further than the scope of TUPE, a fact apparently not intended by the Bill's sponsor, who indeed offered to withdraw these at the (hypothetical) committee stage when challenged in the House of Commons.[158] Examples include additional information and consultation rights, including employee representatives' entitlement to commission external expert studies and a *quasi*-works council setup for the first five years after the transaction,[159] the requirement to seek employee agreement before the transaction can take place, and an additional remedy in the form of injunctive relief in the High Court.[160]

The Bill's initiative was welcomed by the Trade Union movement; indeed it closely mirrored the substantive suggestions set out by Jack Dromey, the (then) Deputy General Secretary of the Transport and General Workers Union in a *Financial Times* article calling for increased regulation of Private Equity 'employers' the previous year.[161] The BVCA, a Private Equity industry body, unsurprisingly came out strongly against the proposed measure, suggesting that no substantive changes, including as regards employee protections, were brought about by share sales: '[i]n relation to any concerns regarding potential job losses there is existing employment legislation [to protect employees – TUPE]. […] There is no basis in logic or law for such an extension. It is unnecessary and would be grossly unfair.'[162] This stance was supported by leading PE practitioners, notwithstanding their contradictory (and probably more truthful) advice that the enactment of the draft Bill 'would have made

[157] V Keter, 'Private Equity (Transfer of Undertakings and Protection of Employment) Bill 2007-08: Research Paper 08/23' (House of Commons Library 2008) 9.

[158] HC Deb 7 March 2008, col 2031.

[159] Bill, cl 4(5) and 4(3), respectively.

[160] Bill, cl 5(2).

[161] J Dromey, 'Protect Workers from Private Equiteers' (Financial Times 3 July 2007)

[162] BVCA, 'TUPE Briefing Note' (London 2008)

the restructuring and renegotiation of employment terms on or post completion much more difficult.'[163]

This strong opposition, in combination with its sponsor's own admission that there were significant 'technical difficulties in the Bill'[164] and lacking support from the government, meant that the Bill failed to reach its committee stage on March 7, 2008.[165] Until its promised return in a refined version,[166] the identified 'anomaly' in the law therefore remains.[167]

Section two has thus identified some of the implications of the conflicted notion of the employer in the context of multiple entities' joint exercise of employer functions, be they shared or parcelled out. The multi-functional aspect of the current conceptualisation would easily permit the identification of relevant entities, but different elements in the unitary strand limit the enquiry to a single entity. The distinct legal personality of group entities was seen as a particular obstacle: obligations are placed on a limited subset, which may frequently contain only one of the relevant decision making entities, or even an inappropriate one that was merely executing decisions taken elsewhere. The unitary strand furthermore drives a strong perception that the corporate entity employer must under all circumstances be completely distinct from its shareholders, despite the illogic consequences this can lead to, for example in determining whether a change of employer has taken place in a corporate restructuring.

163 C Wynn-Evans, 'TUPE or not TUPE?' 94 Dechert Comment: Private Equity Europe 8

164 HC Deb 7 March 2008, col 2031.

165 HC Deb 7 March 2008, col 2092 (Motion and bill, by leave, withdrawn).

166 L Peacock, 'MP vows to carry on fighting for TUPE private equity deals' (Personnel Today 10 March 2008)

167 HC Deb 7 March 2008, col 2029.

SECTION III: EVALUATION

Having set out a broad range of practical examples, discussion thus returns to the second goal of part two: to collect first guidelines for the reconceptualisation of the notion to follow in the final part. Three such lessons can be identified at this stage. First, the extent to which the notion of the employer is shaped by an unconscious assumption of *excessive homogeneity*. Second, that in resolving the tension between the *formalist or unitary and the functional strand*, the latter may be the more promising avenue to pursue: the strict attachment to contractual formalism can quickly lead to the breakdown of coverage, leaving the notion of the employer vulnerable to changing socio-economic circumstances. A cautious functional approach, on the other hand, is less susceptible to such developments, as first judicial pronouncements in that direction show. The third lesson, finally, is that if the legal framework within which a particular problem is set up is itself problematic it can only be addressed by a *careful departure that remains within existing frameworks*. The TUPE (PE) Bill discussed earlier is an example of how on-the-spot solutions frequently fail for that very reason; a similar point applies in the context of purposive judicial intervention, which is not immune from this problem, either, as an analysis of the ECJ's decisions in *Rockfon* and subsequent cases shows.[168]

Avoiding Excessive Homogeneity

There are two clear illustrations of the first observation, *viz* that the notion of the employer is currently shaped by an unconscious assumption of a high degree of homogeneity. It is not accurate to assume, for example, that regulatory coverage will be complete in all situations where there is a contract of service in any particular employment relationship. The examples given in section two are stark reminders of

[168] *Rockfon* (n 110).

how substantive compliance can quickly be defeated where the exercise of employer functions is shared between multiple entities. A second, related, insight derives from a specific aspect of regulatory technique: as the analysis of the ARD and TUPE provisions has shown, it is crucially important to address fundamental distinctions within the field to be regulated instead of assuming an artificial homogeneity throughout the group. In the present context this could be achieved, for example, by focussing on the different economic incentives of distinct groups of shareholders: at its most basic, the difference between individual dispersed and disinterested shareholders, and sophisticated block owners with a direct interest in the management of their portfolio company.

The current approach sees shareholders as a homogenous group at the former end of the spectrum. As a result, the shareholder exception conflates 'change in shareholder' with 'no change in the employer's identity'. It is true to say that the first step in this reasoning, that a change in shareholder does affect the company's legal personality, is correct. However, not every change of a company's identity requires a change of legal personality. The reasoning therefore only works in a particular subset, dispersed shareholders, where the underlying premise of the shareholder exception is true: legal personality and the realities of control (and hence the identity of the employer) remain unchanged when shares are bought or sold on a public exchange. In the case of block or majority share ownership, on the other hand, there is no such link: with the shareholder change comes a change in control, and thus in identity – indeed that will frequently be the purpose of acquiring a controlling block in the first place.[169]

[169] Equity markets price this distinction into block acquisitions as the control premium.

To put the same point differently, it is accurate to say that a sale of shares does not affect the legal personality of the company, but merely its beneficial ownership.[170] It is then fallacious, however, to jump from this to the assertion that '[s]hare transfers do not change the identity of the employer' under any circumstance,[171] as even the (then) Minister for Employment Relations, Pat McFadden, suggested in setting out the government response to the Private Member's Bill.[172] When a principle that is correct for a particular sub-group is artificially stretched to encompass a larger, heterogeneous group, the door is opened for it to produce paradoxical results in situations that do not fit with the assumptions of the original paradigm. In the context of different groups of shareholders, other areas of the law have long realised this principle and given effect to it: company law, for example, treats block or majority shareholders differently in a number of instances, from acquisition reporting requirements to additional duties towards other (minority) shareholders.[173]

Towards a Functional Approach

The second lesson that emerges from the material surveyed is that in resolving the tension between the unitary and the multi-functional strand, the former may have to give way more than the latter. The utility of the current unitary approach has come under particular scrutiny, as the consequences of a strict attachment to its inherent formalism can quickly lead to the breakdown of employment law coverage, as demonstrated in triangular relationships. In corporate groups, on the other hand, the present state of the law may appear to be entirely satisfactory: corporate groups should

[170] Keter (n 157) 13.

[171] ibid 14.

[172] HC Deb 7 March 2008, col 2088.

[173] P Davies and S Worthington, *Gower and Davies' Principles of Modern Company Law* (9th edn Sweet & Maxwell 2012) ch 19.

be able to partition their assets and liabilities as they see fit; any downsides such as potential regulatory costs arising from such actions will be priced into the value of the firm. [174] Employees will always be able to claim a monetary award if their representatives can prove that key decisions had been made by the PE management company and that portfolio company management simply went through the motions of consultation once it had been instructed to effect the layoffs: the superior entity's anterior decision cannot be invoked as a defence. The punitive element of the damages awarded, finally, ensures that firms will not engage in such behaviour on a repeated basis.

This approach – reflected to a large extent, for example, in the United Kingdom's reductive interpretation of what employee consultation is about – is unsatisfactory on a number of levels. Both the economic goals of majority shareholders and the personal interests of individual workers would be better fulfilled by a *functional* approach, ie one that looks at consultation as the underlying goal, independent of formal technicality. On this view, the *ex post facto* imposition of punitive awards for failure to consult with employee representatives about the avoidance or reduction of redundancies is the least desirable outcome: for the majority shareholder, because value is lost not only by the absence of employee voice, but additionally the regulatory fines; [175] for the employee, because it will be very difficult, if not impossible, to weigh up the value of his or her employment in simple monetary terms. A functional approach to this problem would be designed to achieve compliance with the consultation provisions by adjusting the *locus* of the consultative obligation in line

[174] H Hansmann and R Kraakman, 'The Essential Role of Organizational Law' (2000) 110 Yale Law Journal 387.

[175] For recent research on which see J Armour, C Mayer and A Polo, 'Regulatory Sanctions and Reputational Damage in Financial Markets' CELF conference paper, Oxford 13 April 2011.

with the relevant decision making power, thus engaging both positive and negative aspects of employee protection.

There is therefore a clear need for a cautious functional approach in moving beyond restrictive notions of the employer. At the European Union level, the ECJ's decision in *Albron* achieved precisely this result: what mattered there was being responsible for the economic activity.[176] This approach, independent of group companies' formal arrangements, allowed the Court to sidestep the worker-protective *lacuna* that could arise from a strictly technical or formalistic interpretation. A focus on 'the substance and not the form of the transaction'[177] is similarly possible at the domestic level, as a recent decision in the present context demonstrates.

In *Millam v Print Factory*,[178] the Court of Appeal had to decide by way of a preliminary question whether the claimant's employment had transferred from F, his original employer to M, when the former's parent entity had sold its shares in F to M.[179] Buxton LJ set out the basic rules in such situations, *viz* that a share transfer does not normally involve a transfer of the underlying business that could trigger TUPE,[180] and that even in group or parent – subsidiary relations there was no assumption of control being exercised over a company's business by its shareholder.[181] However, his Lordship went on to note that these were 'merely reminders that the question is

[176] *Albron* (n 109) [31].

[177] Elias and Bowers (n 150) 43; citing Case C-24/85 *Spijkers v Gebroeders Benedik Abbatori CV* [1986] ECR I-2479.

[178] *Millam* (n 137). For an early note, see Linklaters, 'TUPE: When is a Share Sale Not a Share Sale?' (2007).

[179] In which case its successor entity, the defendant, could potentially be liable.

[180] *Brookes* (n 130).

[181] Case C-234/98 *GC Allen v Amalgamated Construction Co Ltd* [1999] ECR I-8643.

whether as a matter of fact the business […] has been transferred.'[182] On the facts, the tribunal at first instance had found that there had been a transfer despite the share sale, as

> [t]he buyer of the shares did far more than a simple shareholder would have done following a simple sale, or in our experience, a parent company of a subsidiary would have done in similar circumstances. In particular, [M]'s handling of a significant element of the management of [F] set its actions apart from those of a mere shareholder. It made key decisions […].[183]

The Employment Appeals Tribunal subsequently overturned this decision, on the basis that the ET had effectively pierced F's corporate veil. The high 'sham' requirement for this to be possible had not been met, as the two companies continued to have separate boards, accounts and VAT registration.[184] On the analysis of Moses LJ, however, this was not to be understood as a case of piercing the veil: M was not to be liable for F's activities as a shareholder *per se*. Instead, the ET's finding was to be correctly understood as the shareholder, due to its close control and involvement in F, actually having carried out various business activities *through* F. In the course of his judgment, Buxton LJ also noted the key advantage of a successful functional approach: 'The legal structure is of course important, but it cannot be conclusive in deciding the issue of whether, within that legal structure, control of the business has been transferred as a matter of fact.'[185]

[182] *Millam* (n 137) [3].

[183] ibid [4], quoting the ET's decision at [5.9].

[184] *Millam* (n 137) [20] – [24].

[185] ibid [9].

Developing Existing Frameworks

The final lesson to be taken away from chapter three is the realisation that framework problems such as the current tension underpinning the notion of the employer cannot easily be solved by on-the-spot interventions. Neither purposive judicial interpretation nor individual legislative interventions in response to a particular facet of the problem will provide effective solutions: as the frame is bent to fit into one corner, it snaps apart at another – the on-the-spot fix has actually caused further problems.

The first context in which this can be seen is the failure of the Private Equity (TUPE) Bill.[186] To build on the frame metaphor, whilst a new part to be inserted into an existing frame might in itself be different from the element it is to replace, it must nonetheless fit into the pre-existing structure in order to achieve its purpose. Seen through this angle, the key problem of the Bill quickly emerges: it foundered on its attempt to regulate but one particular phenomenon, without taking account of the larger context – as its sponsor admitted before the House of Commons.[187] First, whilst attempting to introduce considerable change by expanding the overall application of TUPE, core notions are reaffirmed in their narrow-most conception: '[r]eferences to employees of the transferor or transferee are to be read as references to employees of the employer'.[188] The emphasis on such orthodoxy should not be underestimated: the ECJ's decision in *Albron*, for example, would have been impossible under this provision, as the claimant employee there did not stand in any direct contractual relationship of employment with the transferor.

[186] The political background to the Bill, which has already been alluded to above, may of course be invoked as part of the answer to the charges which follow, but is not immediately relevant for the present doctrinal-analytical purpose.

[187] HC Deb 7 March 2008, col 2032 (John Heppel MP).

[188] Bill (n 154), cl 4(2).

The failure to engage with large parts of the underlying problem is visible, second, from a failed attempt to define key terms. As the research report accompanying the Bill notes, '[i]n non-legal language the term "private equity" covers a very wide range of businesses. It may be difficult to define with legal certainty which companies should be caught by the Bill's provisions.'[189] This is the case because the Private Equity business model allows the exploitation of an arbitrage opportunity that exists between different forms of economic organisation.[190] Any attempt at reform that does not engage directly with this question[191] will soon run into the third problematic issue: a host of unintended consequences that arise as a result of the conceptual distortion. As Christopher Chope MP noted during the second reading of the Bill, its proposed definition could mean that 'a private equity organisation would be any organisation that is incorporated, other than a public listed company.'[192] Another unintended consequence, discussed at length, related to the possibility of injunctive relief creating considerable delays in the takeover process, which could increase uncertainty for workers, for example in the case of an enterprise nearing bankruptcy.[193]

Purposive judicial interpretation in a limited area is just as vulnerable to framework problems, as can be illustrated in the context of Directive 59/1998. One of its trigger requirements is a minimum amount of employees affected by the planned mass redundancy. There are two alternative formulations of this threshold, either as a

[189] Keter (n 157) 7.

[190] To be explored in detail in a forthcoming paper by the author. The basic idea is that the gains resulting from the elimination of one agency problem (shareholders-management) are higher than the resulting cost in other agency relationships, because only one of the affected stakeholders (creditors) can impose their cost on the controlling shareholder.

[191] For example, by leaving the relevant definitions to the Secretary of State: Bill, cl 1(4).

[192] HC Deb 7 March 2008, col 2053.

[193] HC Deb 7 March 2008, col 2064 ff (Jonathan Djanogly MP).

percentage or as an absolute number; it is up to each Member State to choose which option to implement.[194]

In *Rockfon*,[195] the ECJ had to address the definition of 'establishment' on the facts of a case arising from dismissals within the Rockwell Group, the employers of more than 300 workers in several sub-units that shared a single personnel department. Given the Danish transposition option and the size of the enterprise, the claimants had to show that a certain percentage within the establishment had been affected in order to claim under the collective redundancy provisions. It was undisputed that if Rockfon, one of the three units, were found to be an establishment, the relevant member state provisions would apply. The Danish Labour Council defined establishment as the Rockwell Group as a whole, and held that no obligations had therefore been triggered.

The ECJ set out by affirming that the Directive was not aimed at restricting the freedom of undertakings to organise their activities, nor intended to lay down rules relating to the internal organisation of undertakings or the management of their personnel.[196] Based on the AG's opinion, it went on to suggest that as the wording of different language versions was unclear, regard had to be had to the 'purpose and general scheme of the rules' – in this particular instance, the 'greater protection of workers in the event of collective redundancies.'[197] An interpretation that would allow companies to make the Directive's application more difficult would allow companies 'to escape the obligation to follow certain procedures for the protection of workers and large groups of workers could [thus] be denied the right to be informed and

[194] Collective Redundancies Directive (n 68) art 1.

[195] (n 110).

[196] ibid [21].

[197] ibid [28] – [29].

consulted.'[198] It was therefore not surprising that the Court defined the meaning of the term 'establishment' as narrowly as possible. On the facts of the case, this purposive interpretation produced a worker-productive result. Given its position in the larger statutory framework, however, problems soon emerged. As opposed to Denmark, the United Kingdom had chosen the trigger requirement in Article 1(a)(ii) of Directive 59/1998: the dismissal of at least 20 workers over a period of 90 days, whatever the normal size of the establishment. In this context, the *Rockfon* jurisprudence (as confirmed in subsequent cases[199]) was to have the very opposite effect: the narrower the definition of enterprise, the easier for an employer to compartmentalise its workforce to avoid triggering the provisions of section 188.

In *MSF v Refuge Assurance*,[200] two companies consolidated their headquarter and field staff following a merger. The employment tribunal found that the meaning of term 'establishment' covered the entire field staff at each company, thus triggering a duty to consult. On the employer's cross-appeal, the EAT (having questioned the validity of the transposition) cited the ECJ's decision in *Rockfon* that an 'establishment' did not necessarily need to have separate management which could independently effect the collective redundancies.[201] Despite the ET's warning that if each branch were held to be an establishment productive industrial relations would be rendered fictional as the employers could avoid consultation by not identifying specific branches in time, the EAT considered itself bound by the ECJ's case law, and allowed the employer's appeal. The final lesson to be drawn from the present chapter, therefore, is that even openly purposive interpretation by the courts will not

198 ibid [30].

199 Also see Case C-270/05 *Athinaiki Chartopoiia AE v Panagiotidis* [2007] ECR I-1499.

200 *MSF* (n 108).

201 ibid [52] – [53].

necessarily be enough to address the problems that can arise once the exercise of employer functions is shared by several entities: the framework itself must be able to take account of complex scenarios beyond a narrow paradigm.

CHAPTER IV
COMPLEX EMPLOYMENT STRUCTURES IN GERMANY: A COMPARATIVE PERSPECTIVE

The initial chapter of part two explored the practical implications of the tension inherent in the notion of the employer in the context of collective redundancies and the transfer of undertakings. This analysis served a dual purpose: to give examples of potential problems, and to start gathering parameters for the eventual task in the final part of this thesis: the development and evaluation of an updated notion of the employer, able to take into account the economic realities of complex employment relationships. The present goals are similar: the notion of the employer in German law will be explored to determine how key rules and institutions have developed to take account of the challenges posed by complex *Konzern* (corporate group) structures. Seen from an employment law perspective, the *Konzern* turns one of the discipline's most vexing questions – that as to the nature of the employee – on its head, asking instead: who is the employer? The existence of multiple entities on the work-taking side leads to a search for the 'lost employer, […] *le patron introuvable*.'[1]

The basic structure of the chapter loosely mirrors that of the previous one, despite its setting in a different context: after an introductory discussion of comparative methodology, the notion of the employer in German law is set out, followed by a discussion of the *Konzern* concept as the context of multiple *loci* of corporate control. Analysis then focuses on the modification of general employment law standards in the

[1] C Windbichler, *Arbeitsrecht im Konzern* (Beck 1989) 25. The following sections draw on this *Habilitation* work (especially as regards their general framework and analysis of the individual employment relationship). The author gratefully acknowledges Professor Windbichler's support in his comparative endeavour, as well as subsequent discussions with Leopold Bauer and Professor Horst Call.

Konzern context. The results of this comparative study will demonstrate that some of the deeper problems underpinning modern economic phenomena, such as their potential to frustrate the full application of employee rights, are not limited to the United Kingdom and provide further insight and background material for the thesis' eventual task.

SECTION I: A METHODOLOGY OF COMPARATIVE LAW

Zweigert and Kötz have suggested that comparative scholarship may to a large extent always remain an area where 'only sound judgment, common sense, or even intuition can be of any help.'[2] Even if one were to agree with this assessment, however, both choice of subject *and* method must be conscious ones,[3] as questions of structure and methodology are closely linked and of heightened importance in the comparative context.

As regards general methodology, much debate has raged about the ongoing validity and utility of a *functional* method of comparative law. This covers a range of techniques and outcomes with varying degrees of normative force;[4] an unsurprising discussion given the wide variety of approaches that underpin the functional method.[5] Whilst it may therefore be characterised as a *chimera* of sorts,[6] there are several core

2 K Zweigert and H Kötz, *Introduction to Comparative Law* (Tony Weir tr, 3rd edn Clarendon Press 1998) 33; recalling the earlier warning that 'sciences which have to busy themselves with their own methodology are sick sciences': G Radbruch, *Einführung in die Rechtswissenschaft* (12th edn Köhler 1969) 253.

3 O Kahn-Freund, 'Comparative Law as an Academic Subject' (1966) 82 LQR 40, 41.

4 M Freedland and N Kountouris, *The Legal Construction of Personal Work Relations* (OUP 2011) 49.

5 R Michaels, 'The Functional Method of Comparative Law' in M Reiman and R Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2007) 340, 345ff, 360.

6 ibid 340.

aspects on which most functionalists agree, and which will therefore inform the present effort:[7] first, the comparative focus is not only on individual rules of a particular system, but also their aggregate effects. It follows, second, that law cannot be seen in a vacuum, isolated from society. Third, function itself serves as the *tertium comparationis*: institutions, both legal and non-legal, even doctrinally different ones, are comparable if they are functionally equivalent. Functionality, finally, may also serve as an evaluative criterion in and of itself, subject to objections to be discussed, below.

The field of Comparative Labour Law more specifically covers a range of genres,[8] from mostly descriptive 'academic tourism'[9] and purely theoretical treatises to efforts predictive of future social or economic problems and purposive comparative work. A combination of the latter two may 'cause the reader to think and see outside his or her accustomed frame of reference; to learn that there are other ways for the law to deal with an economic or social question, ways that may actually be more protective of values the reader's system professes, that are more effective, that have lower transaction costs or fewer negative externalities;'[10] it is in this area that the present chapter hopes to be situated.

The necessity and value of comparative labour law has been recognised in leading generalist works for a considerable period,[11] and despite some warnings against

7 ibid 342 for a full overview.

8 M Finkin, 'Comparative Labour Law' in M Reiman and R Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2007) Taxonomy 1129 ff.

9 ibid (Clyde Summers).

10 Finkin (n 8).

11 H Gutteridge, *Comparative Law: An Introduction to the Comparative Method of Legal Study & Research* (CUP 1946) 31.

comparative efforts in at least one leading German textbook,[12] it is evidently clear today that 'labour law in Europe is no longer local.'[13] Historically, the majority of comparative research was found in the collective domain.[14] More recently, however, there has been a resurgence in comparative analyses of the individual employment relationship in different European legal system, both in books[15] and leading journals.[16]

The range of methodological issues to be confronted in a comparative enquiry is tightly linked to its purpose; in the present context, primarily to gather thoughts from German law to inform and evaluate the proposals to be set out in part three. This recourse to comparative law as an '*école de vérité'*, to extend and enrich the domestic 'supply of solutions'[17] is not without its own controversies, particularly as regards the normative force of its outcomes. While '[c]omparative legal enquiries are frequently made as part of an effort to improve a legal rule or institution which has been suspected or recognized as a source of problems,'[18] it has also been suggested that within a functional framework, 'recognizing different solutions abroad does not show us deficiencies at home. Functionalist comparison can open our eyes to alternative solutions, but it cannot tell us whether those solutions are better or not.'[19] This stance

12 Finkin (n 8) 1149.

13 ibid 1150.

14 P de Cruz, *Comparative Law in a Changing World* (3rd edn Routledge-Cavendish 2007) ch 13.

15 Freedland and Kountouris (n 4).

16 See eg L Mitlacher and J Burgess, 'Temporary Agency Work in Germany and Australia: Contrasting Regulatory Regimes and Policy Challenges' (2007) 23 International Journal of Comparative Labour Law and Industrial Relations 401.

17 Zweigert and Kötz (n 2) 15.

18 G Dannemann, 'Comparative Law: Study of Similarities or Differences?' in M Reiman and R Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2007) 403.

19 R Michaels (n 5) 379.

conflates two distinct points – the reliance on comparative law as a source of fresh ideas from a common fund, which is a long way removed from its 'hard' use in explicit value judgments.[20] The subsequent focus on comparative law as a tool to improve one's own (understanding of) domestic law[21] thus brings with it few of the traditional legitimacy problems.[22] Indeed, it has been suggested that in the specific context of labour law, comparative ventures can 'significantly enrich the reformers' imagination of what could be done'.[23]

Having thus situated the chapter in the broad field of comparative law, its specific methodology falls to be developed – keeping in mind the object decided upon at the outset.[24] The approach will be a multi-axial one, building on Schmidt,[25] whose suggested axes include both functional as well as doctrinal aspects; thus covering both specific outcomes, and the rules and debates behind them. The *microcomparisons*, or 'focus on specific legal […] problems'[26] will centre on the extent to which employment law coverage is affected by complex corporate structures as the 'factual situations […] which arise in connection with the topic under comparison.'[27] Given the deep connection of labour law with broader social and political norms, it has been

20 T Annus, 'Comparative Constitutional Reasoning: The Law And Strategy Of Selecting The Right Arguments' (2004) 14 Duke Journal of Comparative and International Law 301.

21 Kahn-Freund (n 3) 60.

22 J Smits, 'Comparative Law and its Influence on National Legal Systems' in M Reiman and R Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2007) 525, 528.

23 M Weiss, 'The Future of Comparative Labor Law as an Academic Discipline and as a Practical Tool' (2003-2004) 25 CLLPJ 169, 178.

24 The test advocated by AE Örücü, 'Methodology of Comparative Law' in J Smits (ed) *Elgar Encyclopedia of Comparative Law* (Edward Elgar 2006) 451.

25 F Schmidt, 'The Need for a Multi-Axial Method in Comparative Law' in H Bernstein, H Kötz and U Drobnig (eds), *Festschrift für Konrad Zweigert* (Mohr 1981) 534.

26 Zweigert and Kötz (n 2) 5.

27 Dannemann (n 18) 407

suggested that there would be little space for comparison;[28] Scheiwe on the other hand has demonstrated that this can be counteracted with an expansion of the functional equivalence term: [29] as every rule or system will always have more than one function, there can be no functional equivalents in every aspect.[30] By focussing on aspects such as a measure's aim (eg allowing the free development of company law structures, but then ensuring employee representation within what has economically grown[31]) it will nonetheless be possible to assemble valuable information for subsequent chapters.

Comparative Steps

The fundamental elements of comparison should include considerations as to the objectives, subject matter and method of comparison *stricto sensu*. [32] Hugh Collins, writing in the context of comparative contract law, develops the following five steps:

1. Identification of some aspect of domestic law which seems confused or lacks a clear rationale.

2. Identification of the social problem which this aspect of domestic law addresses.

3. Examination of the legal doctrines and techniques by which one or more foreign legal systems tackle or avoid the same problem.

[28] Zweigert and Kötz (n 2) 38.

[29] K Scheiwe, 'Was ist ein funktionales Äquivalent in der Rechtsvergleichung? Eine Diskussion an Hand von Beispielen aus dem Familien- und Sozialrecht' (2000) 83 Kritische Vierteljahresschrift für Gesetzgebung und Rechtswissenschaft 30, 33.

[30] ibid 36-37.

[31] M Kort, 'Der Konzernbegriff i.S. von §5 MitbestG' (2009) 36 NZG 81.

[32] A de Roo and R Jagtenberg, *Settling Labour Disputes in Europe* (Kluwer 1994) 8; drawing on JH Merryman, 'Comparative Law and Scientific Explanation' (Reports to the Academie Internationale du Droit Comparé 1974) 121.

4. Evaluation of the foreign solution to decide whether its approach is superior, be it in technique or result.

5. Re-analysis of domestic situation in order to reveal the conceptual obstacles to the achievement or more satisfactory results, be it in technique or policy goals.[33]

Several of these steps are outside the scope of the present chapter, or even part two more broadly: a legal problem (the split of employer functions in complex corporate structures) and its practical implications in domestic law have already been identified. The final step will run through part three. Steps 3 and 4, the examination (and, to a lesser extent, evaluation) of foreign legal techniques and solutions are thus at the heart of the present chapter. At this stage, they remain to be broken down into two further methodological points – selection, and description.[34]

The one explicit choice that remains to be explained is that as to the comparator legal system. While it has been suggested that in solution-seeking, the closer two legal systems are related the better a source of comparison,[35] the lack of radically different solutions can also be an obstacle, thus requiring a search for 'controlled difference'.[36] Indeed, the choice of comparators is highly topic-sensitive; the more specific the enquiry, the more freedom one is allowed, though a general preference for 'parent' system remains.[37] German law clearly fits this purpose: as a legal system, it has developed the necessary conceptual and technical apparatus across company and employment law to address both complex inter-related corporate ownership and

[33] H Collins, 'Methods and Aims of Comparative Contract Law' (1989) 11 OJLS 396, 399.

[34] Following Dannemann (n 18) 406ff.

[35] ibid 410, building on common law judges' preference for authorities from other common law jurisdictions.

[36] ibid 411.

[37] Zweigert and Kötz (n 2) 41-42.

employee involvement within these structures. The comparison of civil and common law is therefore 'the most fruitful field to till'.[38]

With the choice of Germany as the comparator system there comes a linguistic issue: in working with German texts, it will not only be important to watch out for *faux amis*,[39] but also to ensure consistency in the use of foreign terms in the thesis while maintaining readability. It is hoped that this will be achieved by translating into the text all materials other than relevant key terms, which will be explained (and sometimes abbreviated) at their first occurrence. Turning to the second issue, the appropriateness of the descriptive effort, Dannemann's warning to beware of immediately seeing differences or falling for similarities by slotting material into known (domestic) legal categories will be kept firmly in mind. Whilst description will be focussed on the aims and effects of different rules, the broader context cannot be ignored. [40] The functional specificity emphasised earlier does not limit one's understanding of wider issues, but focusses it where necessary. [41] Heeding Eichendorff's warning to the novice comparativist,[42] account will thus be taken not only of the 'law in the books' but also of general conditions of business, customs and practices[43] in the ambition of treating as a source of law all those factors moulding or

[38] F H Lawson, *'The Field of Comparative Law'* (1949) 61 Juridical Review 16, 35 (as cited by J Cairns, 'Development of Comparative Law in Great Britain' in M Reiman and R Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2007) 164).

[39] M Ancel, *Utilité et Méthodes du Droit Comparé: Eléments d'Introduction Générale à l'étude Comparative des Droits* (Ides et Calendes 1971) 92.

[40] Dannemann (n 18) 412-3.

[41] B Markesinis and J Fedtke, *Engaging With Foreign Law* (Hart 2009) 320.

[42] Zweigert and Kötz (n 2) 36: '*Hüte Dich, sei wach und munter!*' (Be careful, alert and cheerful!)

[43] ibid 11.

affecting the living law in the chosen system.[44] Such a move beyond the text of generalist Codes is particularly important in employment law. As Zweigert and Koetz note, the 'legal values of bourgeois liberalism' embodied in the *Bürgerliches Gesetzbuch* (BGB)[45] mean that the vast majority of employee-protective norms developed through additional actions by courts and the legislature.

This broad context, finally, matters not just in what is analysed, but also in how the results are used. Part three will not suggest any direct legal 'transplants' from German employment (or indeed company) law.[46] Even if a particular approach works well in one jurisdiction one cannot assume that a more or less direct translation would fulfil a similar purpose successfully in another.[47] A series of *ad-hoc* transplants could furthermore lead to an unnecessary fragmentation of domestic legal scholarship, and thus a 'bland convergence with the theoretical discourse of other national systems of labo[u]r law such as those of continental European countries.'[48]

The 'borrowing' of legal ideas, however, can also be a dynamic process over an extended period of time, with initial phases involving no more than the identification

[44] ibid 35. See also R Fahlbeck, 'Comparative Law - Quo Vadis?' (2003-2004) 25 CLLPJ 7: the importance of comparative labour law working with other disciplines.

[45] Zweigert and Kötz (n 2).

[46] As has happened in domestic labour law: O Kahn-Freund, 'On Uses and Misuses of Comparative Law' (1974) 37 MLR 120.

[47] Discussed in an analysis of Kahn-Freund's 1973 Chorley lecture at the LSE: M Freedland, 'Otto Kahn-Freund (1900-1979)' in J Beatson and R Zimmermann (eds), *Jurists Uprooted - German Speaking Émigré Lawyers in Twentieth-century Britain* (OUP 2004) 311. The issue is not a new one: ibid 312 (fn 51), Montesquieu, *De L'Esprit des Lois*, vol I, ch 3 'Des lois positives': *'les lois politiques et civiles de chaque nation […] doivent être tellement propres au peuple pour lequel elles sont faites, que c'est un grand hazard si celles d'une nation peuvent convenir à une autre.'*

[48] M Freedland and P Davies, 'National Styles in Labor Law Scholarship: the United Kingdom' (2001-2002) 23 CLLPJ 765, 787.

of appropriate models.[49] It is with this goal of influence, inspiration and cross-fertilization[50] in mind that relative weight will be accorded to the comparative and domestic about new 'ways of ensuring that workers are not excluded from employment protections by conceptual or structural rigidities in doctrinal reasoning.'[51]

Subsequent discussion is thus organised as previously indicated: section two outlines the basic notion of the employer in German law generally, including elements from both individual and collective domains. Discussion then turns to the *Konzern* as the legal paradigm grouping of multiple *loci* of corporate control, before focussing on examples of situations where employment law norms have been modified to take account of the *Konzern* context.

SECTION II: THE NOTION OF THE EMPLOYER IN GERMAN LAW

Despite the narrow focus of the comparative venture as just outlined, it will be important to situate the discussion in its broader legal context. The following sections thus cover key features of German labour law as well as, to the extent that enterprise co-decision and the notion of the *Konzern* are situated there, company law, in order to ensure that the enquiry to follow avoids an improper conflation of legal issues and approaches.[52] In so doing, however, it would be impossible to provide a full précis of

[49] J Fedtke, 'Legal Transplants' in J Smits (ed) *Elgar Encyclopedia of Comparative Law* (Edward Elgar 2006) 435. cf the account in B Markesinis, *Comparative Law in the Courtroom and Classroom: The Story of the Last Thirty-Five Years* (Hart 2003), which is closely focussed on utility to practitioners.

[50] M Graziadei, 'Comparative Law as the Study of Transplants and Receptions' in M Reiman and R Zimmermann (eds), *The Oxford Handbook of Comparative Law* (OUP 2007) 443.

[51] M Freedland, 'Developing the European Comparative Law of Personal Work Contracts' (2006-2007) 28 CLLPJ 487, 490.

[52] Windbichler (n 1) 582.

the legal system. Instead, the following sections give a brief account of the standard approach to selected examples in order to then permit an exploration of variations in the *Konzern* scenario, *viz* situations where the second *locus* of control over the employment relationship is a majority shareholder in the employing entity. These limitations are primarily ones of scope; it will nonetheless be important to outline and explain several choices at the outset.

Three topics in particular will be excluded from further consideration: the role of collective bargaining (*Tarifverträge*), senior management, and the extra-territorial application of German law. As regards the first of these, its exclusion might at first appear surprising – after all, collective bargaining is one of the three central categories of employment law statutes.[53] There is however little scope for its involvement in the *Konzern* field: As Boehm and Pawloski flatly note, 'there is no such thing as a *Konzern-Tarifvertrag'*. [54] Even where there is theoretical room in individual provisions of the *Betriebsverfassungsgesetz* 1972 (BetrVG) for collective bargaining agreements to determine co-decision structures,[55] its organisational patterns are too far removed from the area of discussion to be of significant relevance.[56]

The role of senior management, second, is excluded because of its anomalous and highly fact-specific treatment across different areas. Some senior managers (the so-called *leitende Angestellte*) are in fact employees,[57] but do not enjoy the full set of

53 de Cruz (n 14) 475.

54 W Boehm and H Pawlowski, 'Konzernweite Beschäftigungsgarantien bei Umstrukturierung – aber was, wenn die "Heuschrecken" kommen?' (2005) 22 NZA 1377, 1380; cf BAG decision of 11.09.1991, (1992) 9 NZA 321 (*Goetheinstitut*), 323 where the BAG held that whilst a German mother entity should try to influence foreign subsidiaries, no direct enforcement was possible.

55 M Kort, 'Bildung und Stellung des Konzernbetriebsrats bei nationalen und internationalen Unternehmensverbindungen' (2009) 26 NZA 464, 466; discussing §3 BetrVG.

56 Windbichler (n 1) 582.

57 They may even have contracts *across* the Konzern: Windbichler (n 1)

employment rights.[58] Others, notably the CEO (*Geschäftsführer*) of a GmbH are not employees despite being subject to direct control,[59] but nonetheless enjoy a legislative extension of individual employment protective measures, such as minimum dismissal periods.[60]

The impact of German law on corporate group setups crossing international borders, third, will also not be discussed to a significant extent. The general position, in both company and employment law, is one of strict territoriality:[61] co-decision in an international *Konzern*, for example, will only cover employees located in Germany.[62] If the controlling enterprise is overseas, on the other hand, there will be no scope for co-decision mechanisms there;[63] the possibility of a *Konzern*-works council under such circumstances has been the subject of intense academic debate,[64] but was eventually denied by the Federal Labour Court (*Bundesarbeitsgericht*, BAG).[65] As the issue also touches on questions of international private law, and was not pursued in the domestic legal enquiry in previous chapters, it will not be further investigated.

58 J Kirchner, P Kremp and M Magotsch (eds), *Key Aspects of German Employment and Labour Law* (Springer Verlag 2010) 3. They are also excluded (with very few exceptions) from the scope of the BetrVG: §5 III 1.

59 The *Gesellschafterversammlung*'s *Weisungen.* This power stems from §37 I GmbHG, not the contract of employment.

60 W Zöllner, K Loritz and C Hergenröder, *Arbeitsrecht* (Beck 2008) 40: BGB §622.

61 BAG decision of 14.02.2007, (2007) 24 NZA 999.

62 A seat may sometimes be offered to a foreign representative: M Gentz, 'Das Arbeitsrecht im Internationalen Konzern', (2000) 17 NZA 3, 5 (noting the presence of a US trade union representative on the board of DaimlerChrysler).

63 cf the (limited) anti-avoidance provision in §5III MitbestG, discussed below.

64 Kort (n 55) 467.

65 BAG decision of 14.02.2007 (n 61). For critical discussion, see H Buchner, 'Konzernbetriebsratsbildung trotz Auslandssitz der Obergesellschaft' in H Konzen and others (eds), *Festschrift für Rolf Birk* (Mohr Siebeck 2008) 11 ff.

Turning from exclusion to selection, finally, there are two areas in which specific norms were chosen to illustrate, *pars pro toto*, underlying points. In the area of individual employment law rights flowing from the contract of employment, this is unfair dismissal protection (in the form of the *Kündigungsschutzgesetz* 1969, KSchG): the Konzern-situation may have a direct impact on its provisions, and has been the subject of fairly recent academic and judicial discussions.[66] In the field of enterprise co-decision, the example to be discussed will be the *Mitbestimmungsgesetz* 1976 (MitbestG), instead of the *Drittelbeteiligungsgesetz* 2004 (DrittelBG) or *Montanmitbestimmungsgesetz* 1951 (MontanMitbestG), as it best illustrates the issues at stake. In terms of substantive co-decision powers, it ranges in the centre of the employee voice spectrum; likewise in terms of the applicability of its norms: while the MontanMitbestG has priority,[67] it is limited in practical impact due to its exclusive focus on mining-related companies; the MitbestG is then to be applied in preference to the DrittelBG.[68]

SUB-SECTION 1: THE EMPLOYER AS COUNTERPARTY TO THE *ARBEITSVERHÄLTNIS*

As Mehrhoff suggests, the notion of the employer (*Arbeitgeber*) in German law has historically been constructed around a duty to protect the weaker party to the *Arbeitsverhältnis* (employment relationship), despite many developments in line with social and economic structures of society.[69] There is no explicit definition of the employer; the starting point of any enquiry is the contract of employment

66 BAG decision of 26.9.2002, (2003) 20 NZA 549 (*Rheumaklinik*).

67 §1 II MitbestG.

68 §1 III MitbestG.

69 F Mehrhoff, *Die Veränderung des Arbeitgeberbegriffs* (Schriften zum Sozial- und Arbeitsrecht Band 75, Duncker & Humblot 1984). Reviewed by R Becker (1986) 3 NZA 190.

(*Arbeitsvertrag*) as the central legal organising device (*Rechtsfigur*) of employment law,[70] to which the employer is the work-taking counterparty. This is mirrored by a lack of a clear definition of the employee, with uncertainty continuing despite a long historical track record,[71] including even a constitutional challenge.[72]

The contract of employment needs to be a contract of service, with a focus on the employee's effort rather than outcome.[73] It is defined via the status of the wage-taking party,[74] the key criterion being personal subordination or a lack of independence.[75] Despite ample criticism of this approach,[76] no alternative criteria, such as a version of the business integration test,[77] have been accepted. [78] For these and a host of additional reasons,[79] then, the contract of employment itself cannot suffice as a regulatory tool. Indeed, as Simitis notes, it was the path away from an undisputed

[70] Zöllner, Loritz and Hergenröder (n 60) 1. The ECJ's decision in Case C-242/09 *Albron Catering BV v FNV Bondgenoten* [2011] All ER (EC) 625 is unlikely to upset this: H Willemsen, 'Erosion des Arbeitgeberbegriffs nach der Albron-Entscheidung des EuGH? Betriebsübergang bei gespaltener Arbeitgeberfunktion' (2011) NJW 1546.

[71] Zöllner, Loritz and Hergenröder (n 60) 27, 29: first mentioned in 1794, *Allgemeines Landrecht für die preußischen Staaten*, II.8 §423.

[72] BVG decision of 20.05.1996, AP Nr 82 zu §611 BGB Abhängigkeit. Discussed in W Däubler, 'Working People in Germany' (1999-2000) 21 CLLPJ 77.

[73] Zöllner, Loritz and Hergenröder (n 60) 35-37.

[74] Equally across all areas, other than social security and tax: Däubler (n 72).

[75] *Unselbstständigkeit* or *persönliche Abhängigkeit*: BAG decision of 20.08.2003, (2004) 21 NZA 39.

[76] Zöllner, Loritz and Hergenröder (n 60) 42.

[77] eg E Molitor, *Das Wesen des Arbeitsvertrages: eine Untersuchung über die Begriffe des Dienst- und Werkvertrags, sowie des Vertrags über abhängige Arbeit* (Deichert 1925) 82.

[78] See now also the new term 'Beschäftigte' as a specifically gender-neutral attempt: R Richardi, 'Arbeitnehmer als Beschäftigte' (2010) 27 NZA 1101, 1103.

[79] Zöllner, Loritz and Hergenröder (n 60) 2-3.

priority of the contract of employment that gave the discipline its distinct form.[80] Where labour law was thus seen as failing in its protective function, both courts and statute intervened to extend it beyond contract alone to ensure a *Schutzzweckerfüllung* (fulfilment of protective purpose).[81] These additional areas included the field of collective bargaining and a close involvement in the employer's decision making, both at the level of individual measures (through works councils) and entrepreneurial choices more generally (co-decision).[82]

The totality of legal relationships springing from the contract of employment is thus subsumed into the notion of the *Arbeitsverhältnis*. As employment law is seen as concerning employers as much as employees, the notion of the employer in the *Arbeitsverhältnis* is simply the party other than the employee to it.[83]

SUB-SECTION 2: KEY AREAS AND SOURCES

There is no one code regulating the entirety of German employment law. Instead, it can be found in a wide range of relevant sources, from the *Bürgerliches Gesetzbuch* (BGB) and the *Grundgesetz* (Basic Law) to individual statutes (such as the BetrVG) and labour court judgments (*Richterrecht*).[84] There is a fairly clear division, in both doctrine and practice, between the areas of individual and collective employment law,

[80] S Simitis, 'Juridification of Labor Relations' in G Teubner (ed) *Juridification of Social Spheres* (de Gruyter 1987) 114.

[81] Mehrhoff (n 69).

[82] Zöllner, Loritz and Hergenröder (n 60) 3-4.

[83] ibid 33-34, 44. There can be exceptional situations where an employment relationship is formed by means other than the contract of employment, for example in agency work relationships conducted without a permit.

[84] Zöllner, Loritz and Hergenröder (n 60) 31. Windbichler (n 1) 58.

despite a clear acknowledgment that clean dividing lines are difficult to draw.[85] Subsequent paragraphs loosely adopt this division in setting out relevant provisions, turning first to the individual employment relationship. Organised around the contract of employment, key questions in this area (other than those as to the very existence and classification of a contractual relationship) include the mutual duties of the parties, the modification of general private law (*Zivilrecht*) standards, and the termination of the relationship.[86]

The Individual Dimension: das Arbeitsverhältnis

The employer is the party which can demand and control the employee's efforts.[87] This right of control, based on a contract of employment, is a central component of the *Arbeitsverhältnis*.[88] There are few, if any, requirements beyond the criteria set out above, neither in terms of form nor substance: the contract of employment does not need to be in writing,[89] and the parties can, in principle, agree to any terms.[90] One important set of norms that builds directly on the contract of employment relates to general dismissal protection, as set out in §§ 1-14 of the *Kündigungsschutzgesetz* (KSchG).[91] In order to be 'socially justified', an individual dismissal needs to take

85 Zöllner, Loritz and Hergenröder (n 60) 65.

86 ibid 124.

87 J Bauer and D Herzberg, 'Arbeitsrechtliche Probleme in Konzernen mit Matrixstrukturen' (2011) 28 NZA 713.

88 U Preis, *Erfurter Kommentar zum Arbeitsrecht* (11th edn Beck 2011) §611 BGB rn 233.

89 Zöllner, Loritz and Hergenröder (n 60) 137, citing M Kliemt, *Formerfordernisse im Arbeitsverhältnis* (Müller 1998).

90 S Morgenroth, 'Employment Contracts and Further Legal Sources' in J Kirchner, P Kremp and M Magotsch (eds), *Key Aspects of German Employment and Labour Law* (Springer Verlag 2010).

91 Zöllner, Loritz and Hergenröder (n 60) 279.

place on the basis of a specific range of reasons[92] (the 'positive reasons') and must not contravene a further set of 'negative reasons', including previously agreed selection criteria, the existence of other employment opportunities, and selection according to social criteria. [93]

The Collective Dimension: Mitbestimmung

The fundamental idea underpinning this area is that stakeholders affected by an entity's decision should have a voice in the process leading up to it. While an involvement of all groups potentially affected by a company's actions would be impossible, German law has recognised employees' special role through a system of involvement in company decision-making. Whilst the advantages (including additional perspectives, control and explanation mechanisms, and the legitimisation of decisions through proper procedures) and disadvantages (notably the expense, administrative effort, and supposed inefficiency of a highly complex system) have been discussed at length, a general consensus seems to have emerged that positive factors outweigh negative ones. [94] In the context of corporations, two kinds of employee involvement mechanisms are of interest: works councils, created under the provisions of the BetrVG as a mechanism of co-decision 'from below', and the representation of employee representatives on the company's board under the *Mitbestimmungsgesetz* 1976 (MitbestG) as an example of co-determination 'from above'. [95] The notion of the employer is broken down into a distinction between two units: the *Betrieb* and the *Unternehmen*. The line is an inherently difficult one to draw

92 §1II and III KSchG.

93 Kirchner, Kremp and Magotsch (n 58) 5-7.

94 Zöllner, Loritz and Hergenröder (n 60) 456.

95 Kirchner, Kremp and Magotsch (n 58).

– indeed, it has in this regard been compared to the very notion of the *Arbeitnehmer* itself.[96] Whilst both are organisational units within the enterprise, the aims pursued are different: the *Betrieb* focuses on specific, task-related aims; the *Unternehmen*, on the other hand, on the enterprise's broader economic goals.[97] The former is a factual unit, with only the latter having legal personality (*Rechtssubjekt*). The distinction follows from a (legal) doctrinal framing of (economic) business realities, looking at the level at which decisions are taken. In deciding to which level to attribute particular decisions, the primary focus is on the relative proximity to either area.[98]

The Works Constitution: Betriebsverfassung

Turning first to the *Betrieb*-level, co-decision here takes place via the *Betriebsrat* (works council) as an independent organ of the *Betriebsverfassung* (works constitution), as regulated by the BetrVG. The purpose of its provisions is to ensure the organisational involvement of employees in key questions at the works level, as well as the protection and fostering of individual employees. These aims play an important role both in the interpretation of BetrVG norms, but also in guiding worker representatives when participating in individual decisions.[99]

The central institution of the works constitution is the *Betriebsrat*. An odd number of members are elected for four-year terms from amongst the *Betrieb*-employees, depending on the overall size of the unit. [100] Whilst technically independent from trade

96 U Preis, 'Legimitation und Grenzen des Betriebsbegriffs im Arbeitsrecht' (2000) 52 RdA 257.

97 Zöllner, Loritz and Hergenröder (n 60) 458-9.

98 D Joost, *Betrieb und Unternehmen als Grundbegriffe im Arbeitsrecht* (Beck 1988).

99 Zöllner, Loritz and Hergenröder (n 60) 461; M Heinze and A Söllner, *Arbeitsrecht in der Bewährung : Festschrift für Otto Rudolf Kissel* (Beck 1994) 1269.

100 §9 BetrVG.

unions, there will in reality be a significant overlap between members of the works council and trade union representatives.[101] The BetrVG specifies that the works council's interlocutor be the employer, which, in the absence of contrary legislative provisions is the contractual counterparty of the works employees. The employer can however nominate representatives for such negotiations,[102] as long as they are fit for the purpose (eg by being in possession of specific knowledge as regards the topics under discussion).[103]

The wide range of information, consultation and participation rights accorded to the works council by the BetrVG can be divided into specific and general duties. As regards the former, there are three main areas: social (§87ff), personnel (§92ff) and economic matters (§106ff). The majority of the works council's day-to-day work is on social and personnel topics, such as on working conditions, or the inception and termination of individual employment relationships.[104] There is however also scope for involvement in important one-off events, such as significant changes to the *Betrieb* itself.[105] The employer must inform the works council of such plans, consult on the parties' different interests[106] and conclude a social plan to compensate for, or at least mitigate, the resulting economic disadvantages.[107] A range of fundamental principles including faithful cooperation, a duty to ensure the welfare of both workers and the

[101] Kirchner, Kremp and Magotsch (n 58) 59.

[102] M Franzen, *Gemeinschaftskommentar zum Betriebsverfassungsgesetz: GK-BetrVG* (9th edn Beck 2010) §1rn 91.

[103] BAG decision of 11.12.1991, AP Nr. 2 zu §90 BetrVG 1972.

[104] Zöllner, Loritz and Hergenröder (n 60) 477.

[105] §111 BetrVG; Kirchner, Kremp and Magotsch (n 58) 220ff.

[106] §112 BetrVG ('Interessensausgleich').

[107] §112, 112a BetrVG. See further C Gillen and O Vahle, 'Personalabbau und Betriebsänderung' (2005) 22 NZA 1385, 1391.

Betrieb[108] and strict neutrality[109] guide the works council's efforts. Whilst the detailed procedural apparatus is beyond the scope of the present discussion, it is important to note at this point the possibility of several works councils coming together in the formation of a *Gesamtbetriebsrat*[110] and even a *Konzernbetriebsrat*.[111] The general rules for and duties of these bodies are to be interpreted in accordance with the system just set out.[112]

Co-Determination: Unternehmerische Mitbestimmung

In the second area under consideration, employees are directly involved in entrepreneurial decisions taken at the level of the undertaking. There are two key differences to be noted. First, as regards the institutional setup of co-decision, the entity in question is no longer specific to employee issues; worker representatives participate directly in a company organ. Indeed, this explains why co-determination is situated at the intersection of company and employment law.[113] The second shift is one in purpose: to involve employees in a high-level determination of all commercial decisions, rather than issues related to a specific *Betrieb*.[114] Whilst both the legal and

[108] §§2I and 74I BetrVG.

[109] § 75I BetrVG; Zöllner, Loritz and Hergenröder (n 60) 469ff.

[110] §47 BetrVG.

[111] §§54, 55 BetrVG.

[112] E Salamon, 'Die Konzernbetriebsvereinbarung beim Betriebsübergang' (2009) 26 NZA 471.

[113] As shown by treatment in key texts in both areas: Zöllner, Loritz and Hergenröder (n 60) §53 ('Mitbestimmung in Unternehmensorganen'); Emmerich and Habersack, *Konzernrecht* (9th edn Beck 2008) §4.V ('Mitbestimmung im Konzern). The following paragraphs draw on accounts given there. See also Kirchner, Kremp and Magotsch (n 58) 308.

[114] Zöllner, Loritz and Hergenröder (n 60) 567.

economic merits of this approach are hotly debated in domestic and international literature,[115] such questions are beyond the scope of the present discussion.

Which of the three models of co-determination available under German law applies in any given situation is determined by the industry, size and legal form of an undertaking. As explained in the introductory paragraphs, the provisions to be discussed in this chapter are taken from the *Mitbestimmungsgesetz*, which is applicable to companies with more than 2000 employees, covering all industries and including (*inter al*) both AGs and GmbHs.

Co-determination is exercised by elected employee representatives,[116] who hold the same number (one half of 12, 16 or 20, depending on company size) of seats on the supervisory board as shareholder representatives.[117] If the company's legal structure does not mandate the existence of a separate supervisory entity (eg in the case of a GmbH), a board is to be formed for co-determination purposes.[118] Employee representatives are thus involved in all decisions within the powers of the co-decided board.[119] Whilst the distribution of board seats suggests exact parity between employee and shareholder representatives, a complex set of voting arrangements avoids deadlocks: by allocating an additional vote to the board's presiding member

[115] ibid 573; More generally: J Rogers and W Streeck (eds), *Works Councils: Consultation, Representation, and Cooperation in Industrial Relations* (University of Chicago Press 1995).

[116] Chosen through a highly complex election system: §9ff MitbestG.

[117] §7 MitbestG.

[118] §§6I, 7I MibestG.

[119] This is dependent on the nature of the Company, there being slightly more powers in an AG as opposed to a GmbH.

(who will usually have been chosen by the shareholders[120]) following an initial draw, the latter will prevail in case of conflict.[121]

SECTION III: THE SHARED EXERCISE OF EMPLOYER FUNCTIONS

The notion of the employer thus set out is not immune to variations.[122] One set of such challenges that has become frequently discussed is a split of employer functions.[123] Whilst the label suggests a unified series of problems, there are in fact several groups of issues: the joint involvement of different kinds of employees, of different kinds of employers, and the utilisation of labour by parties other than the contractual employer. In rare circumstances, this split of employer functions can lead to certain employee rights becoming enforceable against third parties, both via contract and other legal constructions.[124] There is, however, no such thing as a purely functional notion of the employer in German law.[125]

One particularly frequent instance of the phenomenon is agency work, initially legalised in 1972, and liberalised by the *Arbeitnehmerüberlassungsgesetz 2003* (AÜG).[126] In this context, the contractual set-up is directly regulated by statute: a

120 §27II MitbestG.

121 §29II MitbestG. The procedures for electing executive officers differ slightly.

122 H Konzen, 'Arbeitsrechtliche Drittbeziehungen: Gedanken über Grundlagen und Wirkungen der "Gespaltenen Arbeitgeberstellung"' (1982) 13 ZfA 259.

123 Zöllner, Loritz and Hergenröder (n 60) 306ff.

124 ibid 307.

125 ibid 45.

126 M Lembke, 'Neue Rechte von Leiharbeitnehmern gegenüber Entleihern' (2011) 28 NZA 319, 320: amendments in line with Directive (EC) 104/2008 of the European Parliament and of the Council of 19 November 2008 on temporary agency work OJ L327/9 will not lead to a substantive redesign. The separate statutory regulation means that the treatment of triangular agency work situations is of little comparative relevance for present purposes.

contract of employment exists between the agency and the worker; the client end-user's control rights are heavily circumscribed.[127]

SUB-SECTION 1: THE *KONZERN*

The *Konzern*, however, is the most appropriate context in which to explore the split of employer functions in multilateral organisational settings. The fundamental idea underpinning this notion is that a company under the controlling power of another enterprise will deviate from the independent control over its business, the concept on which much of company law is premised.[128] As the external entity's influence is organised through company law measures (as opposed to supply contracts, for example) it will be consistently strong and reasonably permanent,[129] giving the parent company control that can range from a direct exercise of key management functions to a more general influence on the broader setting and direction of stakeholder relationships. The relationships between Private Equity management companies and portfolio companies in German law are a clear example of such setups.[130]

Given the high density of corporate groupings in Germany, it is unsurprising that a specific legal approach to these issues has developed in German law: it knows of *Konzernrecht*[131] as a distinct subset of company law. Despite the *Konzern* label, this area of the law focuses on a wide range of connections between companies, with the *Konzern* as the closest form of integration (short of a fusion) at its very core in §18 of

[127] Kirchner, Kremp and Magotsch (n 58) 47-49.

[128] §76IAktG.

[129] This is sometimes questioned in the context of franchising or just-in-time contracts.

[130] R Schmidt and G Spindler, *Finanzinvestoren aus Ökonomischer und Juristischer Perspektive* (Nomos 2008) 139ff.

[131] Emmerich and Habersack (n 113) §1ff.

the *Aktiengesetz* 1965 (AktG). There is no single code or law regulating the area; judicial pronouncements have played a significant role in developing the law both in terms of substance and scope. As regards the former, for example, new doctrines addressing specific problems not explicitly considered by the legislature remedied judicially recognised issues.[132] As regards the latter, there is nothing in the *Gesetz betreffend die Gesellschaften mit beschränkter Haftung* 1892 (GmbHG; the law regulating one of two major company form found in German law, as explained below) mirroring the *Konzern*-specific considerations of the *AktG*; the BGH (Federal Supreme Court) nonetheless developed the application of relevant rules in parallel.[133] In the context of this parallel development, it may be appropriate to briefly address the distinction between the *Aktiengesellschaft* (AG) and the *Gesellschaft mit beschränkter Haftung* (GmbH*)* as relevant to subsequent discussion: there is a wide range of important distinctions between the two forms as organisational models of business enterprise. For the purposes of this chapter, however, these will frequently be negligible, as a similar purpose is pursued. As has already been seen, for example, the range of substantive co-determination powers differ depending on whether a company is organised as an AG or a GmbH. The underlying principle, on the other hand, is the same: employee representatives can get involved in the same range of topics as owner representatives.

The following section now turns to a brief exposition of the technical construction of the legal notion of the *Konzern* in German company law, the universality of its application across different legal areas, and an outline of the specific (economic)

[132] eg the notion of Existenzvernichtungshaftung (liability for destroying the very existence of an entity), developed in the BGH decision of 17.09.2001, II ZR 378/99 (*Bremer Vulkan*); BGH decision of 16.07.2007, II ZR 3/04 (*Trihotel*).

[133] Especially in its second *Senat Zivil* chamber.

problems arising from connected companies as a key to the purposes of (legal) regulatory measures in the *Konzern*-context.

It is crucial to clarify at the outset that the economic unity inherent in the *Konzern* as an enterprise organisational model does not have a general impact on the law's perception of the corporate grouping: as Windbichler notes, 'there is no such thing as the *Konzern* as a subject, for example as a legal person'. [134] Limited exceptions, for example in the area of group accounting,[135] should not be interpreted as moves in a contrary direction.

SUB-SECTION 2: §18 AKTG FF

§18 AktG sets out the criteria for the *Konzern* as the closest possible connection between legally distinct corporate entities. Different kinds of the wide economic variety of company group arrangements are envisaged by §18, depending on the relative relationship between the companies: §18I applies to situations where the relationship is one of subordination; §18II where they are equal.

§18, however, is not a free-standing provision, building instead on a set of criteria and presumptions laid down in §15 to §17 AktG.[136] Two criteria are usually identified for a subordinated *Konzern*: there must be connected undertakings (in the sense of §15 and §17 AktG), brought together[137] under the unified control of one of the shareholder companies. The application of each of these elements on the facts of a particular grouping can be contentious, which explains the intricate cascade of control,

[134] Windbichler (n 1) 14: '*Den Konzern als Rechtssubjekt, etwa als juristische Person, gibt es nicht.*'

[135] *Konzern-Rechnungslegung*: §290ff, esp. §297III 1 *Handelsgesetzbuch* 1897.

[136] Emmerich and Habersack (n 113) 57

[137] This is on (rare) occasion suggested to be an independent criterion.

dependency and *Konzern* presumptions – irrebuttable in case of contractual or integration arrangements;[138] rebuttable (with a very high threshold, however[139]) for other kinds of dependency.[140] In essence, as Emmerich and Habersack note,[141] unified control in §18 is actual control in the sense of §17AktG, which will always be applicable in the case of of majority shareholdings.[142] How this control, based on general company law rights, is exercised (or indeed whether it is exercised at all) is of little relevance for the existence of the *Konzern*.[143]

Within the category of subordinated groups (*Unterordnungskonzern*), one further division should be noted: that between the *Vertrags-* or *Eingliederungskonzern* (corporate grouping by contract or integration) and the *Faktischer Konzern* (de facto corporate grouping). In the former, unified control is based on one of the contracts mentioned in §18I 2 AktG, that is to say, either a *Beherrschungs- und Gewinnabführungsvertrag*[144] or an *Eingliederungsvertag*.[145] If one of these contracts has been concluded, §18I 3 decrees a rebuttable presumption of *Vertragskonzern*.[146] In the latter, unified control is the result of other arrangements, from majority

[138] §18I 2 AktG.

[139] Kort (n 55) 466.

[140] §18I 3 AktG.

[141] Emmerich and Habersack (n 113) 59.

[142] §17II AktG.

[143] LG Oldenburg decision of 14.03.1991, ZIP (1992) 1632, 1636.

[144] §291 AktG: contract of control and profit redistribution.

[145] §319 AktG: integration contract.

[146] R Richardi and others, *Betriebsverfassungsgesetz: BetrVG* (10th edn Beck 2006) §54 rn 8.

shareholdings to vote control contracts. All that matters in this regard is the possibility to enforce the implementation of parent entity decisions. [147]

In summary, then, the *Unterordnungskonzern* requires a relationship of subordination and the real control of dependent companies through unified direction. [148] For the first criterion, the mere possibility of control, directly or indirectly, is enough; it will be presumed for example in the case of a majority shareholding (§17II AktG). This control will usually be exercised, though it is again (§18I 3) presumed unless rebutted. Unified direction, finally, can come from the majority shareholder, integration, contractual arrangements or de facto subordination. [149]

In spite of these sophisticated arrangements, the notion of the *Konzern* does not serve as a gateway into a wide range of regulatory regimes. [150] Crucially for present purposes, however, the two key provisions to be discussed make direct reference to §18 *AktG*: §5 MitbestG (on *Unternehmerische Mitbestimmung im Konzern*), and §54 BetrVG (on the *Konzernbetriebsrat*).

SUB-SECTION 3: A SINGLE NOTION?

Given the generally purposive approach to the interpretation of statutory norms in German law, [151] and the distinct regulatory aims in company and employment law, the

[147] BAG decision of 22.11.1995, (1996) 13 NZA 706.

[148] BAG decision of 16.08.1995, (1996) 13 NZA 274.

[149] B Schwab, 'Der Konzernbetriebsrat – Seine Rechtsstellung und Zuständigkeit' (2007) 24 NZA 337, 338.

[150] Indeed, Emmerich and Habersack (n 113) 63 note its primary importance as a gateway to the MitbestG.

[151] Windbichler (n 1) 48, 50.

question has arisen whether the notion of the *Konzern* applies equally across these contexts. In the context of §5 MitbestG, this question has been the subject of recent litigation.[152] As Kort notes, however, given the existence of co-determination within company law, the references in §54ff BetrVG to §18I are to be understood in the company law sense; the §15/16/17/18I AktG definition and presumption cascades apply in full. [153] He goes on to dismiss suggestions that contractual control outside company law tools could suffice to fulfil the *Konzern* presumptions; such setups are admitted only in the context of, for example, minority shareholdings.[154] Once within the company law framework, however, there is no need for the actual exercise of unified control power: the arrangement itself suffices.[155] How control is exercised in reality is equally irrelevant; there is no need to give actual orders.[156]

The picture is slightly more difficult in the context of §54 BetrVG:[157] it is an employment law norm, but makes direct reference to the (company law concept of) subordination *Konzern* in §18I AktG.[158] The Federal Labour Court has held that for the existence of a *Konzern* under §54 BetrVG, the legal form of controlling and subordinate enterprise are irrelevant – even a natural person as head entity would come under its provisions, lest the co-decision duties be voided of significance.[159] In

[152] Discussed in Kort (n 31).

[153] ibid 82; Windbichler (n 1) 518.

[154] cf Windblicher (n 1) 519.

[155] K Hopt and H Wiedemann, *Großkommentar Aktiengesetz* (4th edn de Gruyter 1999) §18 rn 29, 32.

[156] U Hüffer, *Aktiengesetz* (8th ed Beck 2008) §18 rn 12.

[157] Schwab (n 149).

[158] BAG decision of 22.11.1995 (n 147).

[159] ibid; BAG decision of 05.05.1988, (1989) 6 NZA 8.

a recent decision,[160] the BAG affirmed that there was no independent notion of the *Konzern* in the BetrVG, and that in applying its provisions the company law definition of subordination mattered.[161] The court left it open, however, whether in exceptional circumstances subordination may also be found beyond the realm of company law. While the BGH had in the past emphasised this limitation as a way of avoiding deep intrusions into the market economy, it had done so specifically in the context of company law. [162] The BAG, on the other hand, had focussed on the possibility of subordination, regardless of means;[163] the academic literature was divided.[164] The desire for legal coherence and certainty could in certain individual cases be outweighed by a need to ensure effective co-decision when required, especially given the legislative aim that a *Konzern-Betriebsrat* should counteract impairments to worker participation resulting from factual and legal external control opportunities.[165] Bäck and Winzer make two important points about these guidelines.[166] They note, first, the high threshold to prove control outside of company law structures: it would not suffice, for example, if such powers were temporary, or partial. They note furthermore that whilst the judgment denies the existence of co-decision mechanisms within broad functional groups, it does clearly confirm the existence of a

[160] BAG decision of 09.02.2011, (2011) 28 NZA 866.

[161] BAG decision of 27.10.2010, (2011) 28 NZA 524.

[162] BGH decision of 26.03.1984, (90) BGHZ 381.

[163] BAG decision of 30.10.1986, AP BetrVG 1972 §55 Nr 1.

[164] ibid [27].

[165] BAG decision of 27.10.2010 (n 161); BAG decision of 13.10.2004, (2005) 22 NZA 647 [30].

[166] U Bäck and T Winzer, 'BAG: Konzernbetriebsrat – Möglichkeit eines Spartenkonzern-betriebsrats?' (2011) 38 NZG 944.

Konzernrecht doctrine, the so-called *Konzern im Konzern*,[167] in employment law, despite its very contentious position in company law.

SUB-SECTION 4: THE PURPOSE OF *KONZERNRECHT*

German law thus gives special recognition to the *Konzern* as a particular model of economic organisation. In concluding, the question should briefly be asked why this is the case, especially as the answer may provide clues as to the general aims and purpose of *Konzernrecht*. The specific recognition, it is frequently suggested, is due to both the advantages and dangers inherent in the *Konzern* model. Turning first to the advantages of economic integration,[168] there are significant efficiency gains from the coordinated approach of multiple entities, with an increase in overall size leading to additional economies of scale. In bringing these advantages about without complete integration, a wide range of stakeholders can benefit: shareholders and customers receive a share in the resulting surplus, creditors benefit from specific capital allocation,[169] and even employees may see advantages in working for a large *Konzern* instead of an individual company.[170] These advantages, however, face an equally important list of countervailing factors.[171]

The general provisions of German company law are designed around the assumption of a collective action problem amongst shareholders: given the high cost

[167] A model where a subordinate company still has relevant control over subordinates in lower tiers: BAG decision of 14.02.2007 (n 61).

[168] For an extensive overview, see K Martens, 'Grundlagen des Konzernarbeitsrechts' (1984) 12 ZGR 417.

[169] H Hansmann and R Kraakman, 'The Essential Role of Organizational Law' (2000) 110 Yale Law Journal 387.

[170] Windbichler (n 1) 41.

[171] Emmerich and Habersack (n 113) 10-11. For an extensive list, see Windbichler (n 1) 40.

of individual shareholder control whilst benefits would be spread widely, an undertaking's management is independent. The same is not true for subordinated companies in the *Konzern*; the balanced system of the AktG is thus thrown out of kilter once a single entity manages to exert pressure in its own interest on the administrative organs of another – indeed, this influence can go as far as the pursuit of aims directly contrary to those of other shareholders, creditors, and even the company itself.[172] *Konzernrecht* maps itself onto these issues by developing detailed rules[173] to protect the various parties identified and provide clear boundaries as to when and how concentration can be achieved. It is against this background that the purpose of separate *Konzernrecht* rules becomes clear: [174] they provide the necessary *organisational* framework for deep changes in enterprise structure, thus facilitating the concentration of control powers, while at the same time *protecting* minority shareholders, creditors, and even the subordinated entity and shareholders in the parent company itself.

SECTION IV: *ARBEITSRECHT IM KONZERN*

Discussion thus turns to employment law in the corporate group, to set out and analyse examples of specific modifications to the general framework which have taken the *Konzern*-context into account in shaping their regulatory design. A linguistic point should be noted at the outset: whilst the topic under scrutiny was historically discussed under the label of *Konzernarbeitsrecht* (corporate group employment

[172] See ibid for examples.

[173] See eg §291AktG ff. A detailed analysis of their operation is beyond the scope of the present discussion.

[174] Hüffer (n 156) §15 rn 3.

law),[175] it has become clear today that the questions are more appropriately framed as concerning *Arbeitsrecht im Konzern* (employment law in corporate groups). This is notably reflected in the title of the first,[176] and to date only, comprehensive investigation of all related phenomena in this *terra icognita*.[177]

The question as to the *patron introuvable* in the corporate group context can only be answered within the existing frameworks of employment and company law, which explains a methodology that focuses on problems and solutions specific to the form instead of attempting a complete restatement of employment law for corporate groups. The first point that arises is that as to the difference between employment in an independent company, and one subordinated to others in a *Konzern*: does the structural difference lead to changes in risk profile? Being embedded in a group structure influences a company in general – but does it also influence the company as an employer in particular? This point matters as regards the joint or shared exercise of employer functions, but is equally important even in the absence of such arrangements, given the general influence of another entity over the employment company.

It has already been seen that company law reacts to the *Konzern* with a range of general stakeholder-protective mechanisms. As Konzen has noted,[178] there can only be an employment law specific extension of such protection if there is a 'hole in the regulatory regime' (*Regelungslücke*), ie if employees are sufficiently different from other stakeholders, such as creditors. Discussion thus turns to a brief comparison of

[175] The term used in Martens (n 168). Early topics included the application of the contract of employment, the *Betriebsbedingte Kündigung*, and, after the *BetrVG* of 1972 the possibility of creating a *Konzern*-Works Council.

[176] Windbichler (n 1).

[177] BAG decision of 18.10.1976, AP Nr 3 §1KSchG 1969.

[178] H Konzen, 'Arbeitnehmerschutz im Konzern' (1984) 36 RdA 65, 66.

these groups,[179] focussing on the interests of employees other than as wage creditors.[180]

At a first glance, both groups will share a primary interest in the solvency of the company, thus benefitting equally from a range of measures designed to protect the daughter company.[181] Henssler[182] suggests that a first difference may arise from the possibility that whilst the fruits of the employees' labour can easily be whisked away to solvent controlling companies, reciprocal employer obligations will remain in a lightly capitalised lower entity. This danger, however, is equally applicable to general creditors' contributions to the firm.[183]

Upon further consideration, however, it emerges that employees have a much stronger interest in the protection of the employing company's 'economic individuality' and on-going existence because of their *existentielle Wirtschaftsabhängigkeit* (existence-critical economic dependence).[184] Individual *Konzernrecht* measures do of course protect the subordinated company to a certain extent; it is however doubtful whether this will always see creditor and employee interests aligned. Indeed, it is not difficult to imagine a situation where the protection of the enterprise as such could lead to the dismissal of workers in order to lower wage expenditure.

[179] Windbichler (n 1) 29-42. This difficulty and importance of the right choice of comparator will matter throughout the evaluative exercise to follow: Martens (n 168) 423ff.

[180] Employees can claim first priority as wage creditors: H Staab, 'Der Arbeitnehmer-Gesellschafter der GmbH im Spannungseld zwischen Arbeitnehmerschutz und gesellschaftsrechtlichem Glaeubigerschutz' (1995) 12 NZA 608.

[181] Windbichler (n 1) 32-33: indirect creditor protection ('Schadenersatz, Nachteils- und Verlustausgleich').

[182] ibid 59.

[183] H Konzen, 'Arbeitsverhältnisse im Konzern' (1987) 151 ZHR 566, 572.

[184] H Wiedemann, *Die Unternehmensgruppe im Privatrecht* (Mohr Siebeck 1988) 97, 108.

Having reviewed these comparisons as well as the relevant economic and legal literature, Windbichler concludes that there are three *Konzern*-specific threats to employees: [185] decisions taken outside of co-decision mechanisms; detrimental influence,[186] and the closure of independently viable economic units. Unsurprisingly there is no one, singular and clear solution to all these issues; the individual approaches will now be explored in turn. It will emerge that while there is little response in terms of individual employment law (other than in exceptional circumstances, which will frequently be highly fact-specific), a broad range of firm regulatory responses can be observed in the collective domain.

SUB-SECTION 1: INDIVIDUAL EMPLOYMENT LAW

As has already been noted, there is no general scope for seeing the *Konzern* as a contractual employer under German law. [187] The following sections analyse this position, as well as criticisms of the approach, before turning to other potential solutions such as piercing the corporate veil.[188] Finally, the scope of unfair dismissal protection mechanisms will be tested in the *Konzern* context. Despite some potential avenues and small modifications the answer there will again be negative,[189] unless additional external factors prevail. [190] The range of solutions introduced in the

185 Windbichler (n 1) 42.

186 '*Nachteilige Einflussnahme'*.

187 T Liebscher, *Münchener Kommentar zum Gesetz betreffend die Gesellschaften mit beschränkter Haftung - GmbHG* (Beck 2010) rn 1100, drawing on Windbichler (n 1) 69. There is a possibility of exceptional contracts for senior management and sending employees across units: 1113, 1112.

188 BAG decision of 14.12.2004, (2005) 22 NZA 697. The only possible routes are outside employment law, for example in the law of delict ('*Existenzvernichtungshaftung'*).

189 See eg most recently BAG decision of 23.03.2006, (2007) 24 NZA 30.

190 For example '*Vertrauensgesichtspunkte'*: see eg BAG decision of 27.11.1991, (1992) 9 NZA 644 and potentially where the group parent actually runs the *Betrieb* in question: R Richardi, *Münchener Handbuch zum Arbeitsrecht* (Beck 2009) §32 rn 33.

collective dimension (or even as regards triangular agency employment relationships) have no formative impact on the individual dimension.

The Contract of Employment

As Windbichler points out, there is a real danger of incongruence between contractual and *de facto* risk allocation in situations where the close connection of the contractual employer to other undertakings directly influences the individual employment relationship.[191] This does not mean, however, that the *Konzern* can somehow become a singular legal entity, and thus a contractual counterparty.[192]

Various attempts to remedy the resulting incongruence draw on a range of 'exceptional' contractual approaches, for example by suggesting a unified employment relationship involving multiple employers, or multiple connected employment relationships.[193] The advantage of such analyses lies in the fact that all non-wage taking parties to the relationship(s) would become subject to the duties placed on employers. The key problem, however, is that for such a relationship to come about, all parties must have taken active steps towards it, which will be rare in reality.[194] Similar considerations speak against a range of related solutions proposed, for example, by Heinze, Fabricius and Müllner.[195] As the BAG has repeatedly and

[191] Windbichler (n 1) 166.

[192] ibid 70, 202ff.

[193] ibid 71: '*einheitliches Arbeitsverhältnis'*.

[194] ibid 79.

[195] M Heinze, 'Rechtsprobleme des sog. echten Leiharbeitsverhältnisses' (1976) 7 ZfA 183, 205; F Fabricius, *Rechtsprobleme gespaltener Arbeitsverhältnisse im Konzern: Dargestellt am Rechtsverhältnis der Ruhrkohle Aktiengesellschaft zu ihren Betriebsführungsgesellschaften* (Luchterhand 1982) 40; W Müllner, *Aufgespaltene Arbeitgeberstellung und Betriebsverfassungsrecht* (Duncker & Humblot 1978) 62.

consistently found, external influence alone cannot suffice for the construction of an employment relationship with the third entity.[196]

Another potential model is that of a partial employer position, for example by identifying the party who reaps the economic benefit of the workers' efforts, and/or can offer the best levels of social protection.[197] In the *Konzern* setting, the controlling entity could be such a partial employer;[198] again, however, the mere exercise of certain rights cannot suffice *ipso facto* to create to an employment relationship.[199]

Dismissal Protection: the **Kündigungsschutzgesetz**

Turning from the very existence of the contract of employment to regulatory frameworks in the individual employment law dimension that build directly upon it, unfair dismissal protection is an interesting further illustration of attempts to infuse individual employment law with the notion of the *Konzern*.

The power to terminate an employment relationship under the KSchG lies firmly with the contractual counterparty. The *Konzern*-dimension can nonetheless give rise to two sets of questions in the dismissal context: first, as to the role of entity-external pressure exerted by other group companies; and second, as to the significance of a subordinated company's relationships with other group members in the application of the various protective steps mandated by the KSchG (especially as regards the social

[196] BAG decision of 08.08.1958, AP Nr. 3 §611 BGB; BAG decision of 26.11.1975, AP Nr 19 §611 BGB; cf BAG decision of 04.07.1979, AP Nr 10 §611 BGB (*Rotes Kreuz*); M Henssler, *Der Arbeitsvertrag im Konzern* (Duncker & Humblot 1983) 58, 66.

[197] T Ramm, 'Die Aufspaltung der Arbeitgeberfunktionen (Leiharbeitsverhältnis, mittelbares Arbeitsverhältnis, Arbeitnehmerüberlassung und Gesamthafenarbeitsverhältnis)' (1973) 4 ZfA 263.

[198] Windbichler (n 1) 80.

[199] Windbichler (n 1) 79.

selection process, and the possibility of continuing employment in different functions).[200]

The answer to the former question appears settled: even if an explicit shareholder order led to the termination, it will be effective as long as the dismissal is otherwise correct.[201] Put differently, the source of the dismissal decision in such a *Druckkündigung* is not an important consideration in the light of other procedural criteria. Turning to the latter point, there is no general *Konzern*-dimension to dismissal protection.[202] This is because each *Konzern-Unternehmen* is a legally independent employer; the KschG norms attach directly to the contract of employment.[203] In the case of social selection, the relevant unit is the even smaller *Betrieb*, thus denying any broader interpretation.[204] As regards the possibility of continuing employment, the reference unit was traditionally understood to be each individual company,[205] rather than the larger corporate group.[206] The *Rheumaklinik* judgment of 2002 created considerably uncertainty on this last point:[207] while the overall position remains unclear, a spectacular extension seems unlikely.[208]

[200] §1 KSchG.

[201] Windbichler (n 1) 252: '*Druckkündigung*'. BAG decision of 10.02.1977, AP Nr 8 §103 BetrVG 1972 bl 4.

[202] BAG decision of 13.06.2002, (2002) 19 NZA 1175.

[203] BAG decision of 14.10.1982, (1984) NJW 381.

[204] Bauer and Herzberg (n 87) 716.

[205] BAG decision of 23.04.2008, (2008) 25 NZA 939.

[206] M Henssler, *Münchener Kommentar zum Bürgerlichen Gesetzbuch: BGB. Band 4: Schuldrecht* (6th edn Beck 2012) KSchG§1 rz 278.

[207] *Rheumaklinik* (n 66); noted G Annuß, 'Die rechtsmissbräuchliche Unternehmerentscheidung im Konzern' (2003) 20 NZA 783.

[208] Bauer and Herzberg (n 87) 785.

The only clear set of exceptions, on the other hand, fits into the pattern that has already begun to emerge: the *Konzern*-Dimension only becomes relevant if entities other than the contractual employer have taken additional steps in that direction,[209] from explicit contractual promises to conduct giving rise to legitimate expectations via the contractual employer.[210]

In summary, the identity of the employment relationship is determined by the contractual parties to it. As the *Konzern* lacks legal personality, it can therefore not be an employer. In exceptional circumstances a third party may become legally involved with the employment relationship.[211] Such circumstances would, however, be highly fact specific; requiring at the very least specific third party interventions into the employment relationship, rather than being based on control over the contractual counterparty more generally. As Windbichler concludes, 'the individual dimension of employment law [therefore] remains firmly independent of the legal and economic organisation of the employer, its entrepreneurial goals and choices.'[212]

SUB-SECTION 2: *BETRIEBSVERFASSUNG* (§54FF BETRVG)[213]

Discussion thus moves into the collective dimension, beginning with the *Betriebsverfassungsgesetz* as one of the few labour law regimes that explicitly take the *Konzern* dimension into account.[214]

[209] BAG decision of 23.11.2004, (2005) 22 NZA 929.

[210] Bauer and Herzberg (n 87) 713: '*Vertrauenstatbestand*'.

[211] For example by signing additional contractual agreements.

[212] Windbichler (n 1) 585: *'Individualarbeitsrecht ist grundsätzlich unabhängig von Rechts- und Finanzierungsform, Unternehmenszweck und –gegenstand des Arbeitgebers.'*

[213] The descriptive elements here build primarily on Zöllner, Loritz and Hergenröder (n 60) 454ff.

[214] Windbichler (n 1) 26.

The logical need for the creation of a *Konzern*-works council (KWC) arises from the fact that different companies within the group will not necessarily form a large, joint *Betrieb*, which would have to consult with a *Gesamtbetriebsrat*.[215] §54 BetrVG thus envisages the (voluntary) creation of a separate body to consult on matters that are of relevance across the entire *Konzern*.[216] It is constituted following an affirmative vote of the *Betriebsräte* representing at least 50% of employees of all *Konzern* companies;[217] this threshold was lowered from 75% in 2001 in order to facilitate and encourage the creation of KWCs. A European works council,[218] if constituted within the same corporate group, exists on a complementary basis – neither regime is exclusive. KWC membership is regulated by §55 BetrVG, in parallel to the provisions for the *Gesamtbetriebsrat*:[219] there is no maximum number of members; each works council sends two representatives who will be subject to the same duties and rights as other works council representatives.[220]

The duties of the KCW are laid out in §58I BetrVG and can be broadly summarised as areas that cannot be meaningfully covered by individual works councils, and those where the *Konzern* situation leads to a mandatory requirement of unified rules across the *Konzern*, or at least the *Unternehmen*. The latter power depends on concrete evidence on the circumstances; a mere desire for efficient

[215] Liebscher (n 187) rn 1098.

[216] §58I BetrVG. This is different from §47 (*Gesamtbetriebsrat*).

[217] As very widely defined: BAG decision of 11.08.1993, AR Blattei ES 530.12.1 nr 5.

[218] Directive (EC) 38/2009 of the European Parliament and of the Council of 6 May 2009 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees [2009] OJL122/28. Given effect in German law by the *Gesetz über Europäische Betriebsräte* 1996.

[219] §47II-VIII BetrVG.

[220] BAG decision of 20.12.1995, (1996) 13 NZA 945.

coordination will not suffice.[221] When it comes to the distribution of powers, §58I *BetrVG* is deliberately designed along the lines of §50 *BetrVG* on the relationship between *Betriebs*- and *Gesamtbetriebsrat*: pursuant to the principle of subsidiarity, each function should be exercised at the lowest level possible.

To illustrate this distribution in each of the three main co-decision areas, for social matters any arrangements will only fall within the ambit of the KWC if their effect reaches across the entire *Konzern*.[222] In the field of personnel matters, the divide will usually mean that the KWC cannot get involved in individual measures (§99ff), focussing instead on matters of general policy and planning across the *Konzern*. In the economic dimension, finally, KWC can only get involved when there is a need for an *Interessensausgleich* or *Sozialplan* on the *Konzern*-level. Despite academic commentary to the contrary, [223] the KWC can furthermore not create a *Wirtschaftsausschuss* pursuant to §106I BetrVG.[224]

In addition to these *inherent* powers, the KWC can also exercise functions delegated to it by the *Gesamtbetriebsrat* (§58II BetrVG), and in turn individual works councils (§50II BetrVG). Its work in this context is conceptually entirely different, however, as one entity merely acts as an agent for another.[225] The difference can be briefly illustrated in the context of *Betriebsvereinbarungen* (works agreements). Whether such agreements could exist on the *Konzern*-level was for a long time

[221] ibid.

[222] BAG decision of 21.56.1979, AP Nr. 1 §87 BetrVG 1972.

[223] W Trittin and others, *BetrVG - Kommentar für die Praxis* (10th edn Bund 2006)§58 rn 37: '*planwidrige Gesetzeslücke'*.

[224] BAG decision of 23.08.1989, (1990) 7 NZA 863.

[225] There is consequently no impact on the notion of the employer: BAG decision of 12.11.1997, (1998) 15 NZA 497.

unclear,[226] until the BAG settled the matter in favour of KWCs, who may now conclude agreements that will apply throughout the corporate group in spite of its legal separation.[227] If negotiations are conducted on the basis of delegated authority, on the other hand, the resulting agreement will only be binding on the individual employer in question.[228]

In concluding, it should be reemphasised that the KWC is an independent entity, neither above nor below other works councils in the works constitution.[229] Similarly, *Betriebsräte* at different levels are not subordinated to each other.[230] Their relative powers, however, are regulated by §58I, and limited to those issues that cannot be meaningfully addressed elsewhere.[231] This cross-entity focus becomes possible because of a shift in regulatory design: the *BetrVG* is based on an organisational and functional model of employee representation: the extent to which works constitution structures can transcend enterprise borders is directly linked to the *Konzern*'s degree of integration.[232] The reverse aspect of this model is that the *Konzern*-dimension has no fundamental impact on whether there should be co-decision on certain matters, or the extent to which it should take place: the set of rights and duties as set out earlier should only be subject to logically required modifications.

[226] K Biedenkopf, 'Konzernbetriebsrat und Konzernbegriff' in P Zonderland (ed) *Liber amicorum Sanders* (Kluwer 1973) 1, 11ff.

[227] BAG decision of 22.01.2002, (2002) 19 NZA 1224.

[228] BAG decision of 12.11.1997 (n 225); Schwab (n 149).

[229] §58I 2 BetrVG.

[230] BAG decision of 12.11.1997 (n 225).

[231] Salamon (n 112) 472.

[232] Windbichler (n 1) 587, 592.

SUB-SECTION 3: *MITBESTIMMUNG* (§5 MITBESTG)

In the already contentious legislative history of the *Mitbestimmungsgesetz*, co-determination's impact on *Konzern*-structures stands out as a particularly controversial area.[233] As the subsequent exposition of three *Konzern*-specific questions will show, this is to a significant extent reflected in the very different goals pursued by the relevant provisions of §§5 and 32 MitbestG.

The first *Konzern*-specific danger under the co-determination provisions is the deliberate use of economic structures by employers trying to avoid the application of the MitbestG:[234] by carving a company up into individual units, employee numbers could artificially fall beneath the relevant thresholds, thus denying any avenue for employee voice on the supervisory board. The provisions in §5 control this danger through a series of attributions:[235] based on the contract of employment, individual workers are counted towards their *Unternehmen*, and in turn tallied up in line with each entity's membership of the corporate group.

From the workers' perspective, the second and arguably more fundamental danger to co-determination in a *Konzern* is as to its very effectiveness. It will be recalled that the MitbestG is designed to provide a system of economic employee co-determination, ie direct involvement in important entrepreneurial decisions.[236] In a chain of externally controlled enterprises, co-determination at the level of the subordinate company will however be of comparatively little value, as decisions are

[233] T Raiser, 'Einleitung' in K Forster and others (eds), *Festschrift für Bruno Kropff. Aktien- und Bilanzrecht* (IDW 1997).

[234] Zöllner, Loritz and Hergenröder (n 60) 575-6

[235] Windbichler (n 1) 590.

[236] BVG decision of 01.03.1979, (1979) NJW 699. As Emmerich and Habersack (n 113) 68 note, the main historic reason for placing this at board level was to ensure employee involvement in the selection of executive officers.

taken elsewhere. By providing that co-determination is to take place at the highest *Konzern*-level, *viz* the *locus* of relevant decision making,[237] the provisions of §5 counteract the potential distortions resulting from group subordination.

Turning to the third *Konzern*-specific issue, it should be noted that attribution of employees under §5I MitbestG does not stop subordinate units from also having co-determination if their employee numbers exceed the threshold.[238] As a result of this cumulative approach, co-determination can end up going further than its proclaimed goal of employee-owner parity:[239] on the board of a large subordinated entity, the shareholder representatives will have to exercise their voting rights as instructed by the parent company board, thus giving effect to the will of both employees and owners as represented there. The fear is that this could result in two problems - employee voice on topics that are purely a matter for the shareholders and an excessive proportion of employee participation overall, as the employee representatives' voting on the subordinated company's supervisory board is not co-determined from above.

As the Federal Constitutional Court has held, in order for co-determination to be in line with the *Grundgesetz*, it must not represent a direct threat to shareholders' interests as the company's owners.[240] Property rights are constitutionally superior, however slightly. Indeed even the choice of co-determination on the supervisory board can be interpreted as a deliberate one is this context, by limiting the scope of co-determined matters primarily to executive officer selection and supervision.[241] It is

[237] This is an *additional locus* of co-determination: Liebscher (n 187) rn 1115.

[238] Emmerich and Habersack (n 113) 73 go as far as describing this setup as 'against the system' ('*systemwidrig*').

[239] Zöllner, Loritz and Hergenröder (n 60) 575-6.

[240] BVG decision of 01.03.1979 (n 236); R Schmidt, 'Das Mitbestimmungsgesetz auf dem verfassungsrechtlichen Prüfstand' (1980) 19 Der Staat 235, 254.

[241] §31 and §25I MitbestG respectively.

therefore important to ensure that co-determination does not take place at the expense of the owners generally, and to avoid employee over-parity (*Überparität*) in particular. §32 MitbestG ensures this protection of shareholders rights, by providing that certain decisions can only be taken by a majority of shareholder representatives on the supervisory board, especially as regards the selection of shareholder representative elections in lower entities, and enterprise contracting.[242]

SECTION V: CONCLUSION

The results of the comparative enquiry in chapter four have been in line with much more extensive German research on the subject:[243] in the individual employment law dimension, *Konzernrecht* does not generally influence the legal fundamentals of the contract of employment.[244] This is a major difference from the *Betriebsverfassungs*- and *Unternehmensmitbestimmungs*-contexts, where provisions such as §54ff BetrVG and *§5* MitbestG operate across legally separate entities. Under the former, a *Konzern*-works council can be created as a separate body to consult on matters that are of relevance across the entire *Konzern*, and would therefore not be captured by consultation obligations on subsidiary units.[245] In the latter context, employee numbers in each subsidiary are attributed to the parent entity through a process of counting individual workers first towards their *Unternehmen*, and then tallying up those numbers in line with each entity's membership of the corporate group. The provisions furthermore ensure that co-determination can take place at the real *locus* of relevant decision making, up to and including the highest *Konzern*-level, thus

[242] §§291, 292 AktG.

[243] Windbichler (n 1) 581ff.

[244] ibid described as group-proof ('*konzernfest'*).

[245] §58I BetrVG.

counteracting the potential distortions resulting from group subordination. Throughout, the economic and legal implications of the *Konzern* grouping are the explanation for when norms have to be adapted, as the impact of structurally inherent and temporally (reasonably) permanent subordination fundamentally changes the relationships between different stakeholder groups.

Having thus seen a cross section of German employment law and tested the extent to which some of its provisions have come to be modified for application in complex corporate structures, the final part of this chapter returns to draw some broader conclusions from the material surveyed in part two, and to note important pointers for the development and evaluation of potential solutions in domestic law. In concluding the previous chapter, three key lessons emerged to guide the eventual reconceptualisation of the notion of the employer in the final part. The results of the comparative analysis confirm and further develop each of these points.

Avoiding Excessive Homogeneity

One of the underlying flaws that was identified as inherent in the received notion of the employer in English law was the assumptions of homogeneity built into it, both as regards the notion itself (ie that it is substantively identical across all different regulatory domains) and the underlying matter to be regulated. German law avoids this to a certain extent, by focussing regulation on particular aspects of complex multilateral relationships. It therefore recognises the *intra-group specificity* of the joint exercise of employer functions, and relies on this observation to distinguish the corporate group or controlling block shareholder scenario from other situations such as dispersed ownership. It is this distinction, furthermore, which is then used to justify and shape a differentiated legal response.

An employing company's membership in a corporate group is not in and of itself an issue that requires legal remedies.[246] The above discussion, on the other hand, has identified a series of particular opportunities and dangers that can arise from such connections, and explored the purpose of various rules in addressing them. The unifying theme throughout was influence or control: the external (corporate) block shareholder has a strong enough impact on all facets of the subordinated enterprise to warrant a departure from standard legal rules.[247] The shared exercise of employer functions is on one end of a *Konzern* spectrum of control and subordination; contracts for partial control (*Teilbeherrschungsverträge*) on the other. Yet, as Däubler has demonstrated,[248] what all points on this spectrum have in common is an underlying lack of truly independent control given concentrated external direction powers. This deviation from the standard model serves both to justify a specific regulatory response in the first place, and explains the reliance on a combination of company and labour law mechanisms to achieve the desired goals.

Towards a Functional Approach

Previous chapters suggested that it is primarily the formalistic, not the multi-functional part of the tension inherent in the notion of the employer that constitutes the problem to be addressed. Germany law has equally come to recognise that the key problem with a formalistic, purely contractual, approach is its vulnerability to changing economic structures; even the presence of a contract of employment does not guarantee full employment law coverage where the exercise of employer functions is shared between or divided up across different entities. The solution to this issue lies

[246] Windbichler (n 1) 592.

[247] Salamon (n 112); Richardo (n 146) §54 rn 4; Vor 54 rn 1.

[248] W Däubler, 'Ausklammerung sozialer und personeller Angelegenheiten aus einem Beherrschungsvertrag' (2005) 32 NZG 617, 619.

in a shift to a functional approach, which must however also be limited carefully in its operation and underpinned by a coherent conceptualisation. The comparative enquiry in this chapter has added a further dimension to this need for limits on any proposed functional reconceptualisation.

First, by recognising that when attempting to modify the notion of the employer in complex multilateral work settings such as corporate groups, the notion can only be modified within the existing frameworks of employment and company law. This requires a methodology that focuses on problems and solutions specific to the form instead of attempting the creation of distinct bodies of employment law. The functional approach, second, must be limited by existing concepts and approaches in neighbouring disciplines. This is clearly illustrated in the individual dimension, where it is very clear that a combination of entities or even the whole group cannot become understood as a single-entity employer. The extension of specific obligations and liabilities to cover additional group companies, on the other hand, ensures a congruent scope of employment law coverage without threatening the fundamental setup of German group company law.

Developing Existing Frameworks

These observations are echoed in the earlier realisation that any change must be logically linked to and take account of its point of departure in order to be successful. One crucial insight from the comparative work in this regard is the idea that a functional approach to the design and interpretation of the notion of the employer can achieve this balance of reconceptualisation and respect for existing structures by relying on a combination of different regulatory methods, driven by the specific regulatory goals in different sub-domains of employment law.

The specific areas where modification of regulatory frameworks could be identified in the comparative work share similar goals: the effective, yet controlled, participation of workers in the management of their employing undertakings. At the same time, however, they rely on very different mechanisms to achieve these goals: §54 BetrVG creates a new entity, the *Konzernbetriebsrat*; §5 MitbestG, on the other hand, adds employee representatives to an existing entity, the worker board representatives at the parent or holding company level. Two distinct regulatory models underlie these differences: one of managerial and one of organisational attachment.[249] A series of further distinctions between the two systems is frequently rehearsed:[250] the BetrVG, for example, is firmly based in labour law, whereas the MitbestG has traditionally been claimed as a domain of company law. The former is limited to the *Betrieb* as the smallest organisational unit possible, and limits consultation to those areas which will have a direct impact on employee's lives; the level of co-decision however is direct and intense. Under the MitbestG, on the other hand, employees may participate in the full range of decisions concerning the undertaking, subject only to the limits on the role of the supervisory board. In return, the level of required cooperation, for example in dealing with a hostile employer, is limited to an advisory function. Neither of these distinctions necessitates a particular regulatory design. A potential answer may however become apparent from a simultaneous consideration of mechanisms and purpose.

The purpose of §54ff BetrVG is to ensure on-going employee participation at relevant levels throughout the company, even if it is within a corporate group structure.[251] The place where this happens is crucial: at the locus of concrete exercise

[249] Windbichler (n 1) 582.

[250] Kort (n 55) 466.

[251] BAG decision of 21.10.1980, (1982) NJW 1303.

of undertaking's control, which can be different according to the measure under consideration. A series of entities (works councils) is therefore created, following this function. This 'functional adaptation'[252] ensures a clear connection to the *Konzern*, whilst remaining flexible depending on the level of group centralisation. At the same time it ensures that the modification does not go further than necessary: [253] there is no impact of the underlying structures of the enterprise.[254]

§5 MitbestG, on the other hand, is aimed at ensuring the institutional attachment of co-determination to the employing organisations.[255] Its technical focus is on the organisational connection to structures rather than individual circumstances. By putting employee representatives on the supervisory board, there is a direct impact on the underlying corporate structure, regardless of the actual exercise of different functions. Windbichler has analysed these differences as a gradation of legal responses to grouped companies, from the execution level (with no *Individualarbeitsrecht* consequences) via an organisational/functional mix (BetrVG) to the purely organisational (MitbestG).[256]

This final insight has an important implication for the subsequent chapter: it will have to survey a wide range of potential techniques that may be used in operationalizing a reconceptualised notion of the employer in English law, and consider in which contexts and combinations they are to be deployed. It is this task to which discussion now turns.

[252] Windbichler (n 1) 582: '*funktionale Anpassung*'.

[253] Kort (n 55).

[254] Konzen (n 178) 68 strongly disagrees. cf Kort (n 55) 465.

[255] W Koberski and others, *Kommentar: Mitbestimmungsrecht* (4th edn Beck 2011) §5 rn 2-3.

[256] Windbichler (n 1); C Windbichler, 'Unternehmerisches Zusammenwirken von Arbeitgebern als arbeitsrechtliches Problem. Eine Skizze auch vor dem Hintergrund der EG-Richtlinie zum Europäischen Betriebsrat in Unternehmensgruppen' (1996) ZfA 1.

PART III
RECONCEPTUALISING THE NOTION OF THE EMPLOYER

The goal of the third and final part of this thesis is to reconceptualise the notion of the employer in response to the problems identified in previous parts. Subsequent chapters will develop and test a new approach in a series of detailed steps; for present purposes it is important to set out a clear overarching goal against which the overall effort may eventually be evaluated. It is suggested that the only way a reconceptualisation can be successful is by addressing the fundamental tension head-on: it is not possible simply to ignore either the unitary or the multi-functional strand, by radically departing from the existing case law, or proposing partial statutory intervention. Indeed, it is in this regard that previous attempts at grappling with the question at hand have struggled. In its place, a careful reconsideration of both functional and unitary aspects will be at the core of subsequent chapters.

Introduction: Recalling Key Lessons

Before turning to this substantive discussion, two preliminary points remain to be made. The first is to recall the three key lessons for a reconceptualisation which became apparent during the case law survey in previous parts, as well as the results of the comparative enquiry into the legal mechanisms developed to address the specific problems arising from complex corporate groups in German law.

As the investigation in part two has shown, there is a second, related, assumption running in parallel with the conception of the employer as a unitary entity: that it must in fact always be the *same*, substantively identical, single entity throughout all areas of

employment law. With the growth of statutory regulation of personal work relationships, the domains within the discipline have multiplied, from setting minimum wage levels and ensuring equal pay to trade union recognition and consultation and information of employees. Within each of these domains, the notion of the employer plays a crucial role, frequently as the key entity on which obligations fasten. In a complex multilateral employment scenario it is however a highly fictional assumption that it will always be the same entity (or combination of entities) that is best placed to operationalize the relevant function: given the possibility for shared exercise of key employer functions, this is a fictional notion derived directly from the unitary straitjacket as discussed in the first chapter. In a Private Equity controlled company, for example, the worker's contractual counterparty will be best placed to ensure the payment of minimum wage levels if it is the entity operating payroll functions, whereas key decisions on redundancy may be taken elsewhere entirely, so that a limitation of consultation rights to the immediate contractual counterparty would hollow out the protective regime's purpose.

The second lesson to be recalled is that both strands of the tension need to be addressed for a successful reconceptualisation, if in very different ways. The solution proposed lies in a shift to a stronger functional approach, underpinned by a coherent single conceptualisation. The primary problem with the current formalistic (ie purely contractual) approach is its vulnerability to changing economic structures: as previous chapters have shown, even the presence of a contract of employment does not guarantee full employment law coverage where the exercise of employer functions is shared between or divided up across different entities. There are, however, also some positive aspects of the unitary fiction, insofar as it provides doctrinal unity, gives employees a clear counterparty to sue for various claims and provides clear contours in causation enquiries. It will be important to maintain such positive facets in the process of dismantling a long-established conceptual straitjacket. On the functional

side, a key temptation to be avoided is the initially simple thought that an answer to some of the practical problems identified could lie in the piecemeal creation of on-the-spot solutions, either through legislative intervention (with distinct and conceptually independent notions of the employer in various contexts) or purposive judicial interpretation. Such an approach would quickly become incoherent, and could even prove counterproductive where compliance with employment law obligations is reduced to financial compensation.

Finally, it is important to remember at all stages that any change must be logically linked to and take account of its point of departure. A functional approach to the design and interpretation of the notion of the employer should build directly on existing case law as identified in part one, and must also be able to sit reasonably comfortably with other areas, notably company law.

The Shift Towards a Normative Approach

This final reminder is reflected in the second preliminary point that needs to be considered before embarking on the substantive task of the following chapters: the methodological departure from earlier parts. The approach thus far has been fundamentally analytical-descriptive, discovering a problem in the current law and explaining its implications. The third part of this thesis is a careful move beyond earlier work into a deliberately normative stance: the proposed reconceptualisation suggests that the only way of resolving the fundamental issue at stake is a new, different approach to our conception of the employer. The following paragraphs hope to give an explicit account of this move by explaining the need for such a step, addressing potential concerns associated with it by demonstrating how it builds on existing foundations, and briefly locating the chosen approach in the light of methodological theory.

A shift towards a more normative approach becomes necessary at this stage because the analytical-descriptive methodology deployed thus far has reached its limits. As earlier chapters amply demonstrate, the multi-functional and unitary strands currently implicit in the notion of the employer lead to a conceptual deadlock in situations beyond a narrow paradigm. Furthermore, it has already become clear that attempts at devising a piecemeal approach to solutions cannot work. The utility of an analytical-descriptive method in overcoming the problem is exhausted with its extensive presentation of the latter. The case for a departure might be put even more explicitly: continuing in a purely descriptive manner could preclude the present effort from arriving at a solution. Indeed, it has been suggested that sticking religiously to such an approach while working with traditional norms in rapidly changing contexts can lead to 'mental imprisonment, the walls of which are self-constructed'.[1] In keeping in line with the careful shift from what the current notion of the employer *is* towards what it *could*, and *should,* be as developed in the introduction to this thesis,[2] subsequent chapters will however not seek to suggest any radical departure, but rather focus on a gradual adaptation of existing principles.[3]

That said, two related terminological issues which are less easy to resolve within existing frameworks need to be openly acknowledged: first, as regards the 'common sense' or general linguistic approach to what the words 'the employer' mean in everyday usage. It is not suggested that the proverbial reasonable 'man on the

1 L Nogler, 'Die Typologisch-Funktionale Methode am Beispiel des Arbeitnehmerbegriffs' ZESAR (10/09) 459, 467: '*Sie geraten in ein geistiges Gefângnis, dessen Mauern sie selbst errichtet haben*.'

2 A Dicey, *Introduction to the Study of the Law of the Constitution*, (Macmillan 1885) Preface to the First Edition vii (as cited by C Harlow, 'Changing the Mindset: The Place of Theory in English Administrative Law' (1994) 14 OJLS 419, 426).

3 D Marsden, '"The Network Economy" and Models of the Employment Contract' (2004) 42 BJIR 659, 671.

Clapham omnibus'[4] would readily perceive the word 'employer' to mean anything other than the anthropomorphic unitary counterparty to a contract of employment as described extensively in chapter one. The proposed solution may in certain factual scenarios lead to context-specific variations as to the precise identity of the entity, or indeed entities, on whom legal obligations fasten: a potentially radical departure in linguistic terms, insofar as the legal concept of the employer is extended beyond contractual privity to an array of relevant parties, will not always fit with 'the employer' as used in common parlance. It is of course not in and of itself problematic if legal notions depart at points from the ordinary meaning of a concept, be it to broaden or narrow it.[5] Indeed, it is frequently already the case that the 'legal meaning of the employer is not synonymous with the sociological or economic idea of the 'enterprise' or 'organisation'.[6]

Second, as regards the difference in the use of the word employer between previous parts and the remaining two chapters: in chapters one through four, 'employer' when used in a technical sense referred to the received common law notion. The methodological shift towards a normative analysis in this part will not be accompanied by a shift in terminology: it is the *meaning* of the legal notion of the employer that needs to change, rather than the label attached to it. In proceeding thus, the terminology deployed can fully reflect the underlying normative argument, as set out at the beginning of chapter five. A detailed explanation for this choice will be offered in the course of the final chapter; suffice it to say for the moment that any other approach, such as the coining of a new term, would serve only to confirm and thus perpetuate the underlying problems instead of addressing them head-on.

4 *McQuire v Western Morning News* [1903] 2 KB 100 (CA) 109.

5 J Bell and G Engle, *Cross on Statutory Interpretation* (3rd edn Butterworths1995) 72-75.

6 S Deakin, 'The Changing Concept of the "Employer" in Labour Law' (2001) 30 ILJ 72, 73.

Without straying too far into the territory of methodological scholarship, it is suggested that the cautious normativity thus advocated sits comfortably in the centre of a spectrum of potential approaches: the aim of the overall thesis, and chapters five and six in particular, is to move beyond the careful balancing of competing intellectual arguments;[7] its effort can thus be characterised as normative in a certain sense. On the other hand, this stance does not necessarily mean that it will go as far as putting forward strong claims for systemic change, in line with the clear sense of vocation for labour law scholarship advocated by Hugh Collins,[8] where drawing on the historic roots of the subject the 'main object of labour law [is] to be a countervailing force to counteract the inequality of bargaining power which is inherent […] in the employment relationship.'[9] This limitation does not necessarily imply a fundamental disagreement with such an approach, but is imposed rather because the task at hand is a much more narrow one: to reconceptualise the notion of the employer in response to a specific contradiction. The effect of restoring conceptual coherence may of course be the extension of employment law coverage to situations currently outside its regulatory scope;[10] it is however suggested that this will only be done to the extent of restoring coverage in line with its original regulatory design, rather than actively expanding employment protection.

In this sense, the present approach is probably closest to what Carol Harlow had in mind when advocating a stronger role for 'theory' in shaping and analysing the law. It

7 J Smits, 'Redefining Normative Legal Science: Towards an Argumentative Discipline' in F Coomans, F Grünfeld and M Kamminga (eds), *Methods Of Human Rights Research*. (Intersentia 2009).

8 H Collins, 'Labour Law as a Vocation' (1989) 105 LQR 468.

9 ibid 469, citing P Davies and M Freedland (eds), *Kahn-Freund's Labour and the Law* (3rd edn Stevens 1983) 18.

10 P Davies and M Freedland, 'The Complexities of the Employing Enterprise' in G Davidov and B Langile (eds), *Boundaries and Frontiers of Labour Law* (Hart Publishing 2006) 277.

is hoped that the potentially 'opprobrious resonance'[11] of such endeavours will be limited by staying within the realm of 'shallow' theory, the 'principled attitude to the development of […] legal concepts'.[12] The proposed reconceptualisation is thus in line with the role of theory as advocated by Stapleton, being able not only to explain the core but also the boundaries of liability scenarios, identifying relevant counterparties, and explaining causal requirements; all in line with deeper underlying principles.[13]

Structure

With these preliminary remarks in mind, the third part is structured around the functional and unitary strands of the notion of the employer, with a chapter broadly dedicated to exploring the necessary changes to each aspect. Chapter five develops the multi-functional limb to show how a careful extension to a fully functional notion can be achieved. Chapter six then turns to addressing the unitary strand to show that while some clear breaks have to be made from the existing setup (particularly as regards privity, and the operation of the employer notion across different substantive domains), there is a clear overarching conceptual notion of the employer which unifies even complex substantive manifestations.

[11] Harlow (n 2) 420.

[12] ibid 421.

[13] J Stapleton, *Product Liability* (Butterworths 1994) 95-96.

CHAPTER V
A FUNCTIONAL NOTION

In developing a functional notion of the employer, discussion in this chapter will be broken down into three broad steps, each with further subdivisions according to the analysis pursued. Section one develops the meaning of a 'functional' notion on an abstract or conceptual level. Section two then turns to an exploration of different legal avenues which may be used to put a functional notion into operation under existing law. A third section, finally, evaluates the proposed reconceptualisation of the first strand against the criteria developed in earlier parts.

SECTION I: FUNCTIONAL DEFINITIONS

As suggested in the introduction, this chapter will argue for a shift in how English law conceptualises the notion of the employer, moving from the current rigidly formalistic approach to a flexible, *functional* notion. In more concrete terms, the following working definition is offered in order to draw together the range of specific elements to be discussed in greater detail, below. It is submitted that employer should come to mean

> *the entity, or combination of entities, playing a decisive role in the exercise of relational employing functions, and regulated or controlled as such in each particular domain of employment law.*

The first section of this chapter is dedicated to an exploration, on a more abstract level, of the idea of a 'functional definition'. Three crucial implications of such a reconceptualisation, as traced through the following sub-sections, should be made

clear at the outset. First, that employment law obligations may be spread across multiple legal entities. This is the core of the reconceptualisation's challenge to received notions of the employer as a single entity. Second, as the functions of the employer can be subdivided into distinct groups, the employer is no longer exclusively defined as an entity exercising a single and simple function comprising all elements identified: exercising a particular subset of employer functions may suffice to trigger responsibility in that regard. Which of the functions are relevant depends on the particular area of legal regulation: the third implication of the functional approach proposed is that the attribution of responsibility will differ across distinct domains within employment law. The legal techniques for achieving such effects will be explored in the subsequent part; it is nonetheless important to elaborate on these potential consequences at an early stage.

A functional approach will, in practical terms, lead to a multiplicity of employers in many employment situations. Historically, when faced with an array of potential counterparties in multi-employer scenarios, privity of contract guided decisions as to where employment law obligations would be placed. An important part of the reconceptualised definition of the employer is the fact that different entities, or even a combination of distinct legal entities, could now be faced with employment law obligations, depending on the particular function and context in question. This distribution of employment law obligations is driven by the multi-functional mode of defining the employer: responsibility attaches to each subset of functions, regardless of whether they are exercised in combination with all other functions by a single legal entity, parcelled out between different parties, or shared across multiple entities.

The third important consequence to note results directly from the earlier observations. Under a functional approach, the composition of the employer acquires a degree of context- or domain-specificity: depending on the regulatory context, different subsets of the five employing functions will be of particular significance in

identifying the responsible counterparty or counterparties. Whilst differences (potential or actual) in the notion of the employer across areas such as tax, tort, vicarious liability and 'employment law proper' have long been the subject of academic and judicial discussion,[14] the proposed definition goes further: adopting a functional method allows for even more detailed differentiation within what may all too easily have become perceived as a single regulatory domain.[15] The resulting responsiveness to different regulatory goals of distinct domains of employment law should not be mistaken as an element of the definition of the employer. As sub-section two explains immediately below, it will be important not to confuse the different senses in which a notion can be 'functional'.

Calling for a functional definition of the employer is not a completely novel approach to the problems identified in previous parts of this thesis. Judy Fudge, for example, has long noted the 'need to go beyond contract and the corporate form, and adopt a relational and functional approach to ascribing employment-related responsibilities in situations involving multilateral work arrangements in employing enterprises.'[16] The present chapter hopes to contribute to that effort, by providing both theoretical foundations and practical illustrations for the workings of such a reconceptualisation. Indeed, as subsequent paragraphs will show, the link between the 'relational' and the 'functional' aspects mentioned by Fudge are crucial stepping-stones in the process. Writing in the domestic context of agency workers some ten years ago, Simon Deakin similarly suggested the development of a functional notion of the employer, focussing on the functions of 'coordination', 'risk' and 'equity' as

[14] See eg E McKendrick, 'Vicarious Liability and Independent Contractors: A Re-Examination' (1990) 53 MLR 770.

[15] Though cf a notable countermove: M Freedland and N Kountouris, *The Legal Construction of Personal Work Relations* (OUP 2011) 17, 25ff.

[16] J Fudge, 'Fragmenting Work and Fragmenting Organizations: the Contract of Employment and the Scope of Labour Regulation' (2006) 44 Osgoode Hall Law Journal 609, 636.

guiding principles.[17] The present effort may at first sight appear somewhat different from this work, both in terms of terminology and scope; it is nonetheless in line with Deakin's suggestion that 'obligations which would normally attach to the exercise of employer functions are to be imposed upon the relevant parties in each case.'[18]

With this background in mind, discussion thus turns to the development and close scrutiny of the idea of a functional notion of the employer: an initial sub-section draws together the existing foundations for a functional approach, before explaining and developing it in the light of theoretical models. Attention will then be given to the crucial limitations of the proposed functional reconceptualisation.

SUB-SECTION 1: FROM MULTIPLE FUNCTIONS TO A FUNCTIONAL NOTION

The foundations for a functional notion of the employer can be traced right through the traditional tests for employment status. As a review of existing case law in part one showed, the law already identifies and regulates a wide range of employer functions, which have been grouped together for analytical purposes into the following five categories:

[1] Inception and Termination of the Contract of Employment

> This category includes all powers of the employer over the very existence of its relationship with the employee.

[2] Receiving Labour and its Fruits

> Duties owed by the employee to the employer, specifically to provide his or her labour and the results thereof, as well as rights incidental to it.

17 Deakin (n 6) 79.

18 ibid 81.

[3] Providing Work and Pay

The employer's obligations towards its employees.

[4] Managing the Enterprise-Internal Market

Coordination through control over all factors of production.

[5] Managing the Enterprise-External Market

Undertaking economic activity in return for potential profit, whilst also being exposed to any losses that may result from the enterprise

A 'function' of being an employer was earlier defined as one of the various actions employers are entitled or obliged to take as part of the bundle of rights and duties falling within the scope of the open-ended contract of service. The Common Law, it was suggested, recognises these different functions in order to identify and classify employment relationships, and thus indirectly the notion of the employer. In revisiting the functional groups, it can be noted further that each function is in some way regulated by at least one domain of employment law. Indeed, as the following examples show, there are frequently several distinct or overlapping areas, each with different sources and regulatory techniques, involved in regulating or controlling the exercise of such functions.

As regards function [1], *Control over the Inception and Termination of the Employment Relationship*, for example, the employer's power over the very existence of a contract of services is regulated in a host of different areas, from anti-discrimination provisions and individual dismissal (both in statute and at common law) to consultation obligations in the case of employer decisions affecting larger groups of workers. Function [3] *Providing Work and Pay* is regulated at common law

under doctrines springing from the law of the contract of employment, ranging from a duty to pay, sometimes even when no work is done,[19] to potentially even a duty to provide work,[20] and a range of statutory provisions, including for example minimum wage levels.[21] Even function [4], the *Management of the Enterprise-Internal Market*, which could be seen as driven by contractual direction rights,[22] is subject to limitations at common law,[23] as well as a host of legislative interventions, for example through provisions on workers' health and safety.[24]

Despite the increasing recognition of these bundles or groups of functions and their use in different regulatory techniques in employment law, however, the problems identified in earlier parts continue to exist. This, it has already been suggested, is because their use as a criterion is overshadowed by historical assumptions leading to a unitary straitjacket in anything beyond a narrow factual paradigm situation of the independent single-entity employer: the assumption that the five functions have to be combined in a single, simple 'function' of the employer. Refocusing attention on a functional definition of the employer will allow the notion to break free from this single view through a detailed analysis of each individual function or groups of functions: from an array of legal entities linked to the employee, employment law obligations will be attached to whichever entity, or combination of entities, is

19 *Clark v Oxfordshire HA* [1998] IRLR 125 (CA).

20 *Nethermere (St Neots) Ltd v Gardiner* [1984] ICR 612 (CA) 632F (Dillon LJ). Although it has also been suggested that it might not be necessary for the courts to decide if an employer's duty is to provide a reasonable amount of work, or merely to pay an agreed and reasonable sum (Kerr LJ in dissent).

21 National Minimum Wage Act 1998.

22 R Coase, 'The Nature of the Firm' (1937) 4 Economica 386.

23 *Simmons v Heath Laundry* [1910] 1 KB 543 (CA). The right need not be unrestricted: *Ready Mixed Concrete Ltd v Minister of Pensions* [1968] 2 QB 497 (HC).

24 Construction (Working Places) Regulations 1966, SI 1966/94, reg 28(1): *Ferguson v John Dawson Ltd* [1976] 1 WLR 1213 (CA).

exercising that very function, or plays a decisive role in its exercise. Whilst the outcome of applying a functional approach may therefore on occasion be radically different from the current, purely contractual, solutions, it is an approach with deep grounding in the current law, carefully developing particular aspects of employment regulation.

SUB-SECTION 2: FUNCTIONAL TYPOLOGY

In order to embrace a functional approach, the law's underlying methods of reasoning need to evolve in part. The following section takes a step back to consider the meaning of 'functional' in the proposed functional notion on a more abstract level, in the hope that this will allow for a clearer account of that approach. It further aims to develop functional typology as a richer concept than simply a contrast to the perceived formalism of the current bilateral-contractual approach,[25] thus avoiding at least some of the dangers of the 'transcendental nonsense' which can result from the indiscriminate use of the 'functional approach' as a panacea to various analytical problems, 'often […] with as little meaning as any of the magical legal concepts against which it is directed.'[26]

At the outset, it is crucial to note the relationship of the functional approach to be proposed with another prominent use of that label.[27] Academic work frequently describes itself as analysing law from a functional perspective, 'ie, in terms of the economic functions it seeks to perform, instead of simply describing the contents of

[25] J Fudge, 'The Legal Boundaries of the Employer, Precarious Workers, and Labour Protection' in G Davidov and B Langile (eds), *Boundaries and Frontiers of Labour Law* (Hart 2006) 310-13.

[26] F Cohen, 'Transcendental Nonsense and the Functional Approach' (1935) 35 Columbia Law Review 809, 822.

[27] Frequently used, for example, in corporate law scholarship: W Douglas, 'A Functional Approach to the Law of Business Associations' (1928-29) 23 Illinois Law Review 673.

the laws.'[28] It has already been suggested that an important consequence of reconceptualising the notion of the employer will be its reflexivity to the aims, or socio-economic functions, of particular domains or layers of employment law. It could therefore be said that the notion of the employer becomes also a functional one, in the second sense of being aligned with those aims. This, however, is an *analytical description* of the results of the functional approach in the present sense, where the exercise of a particular function is the basis for *defining* an entity as an employer. The two terms are thus not mutually exclusive; they simply describe very different aspects of the reconceptualisation. This can be illustrated by a brief attempt to use functionality in its analytical-descriptive sense for definitional purposes: the notion of the employer would simply become 'whatever it should be' for the purposes of, say, unfair dismissal or non-discrimination legislation. Such a definition would be hopelessly imprecise and unworkable. By recognising the dual meanings of the term 'functional', however, it is possible to avoid this trap. Whilst the proposed definition can thus be said to be functional in both senses, they are relevant for different endeavours: the definition of the employer, and an ex-post-facto analytical description of the socio-economic consequences of adopting the new notion.

The account of functionalism proposed for purposes of identifying and defining the employer builds on the sociological concept of functional typologies, relying on the exercise of particular functions to determine the status of potential counterparties. A full exploration of the relevant sociological literature is beyond the scope of this work; the focus will instead be on Luca Nogler's writing in a very closely related area, applying different typological models to the determination of employee status.[29] In order to arrive at the functional typology proposed, two competing models will be

[28] J Payne, 'Book Review: the Anatomy of Corporate Law' (2010) 11 EBOR 477. In a sense, the same is true of 'functionalism' as used in sociology: Nogler (n 1) 463.

[29] Nogler (n 1). The following paragraphs draw extensively on this article and related work.

evaluated and illustrated with examples from the domestic context. Approached thus, the inherent limitations of the current approach quickly become evident, and form the stepping-stones for a functional approach.

Nogler identifies two traditional approaches to the legal classification of complex factual patterns in employment law, elements of both of which can be found in the contradictory strands of the current notion of the employer. Indeed, it could be argued that this approach combines some of the worst features of the two models. On one level, English employment law simply hopes to categorise employers according to a very simple scheme through the use of 'abstract-generalist terms,'[30] ie a definition which rigorously lays down specific criteria to be met in each case. The limitations of this approach are not difficult to see: faced with endless variations of facts and changing circumstances, the application of specific criteria becomes increasingly capricious. The previously cited definition of the employer in section 230(4) of the Employment Rights Act 1996 is a clear example of the shortcomings of this abstract-generalist approach. Whether or not an entity is an employer becomes a question of the presence of specified element(s), which may not even be logically linked: in the domestic context these are the exercise of certain employer functions, combined with the existence of a particular link in the form of a contract of employment.

A shift to analytical typologies was initially perceived as a successful response to these shortcomings of abstract-generalist terms.[31] In its original conception,[32] this approach offers several relative advantages: the categories (or typologies) are open, in the sense of there being no fixed list of criteria, all of which are to be met; at the same

[30] ibid 460, citing Guardini, *Der Gegensatz. Versuch zu einer Philosophie des Lebendig-Konkreten* (4th edn Schoningh 1998) 17.

[31] Abstract discussions beyond the scope of the present work can be found eg in Hempel, 'Typological Methods in the Social Sciences' in M Nathanson (ed), *Philosophy of the Social Sciences* (Random House 1952) 46.

[32] Nogler (n 1) 461.

time their openness allows for gradation within each category. Nogler, however, identifies a range of problems for the legal classification of complex factual patterns: first, there is still a deep underlying assumption that a category such as 'the employer' has a single, clear definition, universally applicable and substantially identical, all components of which can be determined in advance in such a way that future real world scenarios will always fall within them. The English courts' struggle to develop various series of tests for employee status can be seen as a clear example of this difficulty. Second, it is questionable whether gradation (in the present context, for example, on a sliding scale of 'more of an employer' to 'less of an employer') is analytically useful in employment law regulation. As criticism of the the judicial analysis of the worker concept (which attempted just such a gradation)[33] shows, gradation will frequently lead to a lowest common denominator level of protection.[34] Indeed, it could even be argued that such gradation is a symptom of a deeper underlying problem, that of the currently insufficient recognition of different domains of employment law.

Having identified these flaws with existing classificatory attempts, Nogler expresses his conviction 'that in between the (too) strict approach of positivist analysis and the (too) unclear approach of classic typologies there exists a *tertium datur* which permits the development of solutions focussed on the structure of each individual scenario, whilst at the same time presenting a clear rule:'[35] in other words, a functional typology.

The key idea of this *functional approach* is to focus on the specific role different elements play in the relevant context, instead of looking at the mere absence or

[33] Most notably *Redrow Homes Ltd v Wright* [2004] EWCA Civ 469, [2004] 3 All ER 98.

[34] G Davidov, 'Who is a Worker?' (2005) 34 ILJ 57.

[35] Nogler (n 1) 462.

presence of predetermined factors. [36] The presence of a contract of employment (or other contract) can thus be an important indicator in particular fields (for example the obligation to pay wages), but it is by no means the only one. To adopt Nogler's language to the present proposal, a functional notion of the employer is one where the employing entity or entities are defined not via the absence or presence of a particular factor, but via the exercise of specific functions.[37] This exercise of specific functions extends to include a decisive role in their exercise, in order to take account of the judicial recognition in existing cases that as regards employer functions the right to play a decisive role in a particular function is as relevant as the actual exercise thereof.

The working definition set out initially suggested that the notion of the employer should be understood as the entity, or combination of entities, playing a decisive role in the exercise of relational employing functions, and regulated or controlled as such in each particular domain of employment law. There are several steps in putting this abstract conceptualisation into practice. First is the recognition that for each employee, a functional approach to different models of inter-entity relationships will lead to an *array* of potential employing entities, from which one or several may emerge as employers. Being within this array of potential counterparties does not automatically bring any specific set of employment law obligations with it, even less so responsibility for the full domain of labour regulation. It is only as a consequence of the exercise of a particular regulated function that employer responsibilities are triggered; limited, however, to the relevant domain or domains. Without going into details of practical operation – the subject of extensive discussion in the subsequent section of this chapter – several fictional examples on the basis of fairly common factual patterns may serve to illustrate this further.

[36] ibid pt 3.

[37] ibid 463.

The array of those with a decisive role in management, particularly as regards the exercise of employer functions, will vary depending on the context in which the employing enterprises are organised. In triangular employment relationships, for example, it includes both agency and end-user, despite their difference in organisational integration or economic interest alignment. In a Private Equity setting, both the 'immediate' employer (ie the portfolio company) and the PE management company will find themselves within the array. It may also extend further, including for example a franchisor with very tight control over the operations of a particular franchisee.[38] Under the traditional approach, privity (or at most a specific statutory extension) would select the employer from this array of entities potentially able to exercise employer functions. In the reconceptualised notion of the employer this role is replaced by the exercise of various functions. As a result, different employers may bear (or share) a range of obligations, depending always on their specific roles.

A first possible illustration is the decision taken by a Private Equity management company to reorganise a large manufacturing plant by shutting down a particular production line. The selection of individual employees to be dismissed is left to the portfolio company management, who see this as an opportunity to terminate the employment of protected individuals (such as trade unionists, or members of a minority group). Even in this relatively simple example, different employer functions are exercised in different domains; the functional notion can nonetheless respond adequately: for the purposes of mass redundancy consultation, both the PE management company and company management will be 'employers', as they have exercised the regulated function (decisions affecting the employment of a certain minimum number of workers); as regards possible discrimination or protected dismissal claims, on the other hand, liability will fall on the portfolio company alone.

[38] D Weil, 'Fissured Employment' (Presentation given at the 2011 ISA Meetings, Pittsburgh, PA, May 2011).

Another scenario could arise in the context of hotels operated as franchise businesses, with the franchisor laying down, monitoring and enforcing strict regulations for the conduct of evening performances, including a uniform dresscode for all dancers and the equipment to be used. As the dresses and equipment turn out to be highly impractical for their shows, entertainers in hotels regularly end up injured during performances – it is the franchisor on whom the relevant health and safety provisions would fall. In the case of a disabled receptionist whose wheelchair cannot fit under the hotel's front desk, on the other hand, the employer's duty of reasonable adjustments would lie with the hotel alone.

Building on Davidov,[39] a final multilateral example could be the end-user who contracts with an agency for the supply of labour at an incredibly low price, evidently well below the legal minimum wage. In this scenario, the agency itself is in breach of the relevant regulations and will be seen as the employer for that purpose. As the end-user is also involved in the remuneration function, even if only indirectly, it will also be considered as an employer. If, on the other hand, a temporary worker comes up with a particular invention, the employer for purposes of a subsequent claim over patent rights will be the end-user, as it alone exercised the relevant role of the employer (for example training and provision of facilities) in that field.[40]

A detailed discussion of potential avenues to operationalize each of these options follows imminently. For the time being, the breadth and flexibility of outcomes resulting from a functional notion have been demonstrated. The methodology thus proposed allows for a very subtle approach to effective employment law enforcement, as it is able to 'take account of inter-firm relationships so as to determine each firm's

[39] G Davidov, 'Joint Employer Status in Triangular Employment Relationships' (2004) 42 BJIR 727.

[40] M Freedland and J Prassl, 'Resolving Ownership Invention Disputes: Limitations of the Contract of Employment' in M Pittard (ed) *Business Innovation – A Legal Balancing Act* (Edward Elgar, forthcoming 2012).

respective share of responsibility for such events as may occur over the course of the employment relationship.'[41] By looking at the full range of functions exercised across various relationships to determine actual responsibility, obligations are placed on the most relevant party, but not beyond it. Whilst the advantages of a functional approach will be discussed more extensively below, suffice it to say at present that this conceptualisation allows for flexibility across different regulatory domains, and can thus deal with the complexities arising from the fact that there are multiple entities, and multiple modes in which these entities can share the exercise of employer functions. It furthermore avoids several of the traps other potential approaches to bringing more entities into employer status suffer from, from reliance on narrow external doctrines such as fraud to the artificial assimilation of formally independent entities into a single legal personality.

SUB-SECTION 3: THE OUTER LIMITS OF A FUNCTIONAL NOTION

Having thus explored how the exercise of a relevant function can include a wider range of entities in the realm of employment law regulation, the question as to how the array of potential counterparties may be limited arises. In order for the functional notion of the employer to be workable, there also need to be clear outer limits, in order to avoid a search for any factors that may have influenced the 'real decision-maker', or even any causative event leading up to the exercise of a relevant employer function. Indeed, if all such factors were to be included in the reconceptualised notion, it would render most existing norms unworkable.

Employment law generally does not regulate dealings between arms' length parties, such as for example the breach of a commercial supply of goods contract

[41] M Morin, 'Labour Law and New Forms of Corporate Organization' (2005) 144 International Labour Review 5, 15 (as quoted in Fudge (n 16) 645).

between two companies. At the same time, however, such decisions may have a knock-on effect on employment: without orders, the counterparty might no longer be able to sustain production levels, or in the worst-case scenario cease to exist, thus leading to collective redundancies. In order to avoid an extension of employment law into such situations, narrower limits need to be drawn. Indeed, amongst the few positive aspect of a strictly bilateral analysis of the employer-employee relationship was its ability to act as a clear safeguard causation-wise: whilst frequently placed too narrowly, it nonetheless has the virtue of easily identifying limits of responsibility. It is suggested that the functional definition put forward fulfils this function equally well, without however distorting the scope of legal protection: by focussing on the exercise of, or decisive legal role in the exercise of, employer functions, it ensures congruent employment law coverage that is neither under- nor over-determinative.

The functional approach proposed is *not* purely causation-based. If such a model were adopted and taken to its logical extension, a major customer not renewing a substantial order would be under a duty to consider its decision's impact on employees; indeed anyone in a causal relationship may be caught. The crucial limitation in the proposed definition is a relational one, looking at the relationship between the relevant parties, and focused on the exercise of regulated functions *qua* these relationships: these are the crucial factors in determining which actions constitute 'the exercise of employer functions'. Termination of a commercial supply contract, for example, would therefore not be the exercise of an employer function, as neither the relationship between supplier and producer nor the action of not placing further orders fall within the scope of employment law.

In his work on the ascription of legal responsibility in multi-entity scenarios,[42] Collins identified three forms of 'bonding between productive organisations': ownership, contract, and authority. Ownership bonds, usually via an outright holding of the majority or even all shares in subsidiaries, describe what has already been seen in corporate groups and Private Equity fund structures. As regards contractual bonds, Collins suggests examples from construction and manufacturing industries, describing the creation of cores and peripheries. The most relevant instantiation of this linkage for present purposes are triangular work agency setups, which characterise situations of parcelled out employer functions even though the entities involved will not usually be economically aligned. Finally, there are more diffuse 'authority relations', including shareholders with a significant minority equity stake, but also creditors, anyone else on the powerful end of a relationship of economic dependence, and even professional advisors.

Collins rightly suggests that in general, none of these forms of bonding should be enough in and of themselves to contradict basic group liability principles of each legal entity's individual responsibility. At the same time reliance on the contract of employment alone will leave many relevant situations beyond the reach of protective norms. A functional approach to the notion of the employer as developed in this chapter can strike a successful balance between these extremes, by drawing the line at entities' exercise of employer functions, including a legal right to have a decisive role in so doing.

The goal is to ensure congruent legal coverage in situations where multiple entities exercise some form of direct control over the employment relationship - but drawing on the functional approach suggested, the precise kind or mechanisms of bonding

[42] H Collins, 'Ascription of Legal Responsibility to Groups in Complex Patterns of Economic Integration' (1990) 53 MLR 731, 733-4.

matter less than what its function is: if it is to give a legal right to exercise an employer function, or a legal right to have a decisive role in the exercise of such a function, then the party will be within the realm of potential employers. As has been seen, a commercial supply contract, even if written in favour of a financially dominant company, will not usually come within this scope. The functional limitation is more than just a pragmatic choice: it remains flexible to adjust to the specific role a combination of factors may play in a particular context. The fictional customer who decides to breach its supply agreement would not be performing a function of the employer (and is therefore beyond the potential array of counterparties), even though their actions had a major causative impact on the employer's actual decision making.

As the Court of Appeal's recent decision in *Shanahan Engineering* shows,[43] the courts are well equipped and comfortable to draw these sorts of distinctions on the facts of individual cases. There, the energy company Alstom had contracted with Shanahan, a labour supplier who was paid at cost plus arrangement fees, to construct a set of reactors. Upon a change in external circumstances, Alstom decided to switch from simultaneous to sequential construction, thus reducing its manpower requirements. It instructed Shanahan in writing to 'review the resources on site and optimise those resources in line with the new schedule. It is Alstom's expectation that this will result in an immediate reduction of both indirect and craft labour whilst maintaining compliance with the [relevant regulatory] agreement.' Shanahan's local manager consequently selected a number of employees for redundancy, and presented the trade union representatives with a final decision, having failed to consult them previously. On the facts, the special circumstances defence in section 188 TULRCA was not made out, as even though 'instructions given by Alstom made it inevitable that the workforce on the contract would have to be reduced' there had been a wide

[43] *Shanahan Engineering Ltd v Unite the Union* [2010] UKEAT/0411/09/DM.

range of options left to the company, thus placing them under a duty to consult with workforce representatives.[44]

The Court furthermore made it clear that no reliance could have been placed on the external control provisions, 'no doubt because, although Alstom controlled the contract and the work, Alstom did not control Shanahan.'[45] Even if a functional test were normally to place obligations on the party who actually took the decision leading to collective redundancies, rather than the immediate party to the contract of employment, there is no need to fear the liability floodgates.[46] Courts are able to draw appropriate distinctions between different situations, whether by using the language of 'control over contract and work versus control over the company' as developed in *Shanahan*, or the decisive legal role in exercising employer functions suggested in the preceding paragraphs: applying that test, *Alstom*'s commercial decision to alter the construction schedule would not have fallen within the scope of exercising one of the regulated employer functions.

SECTION II: THE FUNCTIONAL NOTION IN OPERATION

The accurate mapping of regulatory obligations onto the entity or entities exercising the relevant functions is thus the key aim to be pursued. As the survey of multi-entity contexts in part two demonstrated, the current situation in English law is far from achieving this goal. This section returns to specific examples of the application of different legal norms to complex factual scenarios, this time, however, in order to demonstrate how the functional notion of the employer can successfully overcome the problems identified.

44 ibid [31]; cf the decision in *Howlett Marine Services v AEEU* [1998] UKEAT/253/98.

45 ibid [11].

46 *R v Associated Octel Co Ltd* [1996] 1 WLR 1543 (HL).

At first glance, it might be thought that a fundamental reconceptualisation of the notion of the employer would require significant innovation in both statutory design and the courts' adjudication. In developing practical illustrations it quickly becomes apparent, however, that this is not necessarily the case. Indeed, it is hoped that in addition to exploring different possible avenues for operationalizing a reconceptualised notion of the employer, the following discussion will demonstrate how relatively little, if any, need there is for radical innovation or departure from existing frameworks to achieve the functional outcome proposed. Many if not all of the required techniques can already be found in various pockets of case law, driven by seeds of the functional approach described in the last section. Depending on fact patterns and the purpose of the relevant area of employment legislation, a combination of techniques already found in the law of the contract of employment and the many statutory extensions to it can be developed to give employment law scope functional flexibility in complex multilateral scenarios.

The idea of looking to existing material for inspiration as to how a functional reconceptualisation might operate in practice is not new. In 1990, Collins examined a range of piecemeal statutory interventions in search of a functional approach;[47] Fudge similarly found existing techniques in a number of statutory devices, notably those lifting corporate veils and ignoring privity for specific purposes in particular contexts.[48] Davies and Freedland went further, setting out examples as diverse as the Gangmasters (Licensing) Act 2004, section 13 of which makes it a criminal offence to be supplied with workers through gangmasters' unlicensed activities, and the case of *Dawnay*,[49] where the court dispensed with the artificial bilateral analysis of restrictive

[47] Collins (n 42) 738ff.

[48] Fudge (n 25) 305.

[49] *Dawnay Day & Co Ltd v De Braconnier D'Alphen* [1997] IRLR 285 (CA).

covenants in financial institution teams; noting at the same time that while these different techniques may contain promising avenues, they were in and of themselves not enough to remedy the underlying problem.[50]

Having delved into the problem itself by looking at the tension between the functional and unitary strands of the current notion, the development of a functional notion in this chapter is the first of two steps in an attempt to address the underlying problem. It surveys the broad range of possible options specifically in order to show how a functional approach can be put into practice, frequently by building on familiar structures. Examples will be drawn from a wide variety of regulatory areas, including techniques sometimes analysed as extensions of the employee notion. This, however, is primarily due to the way accounts of the scope of employment law are classically framed: upon closer inspection, clear traces of the functional approach become apparent in attempts to include multiple entities within the scope of employment law obligations. In presenting practical illustrations of the theoretical model developed thus far the necessary steps are hardly radical ones: even under a functional notion of the employer, a worker's primary contractual counterparty, such as a corporate entity, may frequently be the bearer of many key employment obligations. That, however, will merely constitute the *starting point* of enquiry, not its automatic end.

It is important to note that this emphasis on the use of existing techniques to operationalize the reconceptualised notion should not be mistaken for the suggestion that a coherent approach already underpins the different piecemeal solutions. Whilst it may be true to say on a very abstract level that most are driven by a specific purpose, the current piece-meal approach is highly problematic for a range of reasons, to be fully explored in chapter six. Suffice it to say for the moment that these revolve around a strict adherence to the bilateral and unitary focus of the traditional approach.

[50] Davies and Freedland (n 10).

Indeed, it may be for this reason that many of the cases on which the following section builds were, at least initially, seen as exceptions to established norms.[51]

A related challenge to the proposed approach, particularly as regards the discussion of specific statutory measures, are frequent judicial pronouncements to the effect that regulatory intervention in one particular area should be taken as a clear sign that the legislator intended to go thus far and no further and that specific provisions can therefore not be applied in analogous contexts,[52] or that there is little space left for common law measures once 'Parliament has occupied [a particular] turf.'[53] The response, again, is to recall the purpose of this chapter: it is not its suggestion that a functional notion of the employer can already be found in English employment law, or even that the proposed approach has been a driver of specific statutory reforms. The functional approach does not argue for the extension of specific concepts as such – such piecemeal reforms are inevitably constrained by the underlying unitary conception, as one or two examples will demonstrate. As the introduction to part three made clear, a clear normative step is proposed. It is not, however, one that would require a radical rethink of the techniques to be discussed.

With these considerations in mind, discussion is structured into three sub-sections to analyse representative illustrations of a functional approach to defining employers, drawn from across English employment law. In keeping in line, at least as regards the general scheme, with the historical approach, initial discussion will focus on various *contractual solutions*, with the exploration of implied bilateral or even multilateral contracts in the agency labour context as its starting point. It will be seen how even at

[51] Deakin (n 6) 77, commenting on *MHC Consulting Services Ltd v Tansell* [2000] ICR 789 (CA).

[52] *Dimbleby & Sons Ltd v National Union of Journalists* [1984] ICR 386 (HL).

[53] Most famously in the context of the statutory regulation of unfair dismissal: L Hoffman in *Johnson v Unisys Ltd* [2001] UKHL 13, [2001] 1 AC 518.

common law, there are clear avenues to embrace a functional approach: implied contracts are a leading example of how a functional approach can overcome existing stalemates in this area, whilst remaining solidly embedded in common law reasoning. A second sub-section then turns to illustrations of the functional approach operating in many areas of *statutory regulation*, notably anti-discrimination and equality duties, as well as health and safety. In working through several specific examples, the discussion's focus will be on demonstrating the different ways in which a functional approach can overcome most of the issues that needlessly puzzle courts at the moment – from an individual working for multiple employers on the same job at the same time, to reconciling parties' freedom of contract with regulation in line with economic and social realities. Finally, and in parallel with the discussion of different modes of sharing functions in chapter two, a third sub-section will explore different *modes of ascribing liability* to more than one entity, from joint and several liability to domain-specific responsibilities of various entities. Throughout these sub-sections, two crucial advantages, or flexibilities, of the functional notion that have already been hinted at will begin to emerge more clearly, in preparation for evaluation in a concluding section: the functional approach is context specific, ie it can lead to different answers to the 'who is the employer' question, depending on the goals of the regulatory sub-domain or layer in question. The answer to that question may furthermore frequently involve more than one entity, and in logic combination with the earlier point, potentially different constellation will appear in different areas: the actual operation of a functional notion is highly responsive to the reality of relationships within a broad employment nexus – which is not to say, however, that it cannot also offer clear outer boundaries.

SUB-SECTION 1: CONTRACTUAL AVENUES

The key avenue to be considered in this sub-section builds on implied contracts. Their potential to operate in multi-entity scenarios such as agency work or personal service companies has been the subject of much controversy in both judicial opinions and academic writing. In line with the overall purpose of this chapter, subsequent discussion of these materials is selective, with a focus on techniques that could be used, for example, to apply a functional approach in extending the scope of implied contractual terms, or certain statutory rights that need contractual minimum periods.

The primary testing ground for implied contracts in recent years have been agency worker cases. The setup of triangular relationships in this context will be recalled from part one of the thesis: a worker (in the non-technical sense of that word) is supplied by an agency to perform tasks for one of its clients. In case of employment law grievances there are, broadly speaking, two kinds of parties against whom the worker might attempt to bring his or her claim:[54] the employment agency,[55] and its client, commonly known as the end-user.[56] From a functional perspective, this situation does not present major difficulty: whoever exercises a particular regulated function should be held responsible for any regulatory consequences. As discussed earlier, however, the fact that this setup is beyond the narrow unitary paradigm means that the courts have struggled with finding an adequate legal response to the resulting division of employer functions: while the problem may no longer be one of *sui*

[54] A duality highlighted by E Brown, 'Protecting Agency Workers: Implied Contract or Legislation?' (2008) 37 ILJ 178.

[55] For example, *McMeechan v Secretary of State for Employment* [1996] EWCA Civ 1166 [1997], IRLR 353.

[56] For example, *Dacas v Brook Street Bureau (UK) Ltd* [2004] EWCA Civ 217; [2004] ICR 1437.

generis classification,[57] a very wide range of rights go unprotected in the standard analysis where no contract is found the with end-user[58] and, with increasing frequency, not even with the labour agency.[59]

In direct response to this lack of protection for an increasingly larger sector of the workforce,[60] a string of cases began to draw on the foundations laid in *Franks v Reuters*[61] in developing the idea that a contract of employment may be implied between end-user and worker. Statutory provisions explicitly provide for this possibility; the oft-cited definitional provision in section 230(2) ERA, for example, decrees that a contract of employment is 'a contract of service or apprenticeship, whether express or implied, and (if it is express) whether oral or in writing.'[62]

As outlined previously, Mummery LJ laid out the basic foundations for using implied contracts in multi-entity employment law scenarios in *Dacas*.[63] On the facts of that case, this aspect of the decision was strictly *obiter*, as the claimant had never appealed against the employment tribunal's finding that there was no contract of employment with the end-user. Nonetheless, in overruling the EAT's holding that the cleaner had been employed by the agency, the court found that *as a matter of law*, an implied contract between parties was a possibility that tribunals ought to consider. Mummery LJ's judgment, underpinned by an understanding of the structural problems

57 Initially, sui generis: *Construction Industry Training Board v Labour Force Ltd* [1970] 3 All ER 220 (HC).

58 eg recently in *East Living Ltd v Sridhar* [2007] UKEAT/0538/07/RN.

59 *Montgomery v Johnson Underwood Ltd* [2001] EWCA Civ 318, [2001] ICR 819; confirmed in *Bunce v Postworth Limited t/a Skyblue* [2005] EWCA Civ 490, [2005] IRLR 557.

60 ibid, for example [9].

61 [2003] EWCA Civ 417, [2003] ICR 1166.

62 *James v Greenwich LBC* [2008] EWCA Civ 35, [2008] ICR 545 [5] allows for the possibility of a single work arrangement leading to multiple contracts.

63 *Dacas* (n 56).

facing agency workers is at pains to reconcile the seeds of a functional approach with traditional common law techniques. Its reasoning is firmly based in the classic law of the employment contract, as later cases have confirmed.[64] Starting with the observation that the above-cited statutory reference to employment contracts explicitly includes *implied* contracts,[65] his Lordship set out an approach to implication featuring both traditional tests of mutuality of obligation and control. While the former was included as a necessary element,[66] the objective fact and degree of control was suggested to be the crucial element in finding an implied contract of employment.[67] Sedley LJ agreed with Mummery LJ in a short judgment infused with ideas from another early area of functional reasoning, vicarious liability.[68]

Munby J in dissent voiced rather strong opposition to such functional ideas of a contract with the end-user. Having set out the 'industry['s] assumption' that a contract of employment could be avoided once remuneration and control were split,[69] his opinion referred back to Elias J's EAT decision in *Stephenson* v *Delphi Diesel Systems Ltd*.[70] There, an employee's previous service under an agency arrangement was held not to have been under a contract with the end-user, thus negating the possibility of an unfair dismissal claim. In so doing, Elias J's focus was firmly on mutuality of obligation as the sole test for the existence of a contract – with control

64 *Cable & Wireless Plc v Muscat* [2006] EWCA Civ 220, [2006] ICR 975 [36].

65 Employment Rights Act (ERA) 1996, s 230(3).

66 *Dacas* (n 56) [49].

67 ibid [53].

68 For example ibid [72]. While Mummery LJ mentions (tortious) vicarious liability briefly at the outset of his judgment at [2], he does not conflate the two situations to the same extent.

69 ibid [82] – [83].

70 [2003] ICR 475 (EAT).

relegated to classifying the contract as one of employment once established.[71] The precise opposite of the Mummery LJ's functional reasoning, this approach betrays a firm commitment to analytical typology, illustrating the resulting problems as identified in Nogler's work, above. Munby J built on the President's opinion, finding that the Employment Agency could not be seen as an agent for the employer when it came to remunerating the worker. This concept of Mutuality of Obligation is closely linked – on the employer's side – to a duty to pay the worker's wages. As this was said to be independent from the end-user on the facts of the case,[72] no mutuality and consequently no contract of employment could be found.

This shift towards mutuality of obligation, in combination with an attempt to decrease the importance of various modern manifestations of the control test,[73] traps the court's reasoning in a narrow formalistic approach. Once attention is focussed on the absence of individual factors, analysis can only deal with a single relationship at any given time, without appreciating the role each factor plays in a particular context! Day-to-day direction may, for example, be the most important employing function exercised by the end-user.[74] Yet with it excluded from initial consideration, and mutuality being defined in a way that protects end-users, workers could have easily found themselves without access to any statutory rights.

Despite this powerful dissent, and an increasing unease expressed by the President of the Employment Appeals Tribunal, the functionalist approach continued to develop. In 2006, the Court of Appeal explicitly approved the majority opinion in

71 ibid [11]. This is an illustration of the confusion mentioned earlier.

72 (n 61). *Quaere*, however, whether this can really hold true: normally the agency will only pay the worker if and when work has been done for an end-user, with funds provided by the latter.

73 ibid [102], cited with approval by Munby J in *Dacas* (n 56). The explanation of *Motorala* v *Davidson* [2001] IRLR 4 (EAT) (where the end-user was held to be employer) as a case fought on control alone can be seen in the same light.

74 M Freedland, *The Personal Employment Contract* (OUP 2003) 40.

Dacas. *Muscat*[75] was not a triangular case as such – an important reminder of the practically unlimited number of potential factual constellations beyond the narrow paradigm setup. The claimant had originally been employed directly by the end-user, before the relationship was restructured as a chain of different entities, including work agencies and a personal service company owned and directed by the claimant himself, set up on instructions of the previous employer. For present purposes, the decision in *Dacas* is interesting for two reasons:[76] first, as effective control had been conceded by the end-user, discussion before the court centred on remuneration arrangements – an employer function that had not yet been the subject of extensive judicial discussion. The company's claim that absent a duty to pay the worker directly there could be no mutuality of obligation failed.[77] Smith LJ took a clearly functional approach in holding that pay arrangements could be both direct and indirect. The structures in place were only an element in the factual matrix, and could not in and of themselves be determinative of the outcome.

The second important step[78] was the court's explicit linking of previous *dicta* that a contract could only be implied where 'necessary'[79] to the business reality test of necessity as espoused by Bingham LJ in *The Aramis*.[80] This was a first sign of what some interpreted as a shift in focus away from an overtly functional approach; and it was soon to be driven along in the subsequent case of *James*.[81] The claimant there

75 *Muscat* (n 64).

76 See also *Royal National Lifeboat Institution v Bushaway* [2005] IRLR 675 (EAT).

77 ibid [35]. This has since been applied in several EAT decisions, for example in *Harlow* v *O'Mahony* [2007] UKEAT/0144/07/LA.

78 *Muscat* (n 64) [45].

79 *Dacas* (n 56) [16].

80 *The Aramis* [1989] 1 Lloyd's Rep 213 (CA).

81 [2007] IRLR 168 (EAT).

was again an agency worker, who had for several years been assigned to an asylum hostel operated by Greenwich Council. From a functional perspective, most employer functions were carried out by the council; though crucially not all: the claimant once changed supplying agencies to improve her hourly wage. On the basis of these facts, the Appeal Tribunal held that no contract of service could be implied between the claimant and the council. In the course of his decision, Elias J set out a series of guidelines to suggest that contracts could be implied only in sham contexts, or '[w]here the express contract does not properly reflect the actual arrangements, and it is necessary to imply a contract in order to provide a proper explanation.'[82] The Court of Appeal's ruling in *James* explicitly approved these guidelines.[83] Led once more by Mummery LJ, it upheld the EAT's decision, including the emphasis placed on a strict application of the necessity test.

In response to these decisions, leading commentators were quick to pronounce 'the end of the road for the implied contract'.[84] At a first glance, concerns voiced in various quarters that the shift towards necessity in *James* closed down a previously promising avenue for worker rights seem warranted.[85] Yet, together with most arguments critical of the implied contract approach, for example as regards questions of documentation,[86] this is not directly relevant for the current discussion. Seen through this lense, it is suggested upon closer inspection that the only thing the Court explicitly recoiled from was a possible interpretation of cases such as *Franks* and subsequent dicta that the passing of time alone may be key to the finding of a

82 ibid 'Guidelines' 3(b).

83 *James* (n 62).

84 Brown (n 54).

85 M Wynn and P Leighton, 'Agency Workers, Employment Rights and the Ebb and Flow of Freedom of Contract' (2009) 72 MLR 91.

86 M Wynn and P Leighton, 'Will the Real Employer Please Stand Up? Agencies, Client Companies and the Employment Status of the Temporary Agency Worker' (2006) 35 ILJ 301, 311.

contractual relationship – an approach that would run counter to the established approach to implication in the general law of contract, where even very long-term relationships, for example with suppliers, cannot give rise to a contract simply on the basis of the duration of the engagement.[87] From a functional perspective, this limitation is not problematic – indeed, the existence of fixed factors such as the passage of time would bring their own problems.

The decision may in fact be characterised as rather helpful in several aspects: not least, by limiting the role of Mutuality of Obligation,[88] a paragon of the old formalistic approach. More importantly, and perhaps counter-intuitively, its emphasis on the necessity test opens up the possibility of a functional approach with clear guidance and limits. In *James*, Mummery LJ set out the *Aramis* test as suggesting that implication must be

> necessary […] in order to give business reality to a transaction and to create enforceable obligations between parties who are dealing with one another in circumstances in which one would expect that business reality and those enforceable obligations to exist.

In the narrow context of triangular employment relationships alone, the implications of this formulation may often be negative. On one level, existing contractual relationships between the agency and the end-user can be said to explain the provision of work, thus negating the necessity of an implied contract between worker and end-

[87] *Baird Textile Holdings Ltd v Marks & Spencer Plc* [2001] EWCA Civ 274, [2002] 1 All ER (Comm) 737.

[88] ibid [30], [45]: 'the presence of the irreducible minimum of mutual obligations [is …] not the essential point'.

user. This analysis has led to the failure of most subsequent claims in the lower tribunals.[89]

From the less analytical-descriptive angle of this chapter, however, the necessity test may warrant some further thought: it is suggested that its enquiry could also be understood as a very functional one, in so far as it looks at the reality of the parties' actions, rather than the formal structure of their relationships. A possible objection to this contention can be found in subsequent paragraphs of Bingham LJ's judgment, where his Lordship suggested that

> it would be contrary to principle to countenance the implication of a contract from conduct if the conduct relied upon is no more consistent with an intention to contract than with an intention not to contract […] Put another way, I think it must be fatal to the implication of a contract if the parties would or might have acted exactly as they did in the absence of a contract.[90]

The context in which this formulation was developed must be remembered, however: the *Aramis* was a commercial case in the shipping world. The actors involved were professional parties (such as stevedores and freight agents); the purpose of their contract being a one-off transaction. In Employment law, that transactional element – the wage/work bargain – is arguably only a small part of the contract's purpose, which extends into a wide range of regulatory domains, not least the law of unfair dismissal. From a functional perspective, 'conduct' in the above quote cannot therefore be limited to the immediate presence of the employee on the end-user's premises, or even the receipt of wage payments.

[89] Including *East Living Ltd v Sridhar* (n 58): carer not employed as other explanations for work negate necessity test and *Vidal-Hall v Hawley* [2007] UKEAT/0462/07/DA: social worker in relationship with charity, no need to also imply relationship with HM Prison Service.

[90] Drawing in particular on F Reynold, 'The Status of Agency Workers: A Question of Legal Principle' (2006) 35 ILJ 320 (a piece the conclusions of which the present author respectfully disagrees with).

This thinking is brought out in another formulation of the necessity test. In a case subsequent to the *Aramis*, Staughton LJ suggested that

> it [was] not enough to show that the parties have done something more than, or different from, what they were already bound to do under obligations owed to others. What they do must be consistent only with there being a new contract implied, and inconsistent with there being no such contract.[91]

Applying this analysis in the specific context of a functional interpretation of the scope of employment law, it is suggested that the necessity requirement would be met in many situations. Illustration may even be found in existing law, such as *NGE v Wood*, a case decided by the EAT in the run-up to *James*, already applying the guidelines set out by Elias J.[92] The claimant payments manager had been supplied to the respondent company by an agency; on the basis of his subsequent tight integration into the respondent's business, the Employment Tribunal implied a direct contract of employment on the basis of the sham doctrine. The EAT reversed their finding on this point, reminding the Tribunal of the high thresholds involved, but went on to substitute its own reasoning in favour of an implied contract under the necessity test, relying on factors including the parties' direct negotiations over various terms, and an obligation on the claimant to provide personal service. The resulting reasoning was openly functional, looking at necessity through the parties' long-term actions rather than a formalistic account of why Mr Wood was in NGE's service: '[the company] has chosen to put itself in a direct relationship with the individual, affecting the future conduct between them. The company was not treating the Claimant as a semi-

[91] *Mitsui & Co Ltd v Novorossiysk Shipping Co (The Gudermes)* [1993] 1 Lloyd's Rep 311 (CA) 320.

[92] *National Grid Electricity* v *Wood* [2007] UKEAT/0432/07/DM.

detached member of staff. They were in practice acting as though he were a wholly integrated member of staff.'[93]

This section set out to show how a functional approach might be put in place in English law, and furthermore to suggest that seeds of it can already be found in its various domains. The preceding analysis has given clear examples of functional approaches in those domains regulated directly through the contract of employment: the courts are able to follow employer functions with relevant regulation through the implication of contracts of service. Before turning to the next sub-section, a residual point of criticism of this approach should briefly be addressed: the observation by Collins, that 'in truth the courts are often caught between a rock and a hard place. In trying with the best of motives to rescue temporary agency workers from their plight of being excluded from employment law almost entirely, the courts have resorted to fictions such as the implied contract of employment, and subsequently received their just reward: incoherence in the law followed by ignominious retreat to orthodoxy.'[94] This view serves as an important reminder that nothing in the foregoing discussion should be taken as a suggestion that a fully operational functional notion has already been developed by the courts. Indeed, the reason why the courts are stuck in the way described by Collins is that any attempt at developing functional solutions can only work in combination with a carefully reasoned underlying notion.

[93] ibid [40]. The developments set out in the preceding paragraphs are clearly in line with the Supreme Court's recent decision in *Autoclenz Ltd v Belcher* [2011] UKSC 41, [2011] 4 All ER 745 where L Clarke noted a 'critical difference' between ordinary commercial disputes and employment law litigation [34]. A Bogg, 'Sham Self-Employment in the Supreme Court' (2012) 41 ILJ 328, 332 sees this as clear evidence 'that the common law has now started to dispense with […] fictions and mystifications in respect of contracts for personal employment.'

[94] H Collins, 'Book Review: D McCann *Regulating Flexible Work* (Oxford, OUP 2008)' 2009 (72) MLR 141, 143.

SUB-SECTION 2: STATUTORY REGULATION

As noted at the outset, contractual solutions are the starting rather than the end point of this enquiry: indeed, they may frequently need to be used in combination with other regulatory provisions to ensure that each employer will bear the relevant responsibilities. Discussion thus turns to an exploration of potential avenues for operationalizing a functional definition of the employer, as developed in numerous statutes. Its goal is to add to the understanding of a variety of ways in which it would be possible to place obligations on entities other than the employer's immediate contractual counterparty.

Examples will be drawn from a range of different statutory extensions of employment rights, in particular from the areas of Discrimination and Equality Law, and the field of Health and Safety regulations. Illustrations will by no means be limited thus, however – examples for different ways of operationalizing a functional approach can be found in topics as diverse as whistle-blower protection and the political troubles in Northern Ireland. In discussing these various areas, a full analysis of substantive provisions will usually be beyond the scope of this thesis; the focus will be on the application of various rights and duties to employers in multi-entity contexts. Where the law has moved on, particularly in the field of the Equality Act 2010, this focus on regulatory technique alone will also allow for reliance on partially obsolete older case law, as it is the underlying approach that is of primary interest. The dual purpose already seen in sub-section one remains identical over the following pages: the examples serve to show how the courts may put a functional notion of the employer into practice, drawing on pre-existing pockets of functionality – without however suggesting that that a coherent functional notion is already in place, as a brief mention of several negative examples will highlight.

As regards structure, this sub-section deliberately eschews the mere listing and description of different techniques – both because a complete list of examples would be near impossible to condense into the available space, and because the creation of any such list would significantly distract from the open-ended nature of the functional approach. Instead, the focus is on several instantiations of a further crucial lesson that emerges from this chapter: once the courts embrace a functional approach, freed from the conceptual unitary straitjacket, many if not most analytical issues that have been puzzling courts and commentators fall away: whether it is the embrace of different regulatory aims in purposive interpretation, a focus on the reality of an activity rather than its structural organisation, or the fact that courts are no longer torn between parties' freedom of contract and their evasion of regulatory obligations; even the idea that work is frequently done for a multiplicity of parties whose control over and benefit from the activity are not mutually exclusively – all these question can be addressed in a much more accurate fashion.

Purposive Interpretation in Line with Different Regulatory Aims

A functional notion of the employer can much more readily accommodate specific regulatory aims, and comfortably mould itself to their relevance. It furthermore allows the judiciary to be open about these considerations, keeping in line with constitutional propriety and allowing for greater scrutiny and academic discussion of individual decisions.[95] It is perhaps not surprising that health and safety and anti-discrimination provisions are amongst the earliest examples of the functional approach advocated. There, a clear purpose is easy to state at an abstract level: to ensure that individuals are treated equally and that workers are not physically harmed or injured, respectively.

[95] Nogler (n 1).

Despite this, it is easily possible to envisage potential under-inclusion even in paradigm situations.

Both areas can be seen as intimately connecting employer's economic activity and important regulatory goals. Put differently, the fact that legal anti-discrimination efforts started in employment law is not 'random', but rather a clear function of the 'social powers of employers', which 'may well explain why the law regards it as right to place them under a duty not to discriminate, by contrast with other private actors'.[96] Gardner puts this point very clearly in an attempt to justify discrimination law against liberal criticism, noting the 'special institutional role' of the employment relationship both as regards the distribution of relative advantages and loss of individual control. On this basis, 'when the employer's social significance is recognized, requiring him not to discriminate indirectly is merely a proper response to current patterns of advantage and disadvantage, coupled with an understanding of the distribution of effective social power'.[97] The same is true, *mutatis mutandis*, in the Health and Safety context: the Robens Report,[98] leading up to Health and Safety at Work Act 1974, was keenly aware of the importance of the link between an employer's business activity and worker's health and safety: '[t]he broad objective is to improve the conditions in which people work – to protect workpeople from hazards and to ensure so far as practicable that their working environment is a healthy one. If legislation designed for

[96] N Bamforth, M Malik, and C O'Cinneide, *Discrimination Law: Theory and Context* (Thomson Sweet & Maxwell, London 2008) 5.

[97] J Gardner, 'Liberals and Unlawful Discrimination' (1989) 9 OJLS 1, 11. See also J Gardner, 'On the Ground of Her Sex(uality)' (1998) 18 OJLS 167, 167.

[98] A Robens, *Report of the Committee on Health and Safety at Work*, Cmnd 5043 (1972). As cited in S Deakin and G Morris, *Labour Law* (6th edn Hart 2012) 355.

this purpose is to be meaningful in practice it must allocate responsibilities realistically.'[99]

The purposive approach openly acknowledged by the courts in applying the relevant statutory provisions is a clear example of how the functional approach could work in practice, and of the advantages it would offer – most notably the explicit application of norms in line with their protective function. One of the strongest statements in this regards can be found in an oft-cited passage in *Harrods*, where the Vice-Chancellor Sir Richard Scott noted that

> in approaching the construction of [the relevant provision] we should, in my judgment, give a construction to the statutory language that is not only consistent with the actual words used but also would achieve the statutory purpose of providing a remedy to victims of discrimination, who would otherwise be without one.[100]

Two related ideas come to the fore in this passage: that the ordinary understanding of work or employment covers a much broader range of situations than the narrow current legal construction of employment, and that the scope of protective legislation has to be interpreted widely in order to give effect to its underlying aims accordingly. These factors are both noted by Mummery LJ in returning to a similar point in *Tansell*; holding that such exercises did 'not involve any unconstitutional border crossing'. [101] Finally, it should be noted that while the specific purpose may be different in distinct contexts, the basic model can be applied across employment law,

[99] Robens (n 98) 51 [163].

[100] *Harrods Ltd v Remick* [1998] ICR 156 (CA) 163 F (Sir Richard Scott V-C).

[101] *MHC Consulting Services Ltd v Tansell* (n 41) 798.

even in such specific specific contexts as equal access to employment for workers drawn from across different religious groups in the Northern Irish context.[102]

Focus on Activity, not Structures

The fact that courts can successfully grapple with the core idea underpinning the functional approach, ie, that regulation should focus on the activity in question rather than its formal structural setup, is best illustrated in the context of the provisions of the Health and Safety at Work Act 1957. This Act imposes a wide range of general duties on 'every employer to ensure, so far as is reasonably practicable, the health, safety and welfare at work of all his employees'.[103] Furthermore (and crucially for present purposes), employers are to 'conduct [their] undertaking[s] in such a way as to ensure, so far as is reasonably practicable, that persons not in [their] employment who may be affected thereby are not thereby exposed to risks to their health or safety.'[104] On the one hand, this approach evidently still divides between employees defined in a narrow sense as working under a contract of employment,[105] thus reinforcing formalistic distinctions. On the other, it also includes within its scope all those 'doing work', a category defined to include the self-employed.[106] For present purposes, the provisions can however be treated as identical: as Howes suggests, the sections impose the same kind of 'basic duty […] upon the defendant company to make sure

[102] Fair Employment (Northern Ireland) Act 1976; *Kelly v Northern Ireland Housing Executive* [1999] 1 AC 429 (HL).

[103] Health and Safety at Work Act 1974, s 2(1).

[104] ibid s 3(1).

[105] ibid s 53.

[106] ibid s 52.

that their business (undertaking) is operated (conducted) in such a way that employees and other people are not exposed to risk.'[107]

By focusing on the business activity itself, the provisions leave employers few chances to evade liability with technical arguments based on complex corporate or contractual structures. The point is well illustrated in *R v Mara*,[108] where a retail employee was injured by defective equipment (provided by a third party contractor) outside the store's opening hours. The Court of Appeal was quick to dismiss the contention that activity should be defined narrowly, which would have left the protective duty applicable during store opening hours only.

This functional focus on the activity is even more explicit in one of the leading cases under section 3(1) of the Act, *Octel*.[109] There, the employee of a specialist contractor was severely injured as a result of an explosion in a tank which he had been sent to repair. Under a narrow approach to business activities, it could be argued that the actions that led to the injury were merely ancillary: the defendant company operated a chlorine works, not a fibreglass repair business. This narrow interpretation was however rejected by the House of Lords.[110] Lord Hoffman, with whom the other four Law Lords agreed, unambiguously held that the duty in question was 'defined by reference to a certain kind of activity, namely, the conduct by the employer of his undertaking. It is indifferent to the nature of the contractual relationships by which the

[107] V Howes, 'Commentary: Duties and Liabilities under the Health and Safety at Work Act 1974: A Step Forward?' (2009) 38 ILJ 306, 307; citing *R v Gateway Foodmarkets Ltd* [1997] IRLR 189 (CA) and *R v British Steel* [1995] IRLR 310 (CA).

[108] *R v Mara* [1987] IRLR 154 (CA).

[109] *Octel* (n 46). See B Barrett, 'Commentary: Employers' Criminal Liability Under HSWA 1974' (1997) 26 ILJ 149.

[110] *Octel* (n 46) 1548 D.

employer chooses to conduct it.'[111] The cited provisions of the 1974 Act are thus an excellent example of the functional approach to defining the employer in English law: they allow for purposive interpretation, and allow the court to assess the actual fact pattern to determine which entity, or combination of entities, has played a decisive role in the exercise of a regulated function.

Before turning to the next points, it will be helpful to briefly pause and set out an overview of the scope of the statutory scheme of discrimination law. Historically regulated under a wide variety of measures such as the Race Relations and Sex Discrimination Acts, the relevant provisions are now found in the Equality Act of 2010; nearly all are however materially identical for present purposes. The Act crucially extends the notion of the employer in two distinct ways. First, by broadening the definition of employment to include 'employment under a contract of employment, a contract of apprenticeship *or a contract personally to do work*'.[112] Under this wording, temporary agency workers may find themselves classified as employees of their agency: in *EDS*[113] the claimant was in a fairly standard agency setup with Brook Street Bureau when she was allegedly dismissed on grounds of her recently discovered pregnancy. On a preliminary hearing as to her eligibility to bring a sex discrimination claim under the relevant provisions,[114] it was held that while she did not qualify as an employee of the end-user, such a relationship existed with the agency for the purposes of the Act. That said, the definitional extension nonetheless quickly runs into contractual shackles, especially as it has been interpreted as continuing to require mutuality of obligation. In rejecting a taxi driver's claim under

[111] ibid 1547 B-C.

[112] eg Race Relations Act 1976 (RRA), s 78; equivalent provisions in Sex Discrimination Act 1975 (SDA), s 82 and Employment Equality (Religion or Belief) Regulations 2003 (2003 Regs), reg 2. Today all these are replaced by the Equality Act 2010, s 83(2) of which is materially identical.

[113] *EDS v Hanbury* [2001] UKEAT 128 00 2903, [2001] All ER (D) 369 (Mar).

[114] SDA, s 82(1).

the Race Relations Act 1976 because the relationship with the taxi company formally consisted of no more than an obligation to pay the weekly rent for the taxi meter and ancillary equipment,[115] Buxton LJ explicitly noted the narrowness of the contractual requirement as a key difficulty for discrimination law coverage.[116]

With a hint of linguistic irony, the second extension, on the other hand, breaks free from this narrow limitation. Section 41 of the Equality Act 2010 decrees that: [117]

> (1) A principal must not discriminate against a contract worker
>
> […]
>
> (5) A "principal" is a person who makes work available for an individual who is—
>
> (a) employed by another person, and
>
> (b) supplied by that other person in furtherance of a contract to which the principal is a party (whether or not that other person is a party to it).
>
> […]
>
> (7) A "contract worker" is an individual supplied to a principal in furtherance of a contract such as is mentioned in subsection (5)(b).

The effect of these provisions is that 'contract workers' can bring claims against 'principals' for whom they work, despite the lack of a direct contractual relationship. This openly functional approach brings with it a range of additional advantages.

[115] *Mingeley v Pennock and another (t/a Amber Cars)* [2004] EWCA Civ 328, [2004] ICR 727.

[116] ibid [19].

[117] RRA, s 7; SDA, s 9; 2003 Regs, reg 8; Equality Act 2010, s 41. A full explanation of equivalence can be found, eg, in T Royston, 'Agency Workers and Discrimination Law; *Muschett v HM Prison Service'* (2011) 40 ILJ 92, fn 1.

Moving Beyond Contractual Formalism

It has already been seen how a functional approach allows the courts to focus on regulating actual activity. The contract worker provisions show the other side of that coin: once the function of a relationship, rather than its formal setup, is relevant, traditional puzzles such as who a particular contract is with, what precisely each contract is for, or indeed how many contracts there are in the setup overall, can safely be disregarded.

The leading example for this proposition is the case of *Tansell*, a multi-entity scenario where the contract worker provisions were tested beyond the narrow agency work paradigm. As opposed to the normal triangular setup (which is undoubtedly caught by section 41), an additional company was present in the setup, linking Mr Tansell with his own company to the defendant insurance company via MHC, an employment agency. In reality, the computer technician worked directly on Abbey Life's systems. In defending Mr Tansell's disability discrimination claim, alleging that he had been dismissed following a diagnosis of diabetes, the insurance company argued that the relevant provisions did not apply in their setup, as there was no direct supply contract. The Court of Appeal dismissed this assertion, focussing on the reality of the situation and thus avoiding an unduly narrow interpretation of the provisions. The simple insertion of an additional contractual layer could not defeat the entire anti-discrimination regime: 'the language of the section is […] reasonably capable of applying to the less common case in which an extra contract is inserted'.[118]

The rejection of contractual formalism went a step further in other cases, holding that the provisions applied well beyond the agency or 'supply of worker' setting. In *Harrods*, a franchise contract between the department store and individual goods

[118] *Tansell* (n 41) 797. This point now made explicit by the Equality Act 2010.

manufacturers provided the relevant contractual background; [119] in *Bassi* the contractual agreement was for the delivery of concrete. [120] The flexibility even developed as far as to challenge mutuality of obligation, the very core of the traditional formalistic approach. In the recent decision in *Pegg*, the restrictive approach taken in *Mingeley* (the taxi driver's case, above) was explicitly distinguished for the purpose of the 'contract worker' definition: the court found that there had been a duty to work personally once a particular assignment had been accepted by the claimant. [121]

This is a clear strength of the functional approach, as embodied in the notion of the principal in employment discrimination: what matters for regulatory purposes is the employer's activity, ie the making available of work. It is to that employer function that the relevant obligations attach, regardless of how their provision is contractually structured. The parties remain free to structure their commercial relationships as they see fit; indeed they may even gain flexibility by no longer needing to consider the employment law implications of particular setups. Courts will of course continue to take contractual structures into account, but they are merely one factor in looking at the exercise of employer functions. The EAT's acceptance of counsel's submission that 'the tribunal erred in law in limiting its consideration to the formal contractual position' [122] in *Croke* [123] echoes the earlier words of Lord Hoffman

[119] *Harrods* (n 100).

[120] *CJ O'Shea Construction Ltd v Bassi* [1998] ICR 1130 (EAT).

[121] *LB Camden v Pegg* [2011] UKEAT/0590/11/LA, 2012 WL 1357842.

[122] *Croke v Hydro Aluminium Worcester Ltd* [2007] ICR 1303 (EAT). Note the different context of whistleblower protection under ERA 1996, s 43K(1) which for present purposes can be considered equal to the other discrimination cases cited. See also *Woodward v Abbey National plc (No 1)* [2006] ICR 1436.

[123] *Croke* (n 122) [25], [41].

in *Octel* that a functional approach can legitimately be 'indifferent to the nature of the contractual relationships by which the employer chooses to conduct [its business].'[124]

The Exercise of Employer Functions across Multiple Entities

The current notion of the employer is driven to a certain extent by functional thinking, for example insofar as it seeks to attach employer obligations to the party having control over an employee and benefitting from his or her work. The unitary strand, on the other hand, leads to a struggle once multiple entities become involved, with the intuitive response that in the absence of a single identifiable counterparty, no entity should be made to bear the protective obligations. A functional solution approaches this problem by turning it on its head: it recognises that multiple entities can exercise employer functions such as having control over or receiving the benefits of an individual's work, and responds to this by holding each entity responsible accordingly.

A practical example of this point can be found in *Laing*,[125] where the claimant worked for a charity providing advocacy services to patients in a psychiatric hospital. As a preliminary point in a discrimination claim, the clinic argued that it could not be a principal, because the work done was not 'work for the principal' in the sense of the relevant Act.[126] It submitted that Mr Laing had worked as an independent advocate, and that it was therefore not difficult to envisage situations where that work would be directed *against* the hospital; indeed given the nature of its patients, that was frequently to be expected. In addition to not benefitting form the claimant's efforts, the clinic furthermore had no right of control or direction over his work. The EAT

[124] *Octel* (n 46) 1547 B-C.

[125] *Partnership in Care (t/a The Spinney) v Laing* [2006] UKEAT/0622/06/DA, 2007 WL 1425705.

[126] ibid [15].

disagreed with this narrow interpretation of employer functions, finding that inherent powers of control such as permitting the claimant access to its security facilities easily sufficed.[127] As regards the benefit of Mr Laing's work to the hospital, the fact that the work could also be seen as being for the benefit of others did in no way detract from the fact that the latter had also benefited, even if only indirectly.[128]

In *Bassi*, a similar point was made in an entirely different context: the claimant lorry driver worked (in the broad sense of that term) for a company selling ready-mixed concrete. In the course of a delivery, he was allegedly racially abused by a banksman in the employment of the purchaser of the goods. The fact that he worked for the concrete vendor did in no way preclude the court's finding that his work was also for the company which received and used the concrete.[129] As regards work done for a multiplicity of employers, the Court of Appeal went even further in *Woodhouse*.[130] There, the claimant worked for a company providing management services to a local council under a complex housing outsourcing arrangement when the alleged racial abuse by a council staff member took place. It was held that control or even influence were not necessary ingredients of 'doing work for' a particular party, but rather that the situation had to be analysed in the round;[131] on that basis the Council clearly qualified as a principal for purposes of the Race Relations Act.

[127] ibid [22].

[128] ibid [21].

[129] *Bassi* (n 120) 1138 A.

[130] *Leeds City Council v Woodhouse* [2010] EWCA Civ 410, [2010] IRLR 625.

[131] ibid [27].

The Outer Limits of the Functional Approach

The final point which remains to be made in illustrating the operation of a functional approach is as to its inherent limitations. Previous discussion asserted that the functional approach had inbuilt limitations, and drew on the *Shanahan* case to show how tribunals are comfortable with the drawing of such boundaries. The contexts discussed in this section provide further illustration. One way in which the boundary issue can arise in the Health and Safety context, for example, is as to whether an employer's precautionary obligations are limited to activity taking place on its business premises; a clear limit akin in that sense to the received role of the contract of employment. As the answer is in the negative, critics of a functional approach may be worried about its potential to cast the net too wide, including in business activity items such as 'any repairs, cleaning or maintenance, wherever and by whomsoever they may be done, form part of the conduct by the employer of his undertaking […] the cleaning of the office curtains at the dry cleaners; the repair of the sales manager's car in the garage, [and] maintenance work on machinery returned to the manufacturer's factory.'[132] As Lord Hoffman made clear in *Octel*, however, this danger is significantly overstated. Applying the first shoots of the relational-functional limits as outlined above, his Lordship held that activities such as those described could not be 'fairly described as the conduct by the employer of his undertaking',[133] and expressed confidence in the ability of courts at first instance to draw appropriate distinctions.

A broader point was made by Nicholson LJ in *Jones*, in confronting the suggestion that a purposive interpretation of the scope of contract worker provisions would lead to too many spurious claims. The functional approach in and of itself provides a key

[132] *Octel* (n 46) 1548F.

[133] ibid H.

limitation: only those with the power to take relevant decisions in the first place will be potential respondents to a discrimination claim.

> I am not impressed by the 'floodgates' argument […]. If the principal is not in a position to discriminate against an 'employee' of the person who supplies that individual under a contract with the principal, any claim brought against the principal must, inevitably, fail. And it seems to me that an industrial tribunal should be able to deal with claims [… to] ensure that a genuine case of discrimination can be redressed.[134]

In combination with the previous sub-section, discussion of these different statutory areas has thus served to illustrate from various angles what a functional approach would look like in practice. It may be worth reemphasising at this point that nothing in this chapter should be taken as a suggestion that a functional approach is already inherent in the current setup. Instead, the aim was simply to show how the courts would be able to implement a functional model, not least on the basis of existing techniques, and furthermore to demonstrate how such change would address many traditionally problematic questions. The purely domestic choice of examples here, finally, is complemented by similarly functional approaches on the European level: the ECJ's willingness to purposively interpret employment law norms was made clear in *Allonby*;[135] and the specific extension of this approach to the notion of the employer was discussed extensively in part two: in *Albron*,[136] the ECJ explicitly held that the Acquired Rights Directive should apply equally to 'non-contractual employers'.

[134] *Jones v Friends Provident Life Office* [2003] NICA 36, [2004] IRLR 783 [28].

[135] Case C-256/01 *Allonby v Accrington and Rossendale College* [2005] ECR I-873.

[136] Case C-242/09 *Albron Catering BV v FNV Bondgenoten* [2011] All ER (EC) 625.

SUB-SECTION 3: ALLOCATING RESPONSIBILITY

In exploring the implications of multi-entity employment, the final section of part one of this thesis set out different modes of sharing employer functions. The following paragraphs will explore whether the functional approach proposed can provide the conceptual apparatus for different modes of ascribing liability to more than one entity, in line with the multiplicity of possible scenarios. Three broad groups of fact patterns have previously been identified: functions might be bundled into one entity, parcelled out between different entities, or shared between two or more entities. The first of these modes is the paradigm situation: a single individual or entity exercises all functions.[137] In *shared exercise*, some functions of the employer are simultaneously vested in more than one party. Such sharing of a decisive role in the management of labour functions can be found in contexts as diverse as the classic example in *Hill v Becket*,[138] where a coal yard employed a foreman to be in charge of a gang of workers, to Private Equity fund setups and corporate groups. When functions are *parcelled out*, on the other hand, distinct entities fulfil mutually exclusive roles. The best illustrations for this can be seen in the context of triangular work relationships. Finally, there is the possibility of multi-modality, ie that in the context of a single worker some functions are exercised jointly whilst others are parcelled out – such as in triangular situations where both agency and end-user have the right of dismissal.[139] If the functional approach proposed is to be neither under- nor over-determinative, it must be able to successfully work with multiple modes of attribution, in line with the complex realities of how multiple entities can share employer functions.

[137] Such as the franchisee in *Narich Pty v Commissioner of Payroll Tax* [1984] ICR 286 (EAT).

[138] *Hill v Beckett* [1915] 1 KB 578 (HC).

[139] *Construction Industry Training Board v Labour Force Ltd* [1970] 3 All ER 220 (HC).

Before turning to a more detailed exploration of such avenues, however, it is important to clarify a point that has been obliquely running through the previous sections, without being explicitly brought to the fore. The proposed functional reconceptualisation does *not* lead to a major expansion of liability, in the sense that every entity which exercised, or had a decisive role in the exercise of, a particular function towards a worker will become liable as a counterparty to all employment-law related claims brought by the individual. Such a full liability approach is to a certain extent reflected in French 'legal doctrine and case law on economic and social unity',[140] and may have some superficial advantages: there would be no need for difficult causation enquiries, and the employee could go after whichever entity is the easiest one to sue,[141] be that on jurisdictional grounds or because of a particular entity's deep pockets. On closer consideration, however, it would not be a feasible, or indeed desirable, model to suggest under a functional approach.

First, as Collins explains in his seminal article, it would be very hard indeed to square such a wide extension of liability with the existing common law approach of ascribing responsibility which is driven by capital boundaries even in complex economic organisations.[142] There is a crucial analytical distinction between holding multiple individual entities within a group or other multilateral setting liable, and ascribing responsibility for a particular action to the group as such. Muchlinski, writing in the context of enterprise entity theory, ie the idea recognizing 'corporate group[s] as a distinct form of specialized legal regime'[143] suggests a series of further concerns with such a 'full liability' approach, which can be extrapolated into all multi-

[140] Marie-Laure Morin (n 41), citing there G Teubner, "Nouvelles formes d'organisation et droit" (1993) 96 Revue Française de Gestion 50.

[141] D Brodie, 'The Enterprise and the Borrowed Worker' (2006) 35 ILJ 87, 91 is critical on this point.

[142] Collins (n 42) 732.

[143] P Muchlinski, *Multinational Enterprise and the Law* (2nd edn OUP 2007) 317ff.

entity settings. The determination of outer boundaries can become fiendishly difficult when 'contemporary ideas [of business organization are] used when constructing legal duties of care'.[144] Trying to place obligations directly on the 'group' or another cluster of multiple entities would furthermore fall back into the trap of assuming excessive homogeneity in the practical manifestations of the notion of the employer. Finally, as Teubner has noted,[145] the 'full liability' approach will quickly tend to become hierarchical, ie it will develop mechanisms that try to ascribe liability or impose obligations to some form of head or parent entity – and thus fail to take account of the many factual variations where different entities exercising employer functions are not in a hierarchical relationship.

Given the range of possible multi-modal combinations, a more flexible approach is required: just as employer functions can be divided up in different ways, so can different obligations be placed on entities exercising them. Subsequent paragraphs explore different avenues which could ensure that this happens – again emphasising that while traces may already be found in different parts of English law, it is not to be taken as a suggestion that a coherent underlying approach is already in place.

That the singular entity scenario is not a problem for the functional approach has already been amply discussed: as all functions are exercised together, appropriate obligations will point in the direction of the employer. The question does not change significantly where functions are cleanly parcelled out between different employers, for example where one entity controls the work and another entity pays the worker. A functional approach can easily grapple with this kind of scenario by allocating particular responsibilities to individual entities; indeed that approach is likely to

[144] ibid 320.

[145] ibid 321, citing G Teubner, 'Unitas Multiplex: Corporate Governance in Group Enterprises' in D Sugarman and G Teubner (eds) *Regulating Corporate Groups in Europe* (Nomos 1990) 67, 87 – 92.

become the default position in the model developed, above. It is also in line with the functional model developed by Deakin which, as already discussed, identifies functions of 'managerial coordination' and 'risk' and proceeds to attach the relevant obligations to the exercising entity.[146]

It is in the context of truly shared exercise of employer functions and the overlap of different modes that matters become somewhat more complicated. Guy Davidov has developed his own high-level version of a functional account of the notion of the employer.[147] Whilst focused on other functional factors, such as democratic deficits and dependency,[148] his account is similar enough to allow for a comparative discussion of different remedial approaches. In the context of what are termed 'truly triangular relationships', where different entities exercise different functions to overlapping degrees, Davidov does not appear to be convinced by the approach just outlined: the divison of 'responsibilities is bound to be more complicated and might fail to ensure that workers are protected.' The only way to avoid this is the placing of 'all responsibilities on both [entities] jointly and severally.'[149]

Davidov goes on to concede that sometimes one specific entity may be required as a counterparty to avoid confusion, for example in the area of tax enforcement, but reaffirms that with 'employment standards and collective bargaining laws, the best solution seems to be the placing of joint responsibility.'[150] The present sub-section advocates a refinement of this model: just as the functional approach is context-specific and domain-flexible in its identification of employing entities, so it should

[146] Deakin (n 6).

[147] Davidov (n 39).

[148] Davidov (n 34).

[149] Davidov (n 39) 740.

[150] ibid.

also be in its remedial stage: in some shared-exercise scenarios this may mean the imposition of joint and several liability (though at least at present, this will only work in a relatively small subset of cases as the next paragraphs show), in others, reliance on a regime of primary and secondary liability.

The possibility of dual or joint and several liability in a multi-employer context was discussed in *Viasystems.*[151] There, the claimant had contracted for the installation of air conditioning in his factory; the work was done by a range of sub-contractors. When a negligent fitter's mate of one such subcontractor caused a flooding of the premises while under the supervision of another sub-contractor's employee, the question as to the identity of his employer or employers arose for the purposes of vicarious liability. The Court of Appeal was clearly aware that it was operating on novel territory; after a detailed survey of the authorities it found that traditional arguments in favour of single-entity liability were primarily based on unchallenged assumptions.[152] It therefore went on to explicitly embrace a functional approach, giving 'precedence to function over form',[153] in order to avoid 'an artificial choice required by an inflexible rule of law'.[154] On the facts, it was found that the relationships yielded dual control, ie that both the second and third subcontractors had exercised regulated employer functions.[155] Responsibility (in the sense of vicarious liability) fell in line with that: both employers were found to be liable for half the damage caused.

[151] *Viasystems (Tyneside) Ltd v Thermal Transfer (Northern) Ltd* [2005] EWCA Civ 1151, [2006] QB 510.

[152] eg ibid [76] (Rix LJ); [12], [46] (May LJ).

[153] ibid [55]; cf also the references to function and purpose of the doctrine more broadly, eg [77]; R Stevens, 'A Servant of Two Masters' (2006) 122 LQR 201.

[154] *Viasystem* (n 151) [19].

[155] ibid [79-80]. Rix LJ is somewhat more sceptical whether control is the only criterion, considering also the possibility of 'practical and structural considerations'.

Whilst *Viasystems* is an important case in showing potential avenues for the operationalization of the functional notion, it should – at least on present terms – not be read too far. The finding of a clear and equal sharing of employer functions will only be applicable to a reasonably small set of multi-modal employer function exercise,[156] particularly in some of the group structures under scrutiny. Furthermore, obligations placed on the employer cannot (and should not) be reduced to liability for the payment of financial compensation. Depending on the regulatory context and the factual setup, additional ways of sharing responsibility are required.

Indeed, upon reflection some of Davidov's own examples do not always go as far as suggesting the imposition of full joint and several liability, in the technical sense of that term, in all setups and contexts.[157] His model is underpinned by a more sophisticated approach, which may be termed a model of primary and secondary liability – an approach that is surprisingly close to some examples that can be found in English law. When it comes to the regulation of Minimum Wage levels in the agency labour context, for example, Davidov suggests coordination between entities, with the end-user under a duty to monitor compliance, and in the case of payment failure, a duty to step in and assure wages are paid, at least for the period of work with the end-user. There are a range of different ways to implement such an approach in practice.

The functional notion advocated can assure such a tiered approach to employee protection: with several of the employer functions identified, there will usually be one lead or primary party responsible for its exercise – even in a multi-entity setting. In the first instance, it is that entity which should bear the relevant employment law obligations; without undue deference to formalism, however, in case backup becomes

[156] A Dugdale and M Jones, *Clerk & Lindsell on Torts* (20th edn Sweet & Maxwell 2010) 4-29; see also Brodie (n 141).

[157] Davidov (n 39) 740.

required. The operation of such a tiered model can be illustrated through the National Minimum Wage Act 1998, section 34 of which is designed to ensure the protection of 'agency workers who are not otherwise "workers"'. Sub-section two provides that:

> […] where this section applies, the other provisions of this Act shall have effect as if there were a worker's contract for the doing of the work by the agency worker made between the agency worker and—
>
> (a) whichever of the agent and the principal is responsible for paying the agency worker in respect of the work; or
>
> (b) if neither the agent nor the principal is so responsible, whichever of them pays the agency worker in respect of the work.

The tiered, functional approach is clearly visible in this provision: whoever is responsible for the exercise of the employer function, is under the primary obligation pursuant to subsection (2)(a). In the absence of clear responsibility, subsection 2(b) places responsibility on whichever entity actually effected the payments. It is furthermore not the only example of such regulation: a substantially identical approach applies in the working time provisions.[158]

Other contexts provide further illustrations of possible variations on the primary and secondary liability model that seems to be the unspoken thrust of Davidov's argument. One such variation can be found in the reasonable adjustments provisions, a duty placed on employers by the now historic section 4A of the Disability Discrimination Act 1995.[159] This duty extended to principals of contract workers under the model already discussed, above.[160] In terms of apportioning responsibility, however, principals only came under the obligation to make reasonable adjustments to

[158] Working Time Regulations 1998, SI 1998/1833, reg 36.

[159] In the Equality Act 2010, this duty is squarely based on both entities by s 41(4): 'a duty to make reasonable adjustments applies to a principal (as well as to the employer of a contract worker).'

[160] DDA 1995, s 4B(6).

the extent that the employer wasn't already required to do.[161] A final possible variation under a functional approach would be to find different degrees of obligation placed on separate entities. This can be seen, for example, in the in already discussed Health and Safety context: in *Swan Hunter Shipbuilders*,[162] a company was held to owe a higher duty to employees of subcontractors than to its own employees. The former had not been instructed in the proper use of oxygen tools, as a consequence of which several workers died: as the subcontractors could not be expected to have instructed their workers in the use of specific equipment, the higher duty fell on the principal.

This survey of how a functional notion of the employer may be put into practice has thus shown up a wide range of potential avenues, whether in contract, tort, or statutory provisions. It has been demonstrated how a functional approach would work both in terms of identifying employers and ascribing responsibility to them, and that several of the most vexing problems in the current setup could easily be solved. At the same time, it was not suggested that any of the examples identified come together to form a coherent doctrine. Indeed, it may be apt to recall at this point the warning noted by Davies and Freedland (in discussing the decision in *Tansell*) that piecemeal extensions, leading to a 'willingness to move directly along a chain of intermediaries [do not in and of themselves] satisfy the demand for imaginative legal recognition of complex multipolar work situations.'[163] Similarly, while activity liability in the health and safety context was seen as a good example of functional approach, many of its aspects continue to be hemmed in by the contractual framework, leading to 'serious doubts about the ability of the current regulatory framework for health and safety in

[161] DDA 1995, s 4B(7); H Johnson, 'Contract Workers – Disability Discrimination and Reasonable Adjustments' (2009) 90 Employment Law Bulletin 6.

[162] *R v Swan Hunter Shipbuilders Ltd* [1981] ICR 831 (CA).

[163] Davies and Freedland (n 10) 290.

Britain to adequately control the risks' to employees from the rise of 'networked forms of organisation encompassing the externalisation of work activities.'[164]

As the introduction to part three noted, the eventual solution to the underlying problem lies in a reconceptualisation of *both* strands of the notion of the employer, its functional and its unitary one. The latter will be the task of chapter six; before discussion can move to there, however, one last task remains for the present reconceptualisation of the functional strand. The examples developed in the preceding sections will be evaluated against the criteria developed in the conclusion to part two, with particular attention to two crucial features of the functional notion as illustrated: it makes employment law coverage resilient against rapidly changing complex fact patterns, by allowing for the recognition both of different contexts or regulatory domains, and for the ascription of liability to multiple entities where necessary.

SECTION III: EVALUATION

The overarching goal of this thesis is to explore the notion of the employer in English law and respond to any problems that may emerge with a coherent reconceptualisation. In consequence, the eventual test to which part three must stand up is whether it addresses the underlying tension head-on. In concluding chapter five, it is too early to apply that criterion: the preceding enquiry only constituted the first of two steps in the reconceptualisation. This observation is however not a suggestion that the functional notion developed thus far cannot be evaluated on its own terms. Three criteria emerged from the work in part two as crucial preconditions for a successful rethink: the proposed reconceptualisation has to be capable of accommodating a differentiated view of different domains of employment law; the proposed change needs to be one of careful overall evolution, and the new notion needs to be able to be

[164] P James et al, 'Regulating Supply Chains to Improve Health and Safety' (2007) 36 ILJ 163, 186.

resilient to quick market-driven changes in the legal structures and commercial operations of enterprise. The present section will apply these criteria in turn; with a return to the larger underlying question postponed until the conclusion of part three.

Domain Specificity

The first aspect of the functional approach to be evaluated is its ability, indeed encouragement, to work with the emerging understanding of labour law as consisting of a range of different regulatory domains. In designing the evaluation criteria at the end of part two a second, parallel, tension underpinning the existing notion of the employer was noted, in the form of an assumption that the employer must always be the same, substantively identical, singular entity across a unified body of employment law. The functional approach, on the other hand, permits a perception of the subject as constituted by a range of different domains. It even goes further in this regard, by allowing for an additional analytical subdivision of these domains, and an analysis of at least three relevant sub-aspects: different areas will frequently have different aims, rely on a combination of different regulatory techniques to achieve them, and, crucially, the role of the employer will differ accordingly.

Before exploring this point further, it must be acknowledged that such a multi-domain analysis of employment law is far from being analytically settled, or even uncontroversial. It is therefore important to emphasise that an analysis of labour law as consisting of different domains is not at odds with the account by Deakin and Morris that labour law today can be seen 'as a unified discipline which has outgrown its diverse origins in the law of obligations and in the regulatory intervention of the state [to become] a subject with its own doctrinal unity and structure.' [165] The emphasis on external coherence there is not to be mistaken with a suggestion of

[165] Deakin and Morris (n 98) 1.

internal homogeneity. The latter view may lead to mistaken criticism of the functional approach, as seen for example in Wynn and Leighton's concerns in response to the doctrine of implied contracts, when they suggest that the result of the functional approach in cases such as *'Muscat* is to impose liability on the party who is perhaps least suited to shoulder responsibility for temporary agency workers, i.e. the client of the agency'. [166] With respect, such thinking is underpinned by the fallacious assumption that the unity referred to above equals homogeneity, ie that once identified as an employer, that entity must be fully liable for all employment law claims.

Fudge identifies the 'plurality of different legal contexts and legal norms that make up the broad field of employment and labour law' as one of the main sources of complexity in regulating multilateral factual scenarios.[167] What, then, is the precise meaning of this idea of different legal contexts, or domains or areas of labour law? The concept is different from the idea of sources of labour law, in that it does not suggest the drawing of stark lines between different regulatory modes such as statute and common law, or contract and collective bargaining,[168] fully subscribing to the analysis of 'the Rules of Employment [as …] a complex amalgam'[169] of different sources. It is in that sense also different from the more sophisticated analysis of the heterogeneous composition of labour market regulation developed in Freedland and Kountouris' notion of layered regulation.[170]

[166] Wynn and Leighton (n 86) 302.

[167] Fudge (n 25) 304.

[168] Though there is some utility in exposition: Deakin and Morris (n 98) 57.

[169] M Freedland and P Davies, *Kahn-Freund's Labour and the Law* (Stevens 1983) 51.

[170] Freedland and Kountouris (n 15) 96.

'Labour regulation occurs at different levels and is multi-dimensional, serving a variety of instrumental goals and responding to different normative concerns.'[171] For present purposes, the domains can best be understood as concrete areas of labour law regulation, without suggesting mutual exclusivity or that a definite list should be drawn up. Examples of domains that have been directly touched upon over the course of this and previous chapters include non-discrimination, employment protection, and health and safety. Each area is made up of different layers: in the domain regulating employees' remuneration, for example, these will include the parties' contractual agreement, statutory provisions in a range of areas such as tax, equal pay and minimum wage provisions, and potentially even further layers such as the regulation of occupational pension schemes.

The key reason why a functionalist approach needs to be able to respond to this model of different domains is that each area is also a blend of distinct aims and regulatory techniques, leading to a further set of complex permutations in the role of the notion of the employer. Within the broad mantle of employment law, a range of different aims is pursued: whilst all areas tie in with the larger purpose of redressing inequality of bargaining power or regulating the labour market, the regulation of equal pay is, in that sense, very different from minimum wage provisions: crudely speaking, the former may be said to be about ensuring equality between workers, the latter concerned with ensuring minimum economic provisions. Similarly with the law of unfair dismissal, the aims of which can be seen as rather different from provisions on the information and consultation of employees: one is about balancing the employer's interest in having a flexible workforce and the employee's on-going interest in a stable relationship, the other about giving workers a voice in corporate decision making that may influence the on-going existence of certain jobs. The broad range of regulatory

[171] Fudge (n 25) 304.

sources and technique has already been seen. As each domain is made up of several layers, it will combine several regulatory techniques, from implied terms of a contract and statutory provisions linked to existence of particular forms of contracts to imposing obligations or levying penalties and fines.

As a logical consequence of these variations, the notion of the employer will have very different instantiations in different contexts, 'depending on the purpose of the specific regulation in question' and possibly even the regulatory devices used.[172] Put differently, the role of the employer will be different as a result of these factors, and the notion of the employer needs to be able to respond to that fact.[173] It will only be able to do so successfully when conceived as a functional one: the same flexibility that was analysed in the preceding section to show how the functional notion *recognises* employers applies when it comes to accurately *responding* to that status.

In conclusion, therefore, the attempted reconceptualisation of the first strand has come to preliminary completion: in explaining the conceptual basis for a functional approach and developing detailed examples to demonstrate how it may be put into practice, the groundwork is laid for the next, and final task of this thesis: to reconceptualise the second, unitary strand of the notion of the employer.

Resilient Coverage

The second lesson which emerged from earlier parts was that both the unitary and the functional strand of the notion were in need of reform, but to different degrees, and indeed in different directions: as the unitary aspect is not flexible enough to respond to complex and changing fact patterns, it has to recede to a high, conceptual level. The

[172] Davidov (n 39) 738.

[173] Fudge (n 16) 636.

functional approach, on the other hand, needs to be brought to the fore – if, that is, the proposed notion can make employment law coverage resilient to a plethora of economic organisational models.

At a conceptual level, the core problem of a missing 'fit'[174] between labour law and changed employment circumstances can be traced back to the very way in which the law conceives of the notion of the employer. Nogler's work clearly demonstrated this deep link between the particular analytical method used today and employment law's lack of flexibility and adaptability.[175] The current formalistic approach cannot achieve this because of its very structure: it is either too rigid (in accepting only pre-specified models, notably, the employer as the counterparty to the contract of employment), or it is too unclear and capricious, for example where several overlapping tests are used to determine the same question. In regard of these inherent negative consequences, the functional approach proposed is the very opposite of the prevailing contractual analysis. The only answer to the increasingly complex factual matrix in which the employment relationship is embedded is to take as many factors as possible into account, including different kinds of linkage between multiple entities and different modes of sharing. As the possible permutations are seemingly endless, however, this needs to be done in a structured way. The functional notion provides such a tool: it analyses the different factors in the round, synthesising them as particular instantiations of the general criterion. The moment when it is not the presence or absence of a particular elements in and of itself that matters, but rather the *function* that element performs in the relation in question, employment coverage becomes flexible, and thus resilient to external change.

[174] L Dickens, 'Problems of Fit: Changing Employment and Labour Regulation' (2004) 42 BJIR 595, 604.

[175] Nogler (n 1) 462.

This proposition can be put to the test in the context of some of the actual scenarios that have been encountered. As discussed, Collins identified three forms of 'bonding between productive organisations': [176] ownership, contract, and authority. These can be translated, broadly speaking, into three scenarios: [177] several distinct entities exercising joint control; control diversified across independently managed entities; and more diffuse areas such as multi-employer labour outsourcing or franchising. Once multiplied by the number of modes in which employer functions can be jointly exercised across these different scenarios, a large number of possible permutations emerge. Yet, on a conceptual level they can quickly be processed by a functional notion. The key difference in the various scenarios is as to *how* the relationship between different entities is organised: it may be through shareholdings, it may be a labour supply contract, or even through franchise contract. The legal form which the relationship takes, however, serves only as one of several possible indicators of its function, ie whether it puts the relevant entity into a position of decisive influence in the exercise of employer functions. As a result, the functional approach can accept multi-polarity, and bring the full set of possible combinations back into the scope of employment law. At the same time it also keeps inappropriate parties out of the picture: a worker could have a contract of employment with an agency, for example, but that would not be determinative for health and safety purposes if the agency had no relationship with the end-user's activity that causes injury. On a practical level, this translates into an ability both to identify relevant entities, and to fasten the appropriate employment law obligations on them. The functional approach thus lives up to the 'need to be able to envisage and accept

[176] Collins (n 42) 733.

[177] J Fudge, E Ticker and L Vosko, 'Changing Boundaries in Employment: Developing A New Platform for Labour Law' (2003) 10 CLELJ 329, 361.

multipolar and multi-agency employment relations and contracts as falling within the realm of employment law.'[178]

A perhaps less obvious way in which the functional notion makes employment law coverage more resilient to economic form changes, finally, is by removing the current incentives for rational employers to exploit overly formalistic structures: changes in enterprise organisation will no longer be driven by a desire to avoid the application of particular norms. In Fudge's analysis, the existing bilateral and unitary setup may actually invite rational firms to externalise employment responsibility.[179] If the use of complex legal structures allows an entity to receive the benefit of labour without having to bear its risk, it will make sense to incur the additional transaction cost involved in setting up various subsidiaries service companies, or paying labour agencies. Under a functional approach this incentive falls away. It could thus even be seen as restoring parties' contractual freedom, returning to a position where a 'person conducting his own undertaking is free to decide how he will do so.'[180]

Relationship with the Current Approach

The methodological tension underpinning the reconceptualisation project was briefly addressed in the introduction to part three in justifying the move from an analytical-descriptive account of the notion of the employer to an openly normative suggestion of what it should (and could) become. In order to function successfully, the notion needs to leave sufficient material behind in order to break free of existing assumptions that are the cause of its conceptual limitations. At the same time, however, it cannot roam too freely, as respect for the broader framework is essential to ensure the

[178] Davies and Freedland (n 10) 284.

[179] Fudge (n 25) 301.

[180] *Octel* (n 46) 850.

solution's eventual 'fit', in the sense of being able to be superimposed onto existing law.

The functional notion of the employer achieves this balancing act in two ways. First, on a conceptual level, by building in its approach on the existing multi-functional notion of the employment relationship as embodied in the different tests for employee status: the common law is conceptually capable of identifying particular employer functions, both in order to regulate them and to determine who should be the subject of that regulation. The reconceptualisation will, of course, also have to involve significant modifications; primarily of the second, unitary, strand. Even as regards the functional strand, however, some of the practical results that emerged from this chapter may initially look like bold moves: the array of potential counterparties is significantly widened; different employers can be picked depending on the context; and liability may be ascribed to more than one employer within a particular domain. By relying on the pre-existing functional strand, however, the underlying conceptual shift does not constitute a radical change in conceptual terms despite the potentially considerable differences in its practical emanations. This assertion can be further substantiated when recalling the avenues through which the functional notion could be put into practice. Again, the central proposition in practical terms – that the contract of employment moves from being the endpoint of the enquiry into to the nature of the employer to its beginning – might be seen as a drastic departure from the status quo. This is countered by the fact that there is no need to conjure up new, special technical avenues to give effect to the functional notion. It is of course true that the various contractual and statutory extensions discussed are not used in that particular way at the moment. They are however close enough to the proposed approach that the reconceptualisation, if adopted, could work within the existing framework of employment law. Indeed, as a survey of different methods showed, many of the existing extensions already contain traces of an openly functional approach. The fact

that the extension sought is thus a careful and gradual one should not be mistaken as a suggestion that the present chapters, and indeed the entire thesis, are not underpinned by a clear normative goal: to restore congruence between employment law coverage and businesses' economic activity. The respect expressed for the existing framework primarily serves the purpose of ensuring that the reconceptualised notion can be superimposed onto existing law; whilst at the same time remaining flexible enough to operate in other frameworks such as the reconsideration of employment relationships as Personal Employment Contracts.[181]

[181] Freedland (n 74).

CHAPTER VI
A SINGLE NOTION IN DIFFERENT CONTEXTS

Part one of this thesis identified the key reason why employment law regulation fails to consistently impose obligations on whichever entity or combination of entities are exercising, or have a decisive role in the exercise of, employer functions: there is a deep underlying tension between a singular unitary and a multi-functional conceptualisation of the notion of the employer. Part three set out to address the problem, by working on a reconceptualisation of both strands. Its first step, in chapter five, was to look at the multi-functional conceptualisation of the notion, and show how it could be shaped into a fully-fledged functional approach, with surprisingly little need to depart from existing structures. As a result of these relatively small adjustments, it was implicit that the other, unitary, strand (in the sense of only ever designating a single, substantively identical, entity, the immediate counterparty to the bilateral contract of employment, as the employer across all domains of employment law) would have to give way to a much larger extent. This should not be taken to suggest, however, that the price to pay for a move towards a functional notion is a complete lack of principled approaches, with the notion simply adjusting to the factual realities of each case. As the discussion in the present, final, chapter will show, reform of the unitary notion is possible without sacrificing a coherent underlying conceptualisation.

Introduction

Two steps need to be taken towards that goal. Recalling the earlier lesson that any change in approach needs to stay within existing frameworks, an initial question to be

addressed is whether the unitary strand can be refashioned without coming into conflict with other areas of the law. In analysing the original notion, chapter one identified three external factors that shaped its unitary strand. The first section of this chapter is designed to demonstrate how the law has developed in these areas, leaving the strict unitary approach of employment law out of step with its broader context; what appears to be quite radical change and a departure from the traditional unitary conception could therefore also be seen as bringing employment law back into line. Discussion then turns to the question why a unitary notion of some form is necessary in the first place: there needs to be a deep, underlying concept of the employer to ensure coherence in employment law overall. As section two will show, the assumption that the current version of the unitary notion provides such coherence is deeply flawed on a number of accounts. The proposed functional reconceptualisation, on the other hand, provides both the necessary factual flexibility and doctrinal clarity to ensure congruent employment law coverage.

SECTION I: MOVING BEYOND THE RECEIVED UNITARY NOTION

At a first glance, the practical implications of the current notion as explored in chapter three may lead one to agree with the suggestion that the law's 'traditional focus on regulation within the confines of a single organization remains largely untouched',[1] and that the functional approach proposed would therefore lead to significant upheaval in existing structures: different entities may, after all, now be held to be responsible employers, in line with different modes of joint exercise of employer functions in different contexts and combinations. Its substantive instantiations will therefore

[1] J Rubery, J Earnshaw and M Marchington, 'Blurring the Boundaries to the Employment Relationship: From Single to Multi-employer Relationships' in Marchington et al (eds) *Fragmenting Work: Blurring Organizational Boundaries and Disordering Hierarchies* (OUP 2005).

frequently appear to go against the three factors identified as crucial in shaping the original unitary notion of the employer.

First, under the wide variety of possible combinations there will be situations with more than one employer, or even different employers, depending on the domain in question: how does this work with the meaning of 'the employer' in ordinary language and the historic evolution of fact patterns? A second implication of the functional notion is that a search for a contractual link will no longer be the sole method in selecting the responsible party from an array of potential employers, which seems to go against the idea of privity, a crucial doctrine in the analysis of bilateral contracts. Third, in the context of complex corporate group 'employers', the idea of holding an entity that is not an immediate contractual counterparty liable could also be seen as a violation of each company's distinct legal personality. The following sub-sections turn to each of these three factors in order to demonstrate the absence of the perceived conflicts. Indeed, the opposite will emerge: in many respects, the unitary notion of the employer is drawn much more strictly than legal doctrine requires. A brief conclusion to this section, finally, will look at why this may have come to be the case.

SUB-SECTION 1: LANGUAGE AND FACT PATTERNS

As regards the first aspect, chapter one identified two factors that laid the foundations for a unitary notion: the singular, traditionally male, language used to describe '*the* employer', and the unitary fact patterns of early cases on the existence of a contract of service, which were soon applied as a fixed scheme to analyse more complex scenarios, even where that lead to highly artificial outcomes. Neither of these aspects, however, is conceptually as narrow as traditionally assumed.

The potential difficulty of discussing the 'ordinary' meaning of the 'employer' today has already been alluded to in the introduction to part three: the results of a

functional approach may on occasion depart from its general usage in particular factual scenarios. The present context is however a narrower one, reflecting the specific point made initially about the role of language in shaping a notion. The historic starting point from which the notion of the employer developed is the notion of the master, a single male individual in exclusive exercise of the control right over the servant: '[n]o man can serve two masters'.[2] Indeed, under the Master and Servant Acts the test of 'exlusive service' firmly entrenched that approach.[3] Even linguistically, the notion of the employer has however moved on, and can no longer be seen as admitting only of the current unitary interpretation of 'the *one* employer in all circumstances'.

Whilst it is not suggested that all instantiations of the functional notion will map neatly onto everyday usage, there are two reasons why the gap between the legal concept and the general understanding will not be particularly large: as a result of the earlier rejection of a form of group or collective liability, the proposed approach does not imply that all entities should be seen as together forming *one* employer: the exercise of a particular employer function will only make the relevant entity the employer for the purposes of that specific area of employment law. Given this domain-specificity, different employers may therefore be identified in different contexts. This analysis is made slightly more complex where the exercise of a particular function is not cleanly parcelled out between different entities, but shared: there, the test might lead to two employers being held responsible in the same domain. Despite long-established assumptions, however,[4] there is no clear-cut law rule at

2 *Yewens v Noakes* (1880-81) LR 6 QBD 530 (CA); *Sadler v Henlock* 119 ER 209, (1855) 4 El&Bl 570.

3 S Deakin and F Wilkinson, *The Law of the Labour Market* (Oxford Monographs on Labour Law, OUP 2005) 90.

4 *Viasystems Ltd v Thermal Transfer Ltd* [2005] EWCA Civ 1151, [2006] QB 510 [76].

common law today 'that an employee cannot be the servant of two masters'.[5] As the discussion of *Viasystems*, above, showed, duality of employers is legally possible without creating much linguistically difficulty. Rix LJ, for example, embraced this 'possibility of dual responsibility' where '*[b]oth employers* are using the employee for the purposes of their business.'[6]

A second potential objection to address is the contention that the leading statutory definition of the employer in section 230 of the Employment Rights Act 1996 is firmly limited to single entities. The relevant sub-sections stipulate that:

> (4) In this Act "employer", in relation to an employee or a worker, means the person by whom the employee or worker is (or, where the employment has ceased, was) employed.
>
> (5) In this Act "employment"—
>
> (a) in relation to an employee, means (except for the purposes of section 171) employment under a contract of employment, and
>
> (b) in relation to a worker, means employment under his contract;
>
> and "employed" shall be construed accordingly.

Upon closer inspection, this is not a direct, but an indirect definition of the notion, *via* the contract of employment. As has already been seen, that contractual model is more flexible than traditional analyses might suggest: there is nothing in principle to suggest that a contract of employment could not be a multilateral arrangement, therefore involving more than one party on the employer side.[7] The variety of different definitions offered in specific regulatory contexts, such as the extension in

5 ibid [40], citing *Oceanic Crest Shipping Co v Pilbara Harbour Services Pty Ltd* (1986) 160 CLR 626 (HCA) [32].

6 *Viasystems* (n 4) [77] (emphasis supplied).

7 *James v Greenwich LBC* [2008] EWCA Civ 35, [2008] ICR 545 [20].

various discrimination statutes, is further evidence that even in its statutory definition, the notion is a flexible and context-sensitive one.

Seen from the perspective of the rules of statutory interpretation, 'the employer' is of course a technical term, as it is defined in various Acts of Parliament. A lack of congruence between a term's technical and ordinary meanings is not uncommon. Blackstone noted that whilst lawyers normally ought to see words in their 'usual and most known signification', technical terms should be 'taken according to the acceptation of the learned in each art, trade and science.'[8] In discussing this choice between ordinary and technical meaning, Lord Esher suggested that

> [i]f the Act is one passed with reference to a particular trade, business, or transaction, and words are used which everybody conversant with that trade, business or transaction knows and understands to have a particular meaning in it then the words are to be construed as having that particular meaning, though it may differ from the common or ordinary meaning of the words.[9]

Even if one were to disagree with what the words 'the employer' are capable of expressing in ordinary language, the focus for present purposes is on their specific meaning in employment law. Indeed, there is a clear presumption in favour of the technical meaning as long as the notion is deployed within the intended context.[10]

The mere fact that a term has been defined in statute for some time, finally, does not suggest that its meaning cannot evolve: [11] '[t]here is […] no inconsistency between the rule that statutory language retains the meaning it had when Parliament

[8] J Bell and G Engle, *Cross on Statutory Interpretation* (3rd edn Butterworths 1995) 72, citing Blackstone's Commentaries, vol 1, 59.

[9] *Unwin v Hanson* [1891] 2 QB 115 (CA) 119.

[10] F Bennion, *Bennion on Statutory Interpretation: A Code* (5th edn Lexis Nexis 2008) 1206.

[11] D Greenberg, *Craies on Legislation* (9th edn Sweet & Maxwell 2008) 702ff is the source of most of the following examples.

used it and the rule that a statute is always speaking.'[12] This point can be illustrated briefly with reference to a concept taken from another area of the law, the notion of 'the family': even though its context and technical details are different, the notion similarly plays an important role in a specialist body of law, without however being exhaustively defined in statute, leaving the judiciary with an important interpretative role. Indeed, the family term can be a good example of the proposed functional approach in the larger sense: even though in historic parlance it would have clearly been understood as referring to a married man, his wife and their child or children,[13] it could today also be seen as including everything from large families and single parents to a homosexual couple and their adopted children.

As the House of Lord's decision in *Fitzpatrick*[14] shows, the courts' approach to the notion of the family has not been a static one. In that case, questions arose as to the transfer of a protected tenancy upon the death of the claimant's long-term homosexual partner. One of the questions that fell to be determined was whether the homosexual partner could count 'as a member of the original tenant's family'.[15] As the term was not exhaustively defined in statute, the House of Lords felt able to apply its definition in the modern context.[16] Lord Slynn, having noted that social conventions had moved on considerably from when the term first became used in 1920,[17] applied an openly functional-relational approach in updating its meaning. His Lordship looked at the 'hall marks of the relationship' such as stability and mutual

12 *R (Quintavalle) v Secretary of State for Health* [2003] 2 WLR 692 (HL) [9].

13 This can be seen in early family law textbooks, eg P Bromley, *Family Law* (Butterworth, London 1957). The author is grateful to Dr Rob George for advice on this point.

14 *Fitzpatrick v Sterling Housing Association Ltd* [1993] 3 WLR 1113 (HL). Though today see also *Ghaidan v Godin-Mendoza* [2004] 2 AC 557 (HL).

15 The term used in the (then) Rent Act 1977, sch 1 para 3(1).

16 *Fitzpatrick* (n 14), Lords Hutton and Hobhouse dissenting.

17 ibid [35 A-C].

commitment,[18] and found that the claimant's relationship clearly met them on the facts, thus bringing him within the scope of the relevant statutory provisions.

The importance of fact patterns in shaping a unitary notion has similarly declined. Even if Master and Servant were historically an appropriate paradigm employment situation,[19] not all cases before the courts dealt with simple bilateral scenarios. As a result of the increasing vertical disintegration of enterprise[20] even the notion of a single company employer is no longer entirely accurate. Chapter two showed how the reality of employment today has evolved drastically, to the extent that even relatively new models such as agency work can no longer be considered as atypical. As judiciary and academia take cognisance of these developments[21] there is an increasing expression of unease as regards the 'morally […] unattractive proposition[s]'[22] that may result from strict unitary analysis of the facts.

The practical impact of these changes can be illustrated by reference to *Vamplew v Parkgate*.[23] As discussed in chapter one, the court there held that a worker killed in the pits had been an independent contractor, rather than a servant, emphasising in particular his exercise of employer functions vis-à-vis a group of men and boys engaged to work below him. The unitary conception as shaped by master-servant work patterns meant that by acting, in part, as an employer, Mr Vamplew could not at the same time also be an employee. Today, a similar analysis would not be followed,

18 ibid 38 D.

19 Deakin and Wilkison (n 3).

20 H Collins, 'Independent Contractors and the Challenge of Vertical Disintegration to Employment Protection Laws' (1990) 10 OJLS 353.

21 *JGE v Portsmouth Roman Catholic Diocesan Trust* [2012] EWCA Civ 938, [2012] IRLR 846 [58]; E McKendrick, 'Vicarious Liability and Independent Contractors: A Re-Examination' (1990) 53 MLR 770.

22 *McDermid v Nash Dredging & Reclamation Co Ltd* [1987] AC 906 (HL) 912A.

23 *Vamplew v Parkgate Iron & Steel Co Ltd* [1903] 1 KB 851 (CA).

for example in the context of managerial employees. Whilst it is conceptually difficult to analyse the scenario with satisfactory analytical clarity,[24] there is no suggestion that a departmental manager in a large corporation, with the right to exercise a range of employer functions over his subordinates, would not *as a result thereof* qualify as an employee.

In summary, therefore, even though language and fact patterns were earlier noted as important historical drivers of a unitary notion of the employer, these factors could today be seen as arguments in the opposite direction: employment law's concept is too narrow to capture the full spectrum of its economic and social significance.

SUB-SECTION 2: PRIVITY OF CONTRACT

The second factor identified as driving the unitary notion of the employer was the casting of employment relationships in contractual terms, with contract once described as the 'fundamental legal institution' of employment law.[25] The unitary view emerges as the result of analysing the employment relationship as a bilateral contractual exchange of wages and work, with a single party at either end. This is supported by the strict assumption that a bilateral contractual arrangement may have no impact on other parties: as a result of the strict rules of privity, the idea(l) of freedom of contract in this context is equated to freedom from contract.

In returning to an analysis of the role of contract law doctrine in shaping the notion of the employer, it should be kept in mind that the accuracy of Lord Wedderburn's characterisation in the preceding paragraph is more limited than may at

[24] P Davies and M Freedland, 'The Complexities of the Employing Enterprise' in G Davidov and B Langile (eds), *Boundaries and Frontiers of Labour Law* (Hart 2006).

[25] K Wedderburn, *Cases and Materials on Labour Law* (CUP 1967) 1.

first be thought, both in its historical and potentially future significance.[26] That said, it is nonetheless important to engage with the underlying doctrine directly in order to show how it does not necessarily condition the current singular notion of the employer. Put at its most concise, the doctrine of privity in English law confines the effect of a bilateral contractual relationship to its two parties, who cannot impose a benefit or a burden on a third party.[27] As the following discussion shows, however, an exclusive emphasis on privity in contract law may frequently obscure the importance of other sources of multilateral obligations.

Whereas several continental jurisdictions have flirted with multilateral ideas such as network contracts to regulate the economic reality of multi-entity inter-dependency,[28] English law has eschewed these models for two reasons: privity, as just outlined, and a seemingly strong commitment to the principle of freedom of contract, in the sense of respecting group entities' choice not to contract with employees or each other. Other ways of dealing with the issues raised by 'complex commercial and economic relations' can nonetheless be found.[29] Even before the introduction of a statutory avenue for the creation of third party rights in 1999,[30] the courts had started to develop a series of 'juristic subterfuges'[31] in order to achieve the recognised need for flexibility. A notable example of this can be seen in the law of tort, and the tort of negligence in particular, allowing recovery for loss caused as the result of a contract,

[26] L Barmes, H Collins and C Kilpatrick, 'Reconstructing Employment Contracts' (2007) 36 ILJ 1 and subsequent articles in that special issue.

[27] But cf the Contracts (Rights of Third Parties) Act 1999.

[28] G Teubner and H Collins, *Networks as Connected Contracts* (Hart, Oxford 2011); J Morgan, 'Publication Review: Networks as Connected Contracts' (2012) 128 LQR 472.

[29] S Whittaker, 'Reciprocity Beyond Privity' in P Kincaid (ed) *Privity: Private Justice or Public Regulation* (Ashgate 2001) 180.

[30] Contracts (Rights of Third Parties) Act 1999.

[31] *Swan v Law Society* [1983] 1 AC 598 (HL), 611 (L Diplock); as quoted by Whittaker (n 29) 190.

but not under the contract itself. Whilst a detailed discussion of the tort law exceptions and their particular problems (such as regards the recovery of pure economic loss, for example) is beyond the scope of the present discussion, several crucial lessons can nonetheless be learnt from the fact that even a contractual framing of a set of facts does not limit their legal analysis to a bilateral and unitary view.

Simon Whittaker has convincingly argued that 'true exceptions' to privity can, and already have been, developed by the courts. Whilst

> parties are free in principle to agree what contracts they wish, in most situations the law's response to this agreement is to classify it and regulate its consequences. [… W]here the consequences of a (voluntary) creation of a particular relationship fall to be determined by the law, there is no logical or conceptual reason why the law should not draw consequences for third parties from its creation not merely where this can be justified by the existence of an intention in the parties to do so, but also from the nature of the contract which the parties have entered.[32]

As a broader analysis of situations is thus both within the abilities and proper constitutional role of the courts, the question arises as to how and where such policy-driven exceptions should arise. There are two crucial limitations: context-specificity, and the need for clear-cut additional criteria. As regards the former, exceptions cannot become freely available, lest they subvert the doctrine of privity completely:[33] they can only be found in limited areas (such as employment law) in line with the demands of specific policy objectives.

[32] S Whittaker, 'Privity of Contract and the Tort of Negligence: Future Directions' (1996) 16 OJLS 191, 193.

[33] S Whittaker, 'Contract Networks, Freedom of Contract and the Restructuring of Privity of Contract' in F Cafaggi (ed) *Contractual Networks, Inter-Firm Cooperation and Economic Growth* (Edward Elgar 2011) 278); citing *Law Debenture Trust Corp v Ural Caspian Oil Corp Ltd* [1995] 1 All ER 157 (CA) 364 (Hoffman J).

The need for clear-cut criteria is expressed in the idea of *reciprocity*: 'qui sentit commodum sentire debet et onus; a person who enjoys the benefit must also bear the burden.'[34] Whittaker relies on the provisions of the Acquired Rights Directive[35] as an illustration of this principle: with the acquisition of a business comes the acquisition of employment law obligations. Despite some controversy in contract law doctrine as to its precise terminology or mechanism, the principle underpinning the ARD and TUPE Regulations is a simultaneous transfer of benefit *and* burden. This is significant in two ways: the new employer, first, cannot take the benefit of an existing business without being subjected to the relevant 'burden', or employment law obligations. Second, 'it makes clear that for the future the employees' work for the new employer must be reciprocated by performance of an employer's obligations.'[36]

A strict bilateral conception of the employer is therefore not inherent in a contractual analysis of employment relationships. It should be noted that neither a particular context nor reciprocity between parties are in and of themselves enough to construe relationships beyond the contractual scope: reciprocity, for example, is *not* the justification for extending the relationship's scope; that element is primarily policy-driven. Taken together, on the other hand, these factors become very potent.[37] Their effect includes the imposition of clear outer limits in putting into effect these purposes: the reciprocity of rights and duties was at the core of the original relationship, so it should also form part of the additional benefits and obligations

34 Whittaker (n 33) 261; quoting Coke, 1 Inst 230b.

35 Council Directive (EC) 23/2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses [2001] OJ L 082/16.

36 Whittaker (n 33) 268.

37 ibid 283.

recognised by law as existing between contractual non-parties.[38] This model is very close indeed to the functional approach as advocated, in looking at the exercise of employer functions in particular relationships to attach regulatory obligations. It is equally context specific, and functions exercised as a result of a reciprocal relationship are not only the trigger, but also the limitation of liability.

Even if contract continues to play a central role in shaping the employment relationship, therefore, it does not have to play the limiting unitary effect frequently ascribed to it: indeed, the courts are happy to move beyond it in a wide range of contexts. The last chapter explored several significant examples resulting from statutory intervention to impose duties on employer in the absence of a contractual relationship. Recent decisions have taken this point even further, relying on (and extending) tortious principles in the absence of contractual relationships and specific statutory regulation.

In *JGE*,[39] a victim who had been sexually abused by a priest whilst in a religious care home brought an action for tortious compensation. As the alleged abuser was no longer alive, the preliminary question arose whether the Diocese of Portsmouth (the Trustees of the Diocesan Trust being sued for that purpose[40]) could be held liable vicariously. After an extensive review of the authorities,[41] Ward LJ unambiguously found that there was no contract of service between the bishop and the priest. His Lordship thus noted that '[b]ecause there [was] no relationship of employer/employee between them, then, if one [were] judging the question on conventional lines, the

[38] ibid 270.

[39] *JGE* (n 21).

[40] As the Roman Catholic Church in England has no legal personality as such, the judgment was framed in terms of the relationship between the clergyman and his bishop: ibid [18].

[41] Including *President of the Methodist Conference v Parfitt* [1984] QB 368 (CA); *Percy v Church of Scotland Board of National Mission* [2005] UKHL 73, [2006] AC 28.

bishop is not vicariously liable for the tortious acts of the priest.' He nonetheless went on to enquire whether the bishop could 'be vicariously liable if the *relationship [was] akin to employment*? [Could] the law be extended that far?'[42]

In answering this question considerable reliance was placed on the decision of *Viasystems*, discussed above, as clear evidence of the significance of the *role*, or function, of the employer in any particular area.[43] Indeed, '[t]he actual contract of employment [there] was treated as no more than an irrelevant distraction. Function triumphed over form.'[44] Ward LJ next recalled recent extensions of the second crucial ingredient in vicarious liability, actions within the 'scope of employment',[45] before turning to the policy considerations underpinning vicarious liability to emphasise the context-specificity of the notion of the employer: 'the time has come to recognise that the context in which the question arises cannot be ignored.'[46]

In order to determine whether the present facts constituted a 'relationship akin to employment' for the purposes of vicarious liability, His Lordship extensively analysed how close the tortfeasor's relationship with the bishop was to one of contractual employment. Sufficient proximity was found, as the church could be equated to a multinational organisation, 'with the Pope in the head office, with its "regional offices" with their appointed bishops and with "local branches", the parishes with their appointed priests. This looks like a business and operates like a business. Its objective is to spread the word of God. The priest has a central role in meeting that

42 *JGE* (n 21) [31] (emphasis supplied).

43 eg ibid [39]; quoting *Viasystems* (n 4) [55] (Rix LJ).

44 *JGE* (n 21) [60].

45 *Lister v Hesley Hall Ltd* [2001] UKHL 22, [2002] 1 AC 215.

46 *JGE* (n 21) [59].

target.'[47] The 'relationship with his bishop [was therefore] close enough and so akin to employer/employee as to make it just and fair to impose vicarious liability.'[48]

It is interesting to note that whilst technically this decision was of course not a situation where an exception to privity had to be applied, it was nonetheless equally driven by the factors underpinning the proposed functional approach: context specificity, and a focus on the nature of a relationship rather than its form. Indeed, in that sense Whittaker's conclusion rings true in both scenarios: 'concentration on one contract as the basis of liability in multi-contractual situations obscures the possibility of the creation of a bilateral entitlement between the parties beyond privity.'[49] Whereas earlier paragraphs showed how the *presence* of contract is not an obstacle to multilateral imposition of liability; the decision in *JGE* demonstrates how the courts have come to view that its *absence* is not necessarily a problem, either.

SUB-SECTION 3: COMPANY LAW

In chapter one, discussion of language, fact patterns and contract as general factors shaping the unitary notion was followed by a set of factors specific to the subset of limited liability companies as corporate employers, where the crucial interrelationship between different entities is primarily driven by equity ownership. It was suggested that despite a multitude of actors, from employees and management to a board of directors and shareholders, the company has become a singular focal point for a unitary conception of the corporate entity, with powers and responsibilities perceived in anthropomorphic terms; a notion to which employment relationships then fasten.

47 ibid [77].

48 ibid [81].

49 Whittaker (n 32) 198.

Analysis focussed on the split between the three classic functions of enterprise:[50] 'having interests in an enterprise, […] having power over it, and […] acting with respect to it.' It explained how the corporate form led to their separation, in particular by breaking the link between the first pair. Once the interest in an enterprise and the power over it are no longer in the same hands, particularly in companies whose shares are publicly traded and widely held, two distinct groups emerge: 'the owners without appreciable control and the control without appreciable ownership'. [51] These developments are the background for the operation of the doctrine of separate legal personality and, as one of the consequences flowing from it, the idea of limited liability, that is to say that shareholders can limit their economic and legal risk exposure to the value of their shares, and that claims can only be brought directly against the company itself.[52]

Exceptions to this rule were characterised as the piercing or lifting of the Corporate Veil,[53] noting the Common Law's traditional hostility to the imposition of liability for a distinct legal entity's acts on the shareholders standing behind it: the veil may only be lifted (in the sense just outlined) in cases of fraud[54] or certain statutory provisions. [55] Whilst critics have noted the potential for abuse and artificial technicalities resulting from this approach, [56] a range of policy explanations have been

50 A Berle and G Means, *The Modern Corporation and Private Property* (Macmillan 1939) 119.

51 ibid 121.

52 P Davies and S Worthington, *Gower and Davies' Principles of Modern Company Law* (9th edn Sweet & Maxwell 2012) 207.

53 S Ottolenghi, 'From Peeping Behind the Corporate Veil, to Ignoring It Completely' (1990) 53 MLR 338.

54 The bar for which is set high: *Adams v Cape Industries Plc* [1990] Ch 433 (CA).

55 For example in the Insolvency Act 1986, s 213 and s 214 (fraudulent and wrongful trading).

56 O Kahn-Freund, 'Some Reflections on Company Law Reform' (1944) 7 MLR 54, 56; K Wedderburn, 'Multinationals and the Antiquities of Company Law' (1984) 47 MLR 87, 90.

adopted to support the strict line – most notably the idea that limited liability is necessary for the efficient functioning of public securities markets,[57] and the assignment of creditors to relevant economic units.[58]

The present context is a more specific one, however, as the shareholder is itself a legal person, ie a different company.[59] Such arrangements were not the paradigm situation at the origins of company law, with its emphasis on arms-length dealing.[60] As Strasser notes, 'parent companies in fact present different policy issues and their limited liability should be determined by a different analysis.'[61] 'Changes to the profile of shareholders through the emergence of corporate groups and increased participation of institutional investors in the market for shares[62] provide a principled case for corporate shareholders to be treated differently from individual shareholders.'[63] This is compounded by the fact that employees (other than as wage creditors in insolvency) are a very specific group of claimants, who may appear to be

57 P Halpern, M Trebilcock and S Turnbull, 'An Economic Analysis of Limited Liability' (1980) 30 University of Toronto Law Journal 117 (as cited in Davies and Worthington (n 52)).

58 The 'asset partitioning rationale' set out in H Hansmann and R Kraakman, 'The Essential Role of Organizational Law' (2000) 110 Yale Law Journal 387 (as cited ibid).

59 P Blumberg, 'The Corporate Entity in an Era of Multinational Corporations' (1990) 15 Delaware Journal of Corporate Law 283, 285.

60 K Hofstetter, 'Parent Responsibility for Subsidiary Corporations: Evaluating European Trends' (1990) 39 International and Comparative Law Quarterly 675, 576; J Borg-Barthet, *The Governing Law of Companies in EU Law* (Hart 2012) 58 on which citations and structure of this passage build.

61 K Strasser, 'Piercing the Veil in Corporate Groups' [2005] 37 Connecticut Law Review 637, 638; citing P Blumberg, 'Limited Liability and Corporate Groups' (1986) 11 Delaware Journal of Corporate Law 573, 575. The author is grateful to Professor Jane Stapleton for drawing these articles, as well as further cases and materials on 'veil piercing' in the US context to his attention: T Heiden, 'The New Limits of Limited Liability: Differing Standards and Theories for Measuring a Parent/Shareholder's Responsibility for the Operations of Its Subsidiaries' in Practising Law Institute (eds) *Protecting the Corporate Parent: Avoiding Liability for Acts of the Subsidiary* (PLI 1993).

62 C Bruner, 'The Enduring Ambivalence of Corporate Law' (2008) 59 Alabama Law Review 1385, 1432-33.

63 Borg-Barthet (n 60) 58.

voluntary creditors of the company, but do not in reality enjoy the freedom to bargain for their protection as perceived in most economics literature. [64] The standard rationales become difficult to defend in situations where there is a clear economic unit across legally distinct entities, and the claimants in question cannot contractually adjust to this risk distribution. After some initial equivocation, the English courts however saw no reason to hesitate in extending the orthodox position to corporate groups.[65] It is therefore perhaps unsurprising that leading authors have repeatedly concluded that 'ignoring the group structure will rarely be a policy available to the courts'.[66]

Upon closer investigation in line with the purpose of the earlier two sub-sections, however, the line may not be as clear-cut as it initially appears. In discussing exceptions to the doctrine of separate legal personality, Davies notes that there is only a narrow set of situations where such piercing may take place, in the sense of holding shareholders responsible for the debts or other liabilities of the company. While the rule in *Salomon v Salomon*[67] was intended to apply across the board, an 'impressively long' list of situations where the court have felt able to ignore separate legal personality has developed.[68] It is not surprising, then, that Easterbrook and Fischel find that '"Piercing" seems to happen freakishly. Like lightning it is rare, severe, and

64 cf the position of tort victims: H Hansmann and R Kraakman, 'Towards Unlimited Shareholder Liability for Corporate Torts' (1991) 100 Yale Law Journal 1879.

65 P Blumberg, 'The Transformation of Modern Corporation Law: The Law of Corporate Groups' (2005) 37 Connecticut Law Review 605, 607-8.

66 P Davies and M Freedland, 'The Employment Relationship in British Labour Law' in C Barnard, S Deakin and G Morris (eds), *The Future of Labour Law: Liber Amicorum for Sir Bob Hepple QC* (Hart 2004) 137.

67 *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

68 P Davies, *Introduction to Company Law* (2nd edn Clarendon Law Series, OUP 2010) 32.

unprincipled.'[69] The problem is particularly acute in groups of companies. Writing in the US context, Cardozo J noted that '[t]he whole problem of the relation between parent and subsidiary corporations is one that is still enveloped in the mists of metaphor [which] starting as devices to liberate thought […] end often by enslaving it.'[70]

Davies notes a potential path to resolving many of these puzzles, in making the 'apparently radical suggestion' that

> no single explanation for these cases will be found […] on the basis that it is possible to decide whether to ignore the separate legal personality of the company in this class of case only on the basis of an understanding of the purpose of the rule which is alleged to require this step to be taken. This is true whether the rule in question is statutory, common law, or contained in a contract.[71]

This context-specific approach means that, for example, the resolution of a particular point will be 'a matter for employment lawyers and the vital interests of company law are not implicated, whichever way the decision turns out.'[72] Turning to specific examples of that in the group context, the starting position is nonetheless the applicability of *Salomon v Salomon*.[73] There is no 'routine liability [of corporate group entities for each other], flowing simply from the fact of the existence of a parent

[69] F Easterbrook and D Fischel, 'Limited Liability and the Corporation' (1985) 52 University of Chicago Law Review 89, 89.

[70] *Berkey v Third Ave Ry.* 155 NE 58 (NY 1926), 61 as cited in A Crawley, 'Environmental Auditing and the *Good Samaritan* Doctrine: Implications for Parent Corporations' (1993) 28 Georgia Law Review 223, 223.

[71] Davies (n 68) 33.

[72] ibid.

[73] For a short-lived exception, see L Denning in *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852 (CA).

and subsidiary relationship.'[74] This is not, however, because English law lacks the necessary conceptual apparatus: there are specific exceptions in both statute and at common law, marked out by a particular domain and additional requirements that are closely related to the purpose of the rules regulating that context.[75]

As regards statute, the Companies Act 2006, for example, imposes a range of obligations on shadow directors, defined in section 251 as persons 'in accordance with whose directions or instructions the directors of a company are accustomed to act.' This provision has been held to encompass corporate shareholders.[76] One context in which the provisions play an important role is wrongful trading,[77] the additional features to trigger parent liability being closely in line with the purpose of protecting creditors in the run-up to insolvency: 'the failure of the parent company to treat the management of the subsidiary as having an independent existence, plus negligent disregard by the parent of the interests of the subsidiary's creditors in the period before insolvency.'[78] This limited, context-specific approach does not compromise the default position in company law: while a particular relationship in and of itself will not be enough to trigger liability, additional features in line with the purpose of a particular area justify the exception. Applying a single doctrine across all areas on the other hand would have asked the wrong questions, focussing on 'abstract, generalized

74 Davies (n 68) 97.

75 ibid 96-99, on which the following discussion builds.

76 *Re Hydrodan (Corby Ltd)* [1994] 2 BCLC 180, and *Re Paycheck Services 3 Ltd* [2009] 2 BCLC 309 (CA).

77 Insolvency Act 1986, s 214(7).

78 Davies (n 68) 97.

ideas of entity separateness, and of "wrongful" conduct.'[79] Despite initial appearances, no significant doctrinal change is involved in achieving this result.[80]

The approach at common law is not dissimilar. The ordinary requirements for ignoring the corporate veil have already been seen in chapter one; the threshold is very high indeed.[81] That, however, is the *general* case; in the specific context of employer obligations different requirements may be in operation, as the most recent decision resulting from Cape Industries' asbestos manufacturing activities shows. In *Chandler v Cape*,[82] the claimant had contracted mesothelioma whilst working for a subsidiary of Cape plc; that contractual employer had ceased to exist by the time of the claim. The question therefore arose whether Mr Chandler could bring a direct claim against the parent company. Whilst a separate legal entity, the subsidiary had been managed as a 'branch of the defendant'[83] within the larger group of companies, the core business of which was the manufacture of asbestos based products.[84] The court took the existence of a Group Medical Advisor and a long course of dealings between the entities as 'clear evidence that the Defendant was taking an active part in discussions relating to the health and safety of an employee of one of its subsidiaries'. There was no need to demonstrate full control over all activities of subsidiary, a focus on a particular employer function sufficed. 'It is enough [… to] establish that the Defendant either controlled or took overall responsibility for the measures adopted by

79 Strasser (n 61) 657, 660 – 661.

80 ibid 662.

81 *Adams v Cape Industries Plc* [1990] Ch 433 (CA).

82 *Chandler v Cape Plc* [2012] EWCA Civ 525, [2012] 3 All ER 640; foreshadowed in US law by *Johnson v Abbe Engineering Co* 749 F.2d 1131 (5th Circuit, 1984) as noted by Strasser (n 61) 648.

83 *Chandler* (n 82) [14].

84 ibid [23], [24].

Cape Products to protect its employees against harm from asbestos exposure.'[85] When it came to an application of the 3-stage *Caparo* test[86] to determine whether the parent company owed a duty of care to the employee of its subsidiary, the court found that it had assumed such responsibilities.

In concluding his judgment, Wyn Williams J added a crucial note to 'dispel certain possible misunderstandings'.[87] Each of the three points listed there merits brief further elaboration.

> First, the fact that the Claimant was owed a duty of care by Cape Products does not prevent such a duty arising between the Claimant and other parties.

As has already been seen in the last chapter, the functional approach evident in this judgment easily overcomes the involvement of multiple entities in the employment relationship. The fact that the subsidiary had operated its own health committee was irrelevant:[88] the employer function could be jointly exercised.

> Second, the fact that Cape Products was a subsidiary of the Defendant or part of a group of companies of which the Defendant was the parent cannot mean by itself that the Defendant owes a duty to the employees of Cape Products […] Equally, the fact that Cape Products was a separate legal entity from the Defendant cannot preclude the duty arising.

This observation confirms the important safeguard built into the proposed approach: in order to trigger liability both the particular context of a claim, and the specific functions individual factors exercise in relation to it, need to be present: the

85 ibid [49].

86 ibid [72], [77]; *Caparo Industries plc v Dickman* [1992] 2 AC 605 (HL).

87 ibid [66].

88 ibid [59].

mere existence of a corporate group is not enough unless it provides the context for further factors, in line with the relevant domain, such as health and safety on the facts of *Chandler*. The reverse implication, a further aspect of the functional approach, is equally important: formalistic distinctions will not defeat the applicability of employment law norms.

> Third, this case has not been presented on the basis that Cape Products was a sham – nothing more than a veil for the activities of the Defendant. Accordingly, this is not a case in which it would be appropriate to "pierce the corporate veil".

The outcome on the facts of the case was not one of holding the parent entity liable for its subsidiary's obligations; strictly speaking it was found to have assumed a direct duty of care itself. Functionally speaking, this is nonetheless equivalent to the ideas developed in this subsection in general[89] and the shadow director / wrongful trading scenario under section 214(7) of the Insolvency Act 1986 in particular.[90] The judge's final observation thus returns to the fact that the existence of separate legal entities, separated against creditor's claims by a corporate veil, is not logically tied to the present unitary conceptualisation of the employer. Domain-specific 'exceptions' to the corporate veil exist in a range of areas; their operation is closely aligned with the functional approach proposed.

This increasingly flexible approach to the purposive pursuit of particular regulatory aims is by no means limited to the examples discussed above. In EU Competition law, for example, the ECJ has adopted a 'single economic entity

[89] Strasser (n 61) 648.

[90] Davies (n 68) 99. Written before *Chandler* (n 82), the relevant passage cites several cases, including that of a Cape subsidiary in South Africa, as examples: *Lubbe v Cape Plc* [2001] 1 WLR 1545 (HL).

doctrine' in dealing with infringements in corporate groups;[91] there is at least one documented instance where a Private Equity investor (Goldman Sachs PE) was served with a notice on the basis of alleged infringements of Article 101 TFEU.[92]

As a result of the full development of the functional aspects of the notion of the employer in the preceding chapter, a fundamental reconceptualisation of its unitary strand has become necessary. The purpose of the first section of this chapter was to show that such a development would not be incongruent with developments in the broader areas surrounding the legal notion of the employer. In returning to the three factors identified at the beginning of this thesis as key influences in shaping the notion of the employer as a substantively identical, singular entity across all domains of employment law, it demonstrated how each of these areas has developed beyond the original features. Indeed, the case could be made out that these external developments alone exert a positive pressure for reform.

It furthermore leads to an interesting side-question as to how and why the unitary notion of the employer has continued to exert its influence over time. Freedland and Davies suggest that 'much of the sustaining ideology for the unity of the employer and the bipolarity of the employment relation comes from within employment law.'[93] The unitary notion may thus be linked, at a subconscious level at least, to a particular normative underpinning of the discipline of labour law in general, seeing its primary purpose as the recalibration of a power inequality inherent in the relationship between 'the employer' and 'his' employees; between the master and his servants. With a shift in the normativity of employment law to include the idea of labour market

91 R Whish and D Bailey, *Competition Law* (12th edn OUP 2012) 92ff.

92 L Crofts, 'Buyout Firms should heed EC Action over Cartel Liability' (mLex Market Intelligence, 25 July 2011); Slaughter & May, 'Private Equity and Competition Law: Liability for Infringements by Portfolio Companies' (Client Briefing 2011). The author is grateful to Dr Okeoghene Odudu for this point.

93 Davies and Freedland (n 24) 276.

regulation,[94] that influence (and any consequent subject-internal resistance to a reconceptualisation of the notion of the employer as a functional one) may weaken over time: indeed, it may constitute a further reason in favour of reconceptualising the unitary strand. Space limitations prohibit further development of this point; it should in any instance not be taken as a suggestion that there are no other good reasons for having a single, coherent, concept of the employer. It is this point to which discussion in the following section now turns.

SECTION II: THE DIFFERENT MEANINGS OF A UNITARY NOTION

The material discussed in the previous section provided further evidence in favour of reforming the existing unitary notion of the employer. The crucial question left unanswered there, however, was as to the precise nature of such a reconceptualisation: what goals should it pursue? On one level, it may be tempting to suggest that any search for unitary notion can simply be abandoned, with individual solutions to be developed in each regulatory domain instead. This is not a safe conclusion to draw from the analysis of the three factors shaping the received notion above, however: the purpose there was limited to demonstrating how the current approach is unnecessarily restrictive and inflexible.

The final section of this chapter therefore turns to the very nature of the unitary notion, exploring the importance of an underlying concept generally and linking this to the precise criteria against which any such approach must be evaluated. Put differently, in order to complete the final steps in the reconceptualisation of the notion of the employer, two crucial questions remain to be addressed: why is there a need to have a single, coherent notion of the employer? And, intimately related to the first

[94] See eg the essays in H Collins, P Davies and R Rideout, *Legal Regulation of the Employment Relation* (Kluwer 2000).

point, what should the nature of that singular notion be? It is suggested that the answers to both questions are driven by the historical evolution of labour market regulation, and can therefore be illuminated by drawing on the work of Deakin and Wilkinson in this area.[95]

SUB-SECTION 1: THE REQUIREMENT OF A SINGLE NOTION

For present purposes, this will be broken down into four parts: a look at the regulatory function of a single underlying concept, first, will explain on which level the reconceptualised notion needs to be a unitary one: in its *conceptual* definition of the employer. A second part then explores to what end the notion needs to provide this conceptual unity, recalling its crucial substantive task in balancing employers' control rights and risk absorption obligations. Having explored how the traditional approaches, focussed on the contract of employment as the key 'public-regulatory' device fail to achieve this, the third part explains why a specific focus on the notion of the employer may overcome the challenges faced by the broader analysis of contracts of employment, or indeed the notion of the employee. The fourth part brings these arguments together in developing a concise two-pronged test against which both existing and proposed notions of the employer will then be evaluated.

'Public-Regulatory' Functions

The need for coherent underlying norms in employment law cannot be understated. 'It is no exaggeration to think of the classification of work relationships as the central, defining operation of any labour law system.'[96] Deakin and Wilkinson have shown how this need emerged as a result of the increasing regulation of the employment

[95] Deakin and Wilkinson (n 3).

[96] ibid 4.

sphere, in particular through the 'gradual spread of social legislation in the field of workmen's compensation, social insurance and employment protection'.[97] In order to effectively regulate the wide spectrum of different factual patterns across a range of different contexts, from national insurance and taxation to employment protective legislation, a central unified model was required:[98] that model became the contract of employment. Without coherence in its underlying notions, however, the contract of employment could not live up to this 'public-regulatory character'.[99] The broader implications of the need for a unitary notion are significant: the search for a singular regulatory device is, 'in the final analysis, an argument in favour of an integrative mechanism, or set of mechanisms, which makes it possible for a market economy and a social state to co-exist.'[100]

Translated into the present context, these observations suggest a need for conceptually unified categories which are able to transcend a wide range of factual situations. The way in which the notion of the employer is traditionally seen as being unitary overshoots this requirement and therefore fails to perform its task properly, as the following sub-section will demonstrate. Its singular substantive definition (in the sense of the employer being a single legal entity, the counterparty to a bilateral contract of employment) is radically different from the *conceptual unity* that is actually required.

97 ibid 15.

98 National Insurance Act 1946; Contracts of Employment Act 1963; Deakin and Wilkinson (n 3) 94-95, 36.

99 Deakin and Wilkinson (n 3) 16.

100 ibid 109.

The Trade-Off Between Employer Control and Employer Duties

Having thus established the need for unitary concepts in labour market regulation, the question as to what the precise task of such concepts should be immediately arises. From an historical perspective, the contractualisation of the employment relationship united two previously distinct aspects in order to establish its central role: the 'placing of limits on the employer's legal powers of command' and 'the use of the employment relationship as a vehicle for channelling and redistributing social and economic risks, through the imposition on employers of obligations of revenue collection, and compensation for interruptions to earnings.'[101] Having gained a foothold in the liability of employers for injuries caused by managerial or superior staff,[102] this latter 'principle that the employer should assume responsibility for social and economic risks arising from the employment relationship began to take shape.'[103] Whilst the traditionally assumed stability and regularity of employment relationships may have become significantly weakened today, the idea of a fundamental trade-off continues to exert considerable force. The modern idea of a unitary concept should continue to be driven by the balance of a '"coordination function", which expresses the worker's subordination to the managerial power of the employer within the enterprise, and a "risk function", [which] channels the risks of economic insecurity in such a way as to protect the individual worker against the consequences of that very same dependence on, and subordination to, the employer's superior resources.'[104]

This role of the underlying concept is by no means limited to English law. As Supiot has noted in the pan-European context:

[101] ibid 15.

[102] Employers Liability Act 1880.

[103] Deakin and Wilkinson (n 3) 86-7.

[104] ibid 109.

> [u]nder the model of the welfare state, the work relationship became the site on which a fundamental trade-off between economic dependence and social protection took place. While it was of course the case that the employee was subjected to the power of another, it was understood that, in return, there was a guarantee of the basic conditions for participation in society.[105]

In the evolution of regulation as outlined thus far, the regulatory focus was undoubtedly on the employment *relationship*, as embodied in the idea of the contract of employment. Judicial interpretation of this underlying notion, on the other hand, focussed on the classification of employees in order to determine the existence of a relevant relationship.[106] In its 'public-regulatory character', the contract of employment as the underlying unitary concept was therefore called upon to perform a multiplicity of tasks, including 'classification, regulation and redistribution'.[107] It was not necessarily successful in this range of endeavours: 'the employment model can […] be seen as a construction which was imposed upon a number of different types of work relationship at the cost of varying degrees of artificiality, and which was bound, eventually, to unravel.'[108] It is submitted that the key reason for this failure was the immense rigidity as regards substantive manifestations, resulting perhaps from an overzealous quest for conceptual unity. As advocated in the introduction to this thesis, a focus on and thorough conceptualisation of the 'other party' to the employment relationship, the employer, might be a promising response to this impasse.

[105] A Supiot, *Beyond Employment: Changes in Work and the Future of Labour Law in Europe* (OUP 2001) 10, as cited in Deakin and Wilkinson (n 3) 14.

[106] M Freedland and N Kountouris, *The Legal Construction of Personal Work Relations* (OUP, Oxford 2011).

[107] Deakin and Wilkinson (n 3) 16.

[108] ibid 105.

The Notion of the Employer as a 'Public-Regulatory' Device?

The contract of employment, chosen as the fundamental regulatory concept in English law, is thus characterised by a tension between 'the two functions of economic coordination on the one hand and risk redistribution on the other'.[109] In searching for a better answer to the need for a central 'public-regulatory' device or concept, this trade-off must remain central: as discussed earlier, any potential reform must be closely tied to the original motivation of the unitary conception.

It is suggested that upon further reflection, both of the required aspects (micro-economic coordination powers, and macro-economic risk distribution) could be viewed through the perspective of the employer; indeed, they may best be understood as centred on it: in the traditional analysis, the employer is the party that exercises the coordination function and reaps the benefits thereof; it is also the party which bears the majority of the burden resulting from the risk redistribution function. A coherent conceptualisation of the notion of the employer could therefore be the starting point for a resolution of the often circular reasoning that characterises existing problems with the larger notion of the employment relationship, the contract of service and the notion of the employee. The potential of this different perspective is echoed by Davies and Freedland in their already quoted suggestion that the debate as to the appropriate scope of employment law coverage might 'best be understood from an unfamiliar perspective, indeed initially a counterintuitive one, [where the] problem lies not in the binary analysis of the worker, but in the unitary analysis of the employer. [110]

[109] ibid 16.

[110] Davies and Freedland (n 24) 273.

The Crucial Elements of the Notion of the Employer

Writing in the much broader context of reconceptualising personal work relations generally, Freedland and Kountouris formulate two criteria which an adequate re-conceptualisation needs to take account of. They suggest two different levels, each with its own particular kind of conceptualisation:

> One of those two levels – […] the macroscopic or 'macro' one – is a taxonomical level in which all personal work relations are mapped out and classified into categories.
>
> The other of those two levels – […] the microscopic or 'micro' one – is a structural level in which the structural features of particular personal work relations are identified or assigned.[111]

The direct applicability of this model is limited to a fairly general level, given the different purpose and context of the authors' much larger endeavour of looking at and reconceptualising personal work relations from a comparative perspective. The crucial idea that can be adopted for the present context, however, is that scrutiny of the notion of the employer needs to happen at 'two focus-levels – a broad and distant focus-level on the macro map of personal work relations in general and a narrow and close-up focus-level on the micro-map of particular personal work relations'. Recognising the potential for analytical duality is useful first guidance for present purposes, as is the reminder to consider the close interdependence of both levels.[112]

Seen from the perspective developed in the preceding paragraphs and the broader context of the historical evolution of employment regulation, the notion of the employer thus needs to achieve two aims in order to restore coherence to the larger regulatory regime.

[111] Freedland and Kountouris (n 106) 313.

[112] ibid 313-314.

> *It must be a unitary notion, in the limited formal sense of being able to identify 'the employer' according to the same clear singular set of criteria in all circumstances.*
>
> *It must furthermore, in a substantive sense, ensure that the entity or combination of entities thus identified will be the one best placed to ensure the risk/control trade-off at the heart of labour market regulation.*

This, therefore, is the test to be developed and applied in the final two sub-sections: on the macro-level, does the particular conception under scrutiny offer a singular set of identification principles? And on the micro-level, do they ensure that the party who can best effect the relevant trade-off is selected in all circumstances? It will be seen that when this two-pronged, or dual focus, test is applied to the traditional interpretation of the unitary notion, its shortcomings quickly become apparent. Using a functional perspective, on the other hand, means that the unitary strand of the employer notion can be reconceptualised to successfully meet both criteria.

Before embarking on this analysis, two linguistic points should be reemphasised. The sense in which the notion is expected to be *unitary* in the first limb may appear as a rather unfamiliar idea of a unitary category, different in particular from the 'unitary' bilateral contractual paradigm being reconceptualised in this chapter. As the preceding pages have shown, this is due to the need for unity being a *conceptual*, rather than substantive one; in line with the larger structure of labour market regulation in the United Kingdom. The second observation relates to the very different senses in which the test's two limbs could be said to reflect the move towards a functional notion of the employer. It will be recalled from discussion in chapter five that there are at least two ways in which that term can be deployed: the first limb is functional in the sense of *defining* the employer via the exercise of one or a combination of the five particular functions identified. The second limb, on the other hand, is functional in the sense of providing for an ex-post-facto analysis of the socio-economic consequences of adopting the new notion: is the entity, or combination of entities, selected on the basis

of the underlying concept the one best placed to perform the risk/control trade-off in the layer of employment under scrutiny?

SUB-SECTION 2: THE TRADITIONAL 'UNITARY' NOTION

The traditional conceptualisation of the unitary strand of the notion of the employer is a very narrow one, defining it exclusively as a singular counterparty to the contract of employment, substantively identical across all regulatory domains of employment law. In a formal sense, it could therefore be analysed as meeting the first criterion set out, above: it is able to identify the employer according to a single clear set of principles in all circumstances. As the discussion in part two of this thesis has shown, however, the received notion is at the same time vastly under-inclusive, failing to identify an employer in most multi-entity employment scenarios. As its operation is limited to a narrow set of paradigm cases, therefore, that analysis is at least open to serious doubt. In the second, *substantive* sense, it is clear that the current notion cannot ensure that the party thus identified will be the one best placed to perform the necessary balancing exercise between controlling employer's direction rights and imposing protective obligations on them. Factual complexity quickly destroys conceptual unity, with immediate consequences as illustrated in chapter three: employment law coverage becomes incongruent, and may even break down completely where no responsible employer can be identified.

One possible response to this analysis would be to point to the specific exceptions that have sprung up to extend regulatory coverage in particular circumstances, fixing regulatory obligations on entities other than those identified by the traditional unitary approach. Such piecemeal responses to the identified shortcomings of the existing notion cannot, however, remedy the underlying problem. Indeed, they may exacerbate it by perpetuating the existence of a flawed notion, masked with exceptions which

'lack […] precision that is conceptual, as well as operational.'[113] Fudge notes this point in criticising 'rehabilitative' efforts to address the incongruent scope of employment protection: partial responses not only accept, but indirectly affirm, the *status quo*.[114]

The notion of the associated employer provides a good illustration of this point. It can be found in a series of materially identical statutory provisions in different contexts,[115] decreeing that

> any two employers shall be treated as associated if—
>
> (a) one is a company of which the other (directly or indirectly) has control, or
>
> (b) both are companies of which a third person (directly or indirectly) has control;
>
> and 'associated employer' shall be construed accordingly.

Employees may rely upon these provisions in an eclectic mix of circumstances.[116] The most frequent application in practice is in the context of employment rights that are subject to statutory minimum periods. Time spent working for associated employers will be added up towards the qualification threshold, despite the separate legal identity of the associated employers.[117] Another example where the associated employer provisions will be helpful can be found in the discrimination context. In pursuing an Equal Pay claim, the claimant can choose to rely on an employee of an associated

[113] J Fudge, 'Fragmenting Work and Fragmenting Organizations: the Contract of Employment and the Scope of Labour Regulation' (2006) 44 Osgoode Hall Law Journal 609, 632.

[114] ibid 631.

[115] Employment Rights Act (ERA) 1996, s 231; Trade Union and Labour Relations (Consolidation) Act 1992, s 297; Equality Act 2010, s 79(9).

[116] For a full account of the concept and its operation, see S Deakin and G Morris, *Labour Law* (6th edn Hart 2012) 231.

[117] ERA 1996, s 218(6).

employer as the relevant comparator, as long as all other conditions have been met.[118] At a quick glance, the route thus looks promising, especially now that it has potentially overcome some of the older criticisms of excessive formality in determining whether 'control' has been exercised.[119] However, as Deakin and Morris conclude, whilst 'the notion of associated employers provides a useful means of closing off some of the more obvious routes by which the application of statutory rights could be avoided by the adoption of separate corporate personality [… b]y no means all the possible escape routes are covered.'[120]

From the perspective of the double criterion developed earlier, therefore, the use of such exceptions falls already at the first hurdle: no consistent explanation for the presence of different exceptions is offered. The associated employer notion could be characterised as positively capricious, with extensions added and even withdrawn without coherent justification.[121] Indeed, it may make matters worse in specific circumstances, as the House of Lords' decision in *Dimbleby* illustrates.[122] In granting an anti-strike injunction in a multi-entity industrial dispute, Their Lordships found that whilst a purposive interpretation of the relevant statutory provisions (whether the

[118] Equality Act 2010, s 79(3), (4).

[119] H Collins, 'Ascription of Legal Responsibility to Groups in Complex Patterns of Economic Integration' (1990) 53 MLR 731, 740. Deakin and Morris partially disagree with this assessment, relying, *inter al*, on *Pinkney v Sandpiper Drilling Co* [1989] IRLR 425 (EAT) as evidence; at the same time acknowledging that it is an 'unusal case' and that the outcome could be changed by deploying more complex corporate structures: (n 116) 232.

[120] Deakin and Morris (n 116) 232.

[121] eg Employment Act 1989, s 14: union representatives' right to remunerated time off restricted to work done for the employer only (cf Employment Protection (Consolidation) Act 1978, s 27, which included associated employers' industrial relations).

[122] *Dimbleby & Sons Ltd v National Union of Journalists* [1984] ICR 386 (HL). See also *Hardie v CD Northern* [2000] ICR 207 (EAT): 'employer' in 1995 Disability Discrimination Act cannot be purposively extended to include associated employers.

relevant employer was a party to an industrial dispute[123]) would have generally been within their remit, the fact that Parliament had explicitly provided for an extension of the immediately following subsections to associated employers meant that a strict literal approach was to be followed on the issue before the court.[124]

As Whittaker has noted, a powerful consequence of the 'reliance on the idea of an exception to an existing principle is that it recognizes the force of the principle itself.'[125] It is therefore unsurprising that Davies and Freedland have suggested that while there have been some responses to the multipolar dynamics of complex employment relationships, these efforts 'still [fall] very short of the kind of rethinking of the concept of "the employer" which [is] functionally required.'[126] In the absence of a significant reconceptualisation of its unitary limb, neither the original notion of the employer nor its combination with specific statutory or common law extensions can fulfil the required unifying role. When measured against the criteria developed in sub-section one, both fall at the first hurdle: the former as it is conceptually too narrow to identify an employer in situations beyond a small set of paradigm cases; the latter as it does not even aspire to any conceptual unity at all.

SUB-SECTION 3: THE UNITARY NOTION RECONCEPTUALISED

The central argument of this chapter has focused on the suggestion that the unitary strand of the employer notion can be reconceptualised to successfully resolve the underlying tension with an openly functional approach. Its new formulation therefore

123 Employment Act 1980, s 17(3).

124 Though this may now be attenuating: *British Airways Plc v Unite the Union (No 2)* [2010] EWCA Civ 669, [2010] ICR 1316 (CA).

125 Whittaker (n 32) 216.

126 Davies and Freedland (n 24) 289.

comes as a logic consequence of the stronger position of the notion's functional strand. As has been seen, the employer does no longer have to be a substantially identical entity or combination of entities. In consequence, the traditional *singular* way of understanding the unitary notion is no longer tenable. That does not mean that the search for a coherent underlying notion is simply abandoned, however. The necessary conceptual unity is provided by redefining the singular strand of the notion as identifying

> *the entity, or combination of entities, playing a decisive role in the exercise of relational employing functions, and regulated or controlled as such in each particular domain of employment law.*

In embracing the potentially multi-contextual and multi-entity scenarios arising from the modern organisation of employment relationships, this definition ensures conceptual unity irrespective of factual complexity. The notion of the employer is seen as an aggregate of employer functions as exercised in different domains; it admits of variation between regulatory contexts and different entity patterns.

As in the previous sub-section, this conceptualisation must be tested against the context of the organisation of employment regulation as it has historically evolved. It must be able to meet the requirements of dual criteria; both limbs must in fact be closely tied in with the developments seen in the introduction to the present section. The notion must, first, be unitary, in the *formal* or *macro* sense of being able to identify the employer according to the same clear singular set principles in all circumstances. This test is met by the criterion of the exercise, or decisive role in the exercise, of an employer function regulated in a particular legal domain. The potential variety of instantiations does not distract from the fact that every entity or combination of entities will always have been identified according to a singular criterion: in this limited sense the notion continues to be firmly unitary. Whilst this emphasis on conceptual unity instead of substantive unity may be an unfamiliar

departure from the current approach, its provision of a conceptually unified transcendent meets the criterion as established above; indeed it succeeds in this regard where the previous notion failed due to its too narrow remit.

On a *substantive* or micro-level, the notion must ensure that the party or parties thus identified will be the one(s) best placed to perform the relevant risk/control trade-off in each domain: this was the feature identified as the original reason for stipulating a unitary notion. The reconceptualised unitary strand can equally meet this requirement, as obligations will be imposed, by definition, on the entity that takes the actions employment law seeks to regulate. From a broader normative perspective, this argument that each entity should bear the obligations attached to the exercise of relevant employer functions can be supported both on the basis of the idea of fairness, or reciprocity more specifically, and economic efficiency: employers' incentives will be optimised once 'costs [are] borne by the activity which causes them.'[127]

This point reflects the broader functionalist perspective, in the sense differentiated at the beginning of chapter five: the role or economic function the particular institution of the employer plays in different contexts.[128] This analysis starts from the observation that the reconceptualised notion alleges that there can be a singular underlying conceptualisation despite the nearly limitless possible permutations of practical outcomes. It formalises the two observations to determine whether they can be coherently integrated, relying on the account of different domains, or layers, of employment law regulation as developed above.

[127] G Calabresi 'Some thoughts on Risk Distribution and the Law of Torts' (1961) 70 Yale Law Journal 499, 533 (writing in the context of 'tort costs'). The Coasian counter-argument that this would lead to difficult allocation questions in the tort context is not applicable in the present context of employer functions: the 'activity' and the 'cheapest cost avoider' (cca) overlap under the functional approach proposed: G Calabresi and J Hirschoff 'Towards a Test for Strict Liability in Torts' (1972) 81 Yale Law Journal 1054, 1060; both as discussed extensively in J Stapleton, *Product Liability* (Butterworths 1994) 99-105.

[128] This is not to be confused with the functional account applied hitherto, ie the definition of a particular notion *via* the exercise of particular operational functions.

The initial claim, then, is one of *functional commonality across different layers*. It is furthermore suggested that that functional role of the notion of the employer (in the current sense) is in a certain sense identical across all regulatory domains: it is the regulatory focal point for employers' control rights and risk absorption obligations. This is met by the observation of *substantive differences in each layer.* Different entities or combinations of entities can be found to be employers, depending on each context. The solution to this apparent impasse lies in the recognition that whilst employment regulation overall will always be about the risk/control trade-off identified by Deakin and Wilkinson, the specific functionality of each layer in question is different (eg to ensure equal pay, or ensure stable long-term provision of work), as is therefore the operational or substantive role of the employer (eg to serve as a comparator boundary, or to consult with employees to avoid mass redundancies).

Thinking back to the practical examples developed in chapter five, a single entity could be identified as the employer, as could be different entities for different contexts, or even multiple entities for a particular function. Seen on its own, this may lead to the allegation that the different substantive employer notions cannot be linked by a coherent underlying concept. The solution to this lies in an analysis of the broader picture. The first step is to note how each different layer represents a unique amalgamation of specific goals and the variety of regulatory techniques deployed to achieve them. The second step is then to recall the idea that a single test is being applied equally across all different areas: the reason that the practical manifestations are different is *not* the result of a lacking underlying conception, rather it is simply the recognition of the reality that the single test (the function of the employer) is applied in different contexts, and will therefore lead to different practical outcomes. From a functional *ex-post* analysis, this ensures that the entity or entities identified as the employer will be the one(s) best placed to fulfil the overall purpose of the employer

(the balance of the control and risk functions) as required in that particular layer, regardless of the formal structures shaping the employment relationship.

Conclusion

The second part of this chapter started with a brief summary of the historical development of the labour market and its regulation to understand the need for a single notion, as well as its precise nature. It then applied these findings as a two-limbed test to the competing unitary notions of the employer. In looking at the traditional approach, it was shown how that conceptualisation fails at the second stage, and how piecemeal attempts at improving results cannot improve the situation. The functional approach proposed, on the other hand, brings a different unitary notion with it, in the sense that the single criterion is defined as the exercise of a relevant regulated function. This conceptualisation lives up to the test; indeed, it also stands up to further scrutiny from a functional perspective to dispel the potential allegation that as the functional notion will lead to substantively different outcomes in different factual scenarios, it cannot be connected up by a clear rationale.

The functional reconceptualisation proposed is thus successful because it presents a unitary notion of the employer, in the *dual sense* as historically required: it offers a single organising device, capable of identifying the *locus* where the key trade-off that underpins the regulation of the modern labour market should take place.

CONCLUSION

This thesis set out to explore the legal notion of the employer, with a particular emphasis on its operation in complex multilateral structures. The present conclusion redraws the main lines of argument developed in the course of the previous chapters, and suggests that the final overarching test can be successfully applied to the suggested modifications: the reconceptualised notion of the employer directly addresses the fundamental conceptual tensions underpinning the current approach.

Summary of the Argument

The first part of the thesis set out to conceptualise the notion of the employer in English law. Moving beyond a series of frequently unspoken and unchallenged assumptions, it discovered two competing conceptual strands in the existing case law: the notion was shaped, first, by a range of external factors as a unitary one. The perception of the employer as the same, singular entity serving as the immediate counterparty to a contract of employment started from traditional assumptions surrounding the singular, male master; developing complex fact patterns continued to be analysed through that unitary prism. This was exacerbated by the subsequent rise of contract as the main conceptual device in the organisation of growing regulation of employment relationships, with limited liability companies soon taking over the mantle of the unitary employer.

At the same time, there is little evidence in the traditional tests to suggest an inherent need for the employer always to be a singular entity. Indeed, the common law frequently betrays a strongly multi-functional conception of the employer. Five different groups of such functions were identified, and traced through a wide range of

examples. The first chapter concluded by suggesting that whilst in the paradigm bilateral situation of a single entity exercising all employer functions these different strands are no immediate cause for concern, there is an inherent tension which can quickly come to the fore once more than one entity becomes involved in the direct management of employment relationships.

Chapter two then illustrated how developments in modern enterprise organisation, from agency work to corporate groups and activist investors such as Private Equity funds, are increasingly building on complex multilateral arrangements, thus rapidly moving the majority of employment relationships outside the narrow traditional paradigm. Whilst the different structures surveyed vary considerably in their technical setup and day-to-day operation, they are united in a nearly limitless variety in the shared or parcelled-out management of work. As soon as employer functions are exercised from more than one *locus* of management power divided over several legal entities, the tension inherent in the traditional conceptualisation becomes a challenge to the coherence of employment law coverage.

Depending on the mode of joint employer function exercise workers may find themselves beyond the scope of most protective legislation, or obligations may be placed on entities other than those best placed to fulfil them. In the employment agency scenario, for example, the courts have been increasingly motivated to deny the existence of a contract of employment with either party exercising some of the traditional employer functions, thus leaving the worker without recourse against either the agency or its end-user clients in the case of many fundamental employment norms. In complex corporate setups, on the other hand, it is becoming increasingly difficult to identify the relevant employer for purposes of statutory obligations, such as the consultation and information of employees. As relevant decision-making is rarely limited to the management of the subsidiary serving as the immediate contractual

counterparty to an employee's contract of service, protective obligations may be placed on inappropriate entities or become entirely fictional.

In setting out these examples, several previous attempts at addressing the problems under discussion were analysed to demonstrate their potential flaws: instead of addressing the underlying tension in the notion of the employer, judicial, legislative and policy-based responses have historically been limited in their focus to a particular subset of issues. The difficulty with this approach lies in its focus on the consequences, rather than the cause of the incongruent application of employment law: partial on-the-spot fixes, even if undertaken with clear worker-protective intentions, can cause problems in other areas of the regulatory framework. Attempts at partial reform are furthermore difficult insofar as they tend to perpetuate received notions and thus the very problem itself.

Chapter four turned to a comparative exploration of the scope of employment regulation in multilateral structures under German law, particularly as regards the situation in corporate groups (the *Konzern*). The evidence found confirmed the tentative guidelines for a possible reconceptualisation drawn up in earlier sections. Any successful attempt must not only address the deep underlying tension identified in part one, but also grapple with the assumption of excessive homogeneity which underpins the current regulatory approach: the notion of the employer does not necessarily need to be identical in different domains of labour law, or always be constituted by the same singular entity. Second, as regards reform of each of the two conceptual strands, the unitary one is particularly problematic insofar as it leads to rigidly formalistic outcomes. The reconceptualisation project, finally, needs to strive for a careful balance between overall coherence and flexibility, avoiding a radical departure from existing frameworks whilst at the same time remaining adaptable to future doctrinal development.

With these notions in mind, the third part shifted from the previous analytical-descriptive approach into an openly normative attempt to fundamentally reconceptualise the notion of the employer. Keeping in mind the previous chapter's conclusions, its steps were carefully structured around the functional and unitary strands of the notion of the employer as identified at the outset, with a chapter broadly dedicated to exploring the necessary changes to each limb. Overall, this resulted in very different modifications being proposed: the functional strand was to be strengthened, in particular by the development of a robust theoretical framework, and an extensive demonstration how existing structures could be deployed to that end. In the unitary strand, on the other hand, the proposed changes were more significant, designed to leave behind its current analytical straitjacket without however abandoning a commitment to an overarching notion of the employer.

Chapter five thus developed the existing multi-functional limb to show how a careful extension to a fully functional notion could be achieved. A first section developed a detailed theoretical account of the proposed functional typology, noting in particular its roots in the existing approach and testing its ability to draw clear outer boundaries of the application of employment law norms. Different avenues for the practical operation of such a functional notion were explored in the following section, drawing on a broad range of existing examples from both the common law and different models of statutory regulation, before concluding with a positive evaluation of the proposed modifications of the multi-functional strand against the previously developed criteria.

The final chapter then turned to addressing the unitary strand to show that while some clear breaks have to be made from the existing setup, a unifying overarching conceptual notion of the employer can be maintained. The initial section returned to the three main factors identified as driving the unitary strand in chapter one, re-examining each one to demonstrate a growing incongruence between developments in

the relevant areas and labour law's rigid attachment to perceived historical approaches. This was demonstrated in particular in the areas of privity of contract, and the implications of the 'corporate veil', resulting from the operation of the doctrines of corporate personality and limited liability. Discussion finally moved on to exploring the need for an overarching notion of the employer, developing the formal and substantive expectations against which the existing and proposed approaches could be measured. Analysed thus, the received notion fails to achieve its basic tasks in nearly all situations beyond a narrow factual paradigm, whereas the reconceptualised strands ensure that there is a clear overarching conceptual notion of the employer which can unify even complex multilateral manifestations of shared employer functions.

The Fundamental Tension Resolved

Overall, then, this thesis hopes to have demonstrated that the only way the reconceptualisation of a notion as fundamental as that of the employer can be successful is by directly addressing the inherent tension identified at the outset. It is not possible to simply ignore either the unitary or the multi-functional strand by radically departing from the existing case law. Partial statutory or judicial interventions are similarly bound to unravel, as they look to the symptoms rather than the cause of existing problems, and further perpetuate the received approach. Indeed, it is in this regard that most previous attempts at grappling with the question at hand have struggled.

The proposed reconceptualisation, on the other hand, responds directly to the specific problems identified in earlier parts, both as regards the theoretical setup and its practical implications. It addresses both strands to build on their respective strengths and to address specific weaknesses in a careful modification that takes account of the interdependence of the notion's functional and unitary aspects.

Fudge, drawing on Woodiwiss,[1] has suggested that one factor that has historically kept courts from embracing an openly functional notion of the employer was the fear that this would lead to a lack of consistency and coherence across different domains.[2] As this thesis hopes to have demonstrated, the opposite is in fact the case: it is the current approach that leads to inconsistency and incoherence in employment law coverage. A functional notion of the employer may overcome these problems by addressing the tension at the very core of the received approach: the proposed reconceptualisation seeks to restore conceptual coherence by re-establishing an underlying unitary notion, in the hope of allowing for the scope of employee-protective norms to become resilient to domain-, entity-, and function-specific variations.

[1] A Woodiwiss, Social Theory after Post-Modernism: Rethinking Production, Law and Class (London, Pluto Press, 1990).

[2] J Fudge, 'The Legal Boundaries of the Employer, Precarious Workers, and Labour Protection' in G Davidov and B Langile (eds), *Boundaries and Frontiers of Labour Law* (Hart Publishing, Oxford 2006) 310-11.

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