Britain’s redundancy payments for displaced workers

The Redundancy Payments Act of 1965 established the idea that an employee has property rights to his or her job based on years of company service and instituted an entitlement program for displaced workers sponsored by firms and the government.

LAWRENCE S. ROOT

In 1965, British policymakers created the Redundancy Payments Act, calling for advance notification of workers who are to be laid off (made “redundant”) and mandating lump-sum payments to those affected. In the years that followed, revisions strengthened requirements for joint labor-management planning to avoid redundancies, but the basic structure of redundancy payments remained unchanged. The Act was an effort to spur industrial modernization, but with recent high levels of unemployment, it has taken on a welfare role, providing payments to displaced workers who may face prolonged periods of unemployment. Great Britain has attempted to mitigate the effects of economic displacement by mandating private-sector payments with partial government reimbursement of the costs. The primary and secondary impacts of the Act provide a useful backdrop for the current discussion of policies to deal with displaced workers in the United States.

The legislation: context and content

The Redundancy Payments Act of 1965 was a response by the British government to basic concerns about the flexibility of the nation’s industrial base and, to some extent, its ability to modernize in the face of a traditional union emphasis on job security. Unemployment was low at the time and the primary concern was shifting to newer modes of production and expanding Britain’s economic base to compete in future markets. Policymakers in the Labour government, which had a Parliamentary majority at the time, sought ways:

"...to make it easier for workers to change their jobs in accordance with the needs of technological progress...to push forward the modernisation of British industry as fast as possible, and to enlist the cooperation of workers as well as management in the process..."

The Act established the idea that an employee gains the equivalent of property rights to his or her job by virtue of years of service with the company. Those rights include the privileges and security associated with seniority, as well as rights to the job itself. In his introduction of the bill for its critical second reading in Parliament, the Minister for Labour equated the rights of an employee to a job with those of an owner:

"...if a man is deprived of those rights by economic circumstances outside his control, he ought to be compensated. Industry has long recognized the justice of this for higher management and I believe the House would agree that it is high time to extend it to all workers..."

What emerged from Parliament was an Act which provided for advanced notification of impending cutbacks and lump-sum payments to workers who were made “redundant.” Advance notification of redundancies had been introduced by the previous Conservative government, and there was legislative precedent for mandating payments to redundant workers.

Prior to the Act, severance payments were not widespread. One estimate suggests that fewer than 1 in 6 workers had any form of redundancy or severance pay, and most of those workers were in public-sector employment. A survey in the late 1950’s of “best practices,” representing perhaps 10 percent of all companies, suggested that the most gener-
ous of those companies offered no more than 12 weeks’ pay for their long-term workers. In one work force reduction 10 years before the passage of the Act, a large automaker dismissed 4,900 workers with only 2 days’ notice and no compensation. Subsequent negotiations eventually resulted in 1 week’s pay for those with 3 to 10 years of service and 2 weeks’ pay for those with more.7

The appropriateness of a lump-sum payment rather than increased income maintenance payments was one subject of legislative debate. The authors of the Act held that a lump-sum payment was the appropriate response to a loss of property. It was argued that the redundant worker experiences a loss even if there is no period of unemployment. A one-time payment also had the advantage of avoiding disincentives for reemployment which might result from higher unemployment benefits. The single payment would “never have the effect of giving the prudent worker a financial incentive to spin out a spell of unemployment.”8

The amount of the lump-sum payment was expressed in terms of a number of weeks of pay for years of service at different ages. Years worked when the worker was 18 to 21 result in a half week’s pay per year. Each year worked when age 22 to 40 yields 1 week’s pay. The worker is credited with 1 1/2 weeks’ pay for each year worked from age 41 to the normal retirement age.9 A worker has to have at least 2 years of service beyond the age of 18 to be eligible for the statutory payment. A maximum of 20 years of work are counted and a maximum wage was fixed at £40 per week in 1965. This was increased over the years to £155 in 1986.10 (At the time of this writing, the exchange rate suggested that 1 British pound was equal to approximately $1.50.)

The schedule links payment levels to age, based on the assumption that older workers have more to lose in the event of displacement. This introduction of age into the formula was a departure from the approach of private-sector plans, and it created incentives for older workers to volunteer for redundancy.

The Act also established a Redundancy Fund, financed by a surcharge on the National Insurance tax. The fund had two purposes: first, it made the payments to “redundant employees whose employers were unable to fulfill that obligation”11 and second, the fund also reimbursed employers for about 60 percent of the costs of redundancy payments.

The reimbursements were intended to spread the costs across businesses rather than have them fall only “on those firms and industries which are least able to bear it.”12 Recently, the percentage of costs reimbursed by the Redundancy Fund was decreased and was phased out entirely in the fall of 1986 for establishments with 11 employees or more.

The reimbursement structure initially reduced the costs for companies experiencing redundancies, undercutting some political opposition. This reimbursement structure also had additional political benefits. The governmental share of redundancy expenses was decreased over the years by lowering the proportion of employer expenses reimbursed. In this way, public costs were decreased without reducing the benefit levels to individuals. While this latter feature may not have been intended, the history of decreased reimbursement suggests that it had that effect.

### The incidence of redundancies

There is no central reporting of the total number of redundancies. The existence of the redundancy payments, however, provides some useful indicators of the extent of redundancies in Great Britain.

Three types of data arise from the operation of the Redundancy Payments Act: advance notifications, confirmed redundancies, and redundancy payments.13 While none of these provides a direct estimate of the number of workers who are actually made redundant, each contributes to our understanding the incidence of redundancies.14 Table 1 provides statistics on these three indicators.

Employers are required to give 30 days’ advance notification to the Department of Employment before a redundancy involving 10 employees or more is to occur. (Ninety days is required when the redundancies are to involve more than 100 employees.) Statistics on advance notifications underrepresent the number of redundancies because they exclude actions affecting only a few people. They also may overrepresent the eventual redundancies because subsequent adjustments often negate or reduce the eventual need for the redundancies.

**Confirmed redundancies** are based on Department of Employment followup of the advance notifications. They also exclude establishments of fewer than 10 employees, but are more stable over time than the advance notifications. This stability makes confirmed redundancies a useful indicator of the incidence of redundancies over time.

Data on the number of redundancy payments provide the

### Table 1. Redundancies and unemployment in Great Britain, 1977–85

<table>
<thead>
<tr>
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<td>574</td>
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<td>255</td>
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<td>491</td>
<td>810</td>
<td>635</td>
<td>608</td>
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<tr>
<td>(percent)</td>
<td>7.2</td>
<td>7.8</td>
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<td>22.1</td>
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<td>19.1</td>
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<tr>
<td>Total number of</td>
<td>1,345</td>
<td>1,321</td>
<td>1,234</td>
<td>1,591</td>
<td>1,242</td>
<td>2,806</td>
<td>2,988</td>
<td>3,034</td>
<td>3,149</td>
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<td>unemployed3</td>
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<td></td>
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<tr>
<td>Percent</td>
<td>5.7</td>
<td>5.6</td>
<td>5.2</td>
<td>6.7</td>
<td>10.2</td>
<td>11.9</td>
<td>12.7</td>
<td>12.9</td>
<td>13.3</td>
</tr>
</tbody>
</table>

1 Rate per thousand employees.
2 From April 1983, the unemployment data reflect the effects of the Budget provisions for some men aged 40 and over who no longer had to sign on at an unemployment benefit office. Unemployment rates are based on registered unemployed as a percent of the wage and salary labor force (excludes the self-employed and the Armed Forces).
3 Includes people aged 40 and over who are actually made redundant, each contributes to our understanding the incidence of redundancies.14

third source for estimating the extent of redundancies. While these data include the smallest establishments, they do not include redundant employees with fewer than 2 years of service or those who have reached retirement age.

Although the number of redundancies is not directly measured, we can use redundancy payments to make an estimate. A study of British employment flow found that almost 40 percent of those who became unemployed said that they left their last job because of redundancy, but only 42.5 percent of that group said that they had received or expected to receive a redundancy payment. Another British study of companies applying to the Redundancy Fund for reimbursement found a higher ratio of those receiving payments to those not receiving payments, but the authors suggest that their sample overrepresents that ratio and a one-to-one relationship between eligibles and ineligibles is a more accurate assumption. Using this relationship, we can estimate the number of redundancies by doubling the number of payments.

In chart 1, this estimate is graphed over time, indicating a peaking in 1981 at about 1.6 million redundancies. Overall unemployment, included in table 1, is also displayed in chart 1. Although the relationship is not necessarily direct, we would expect increased redundancies to eventuate in higher unemployment. The data provide some support for this, with the sharp rise in the number of redundancies followed by an increase in unemployment in subsequent years.

The bulk of redundancies have occurred in manufacturing. Table 2 shows the rates of redundancy in manufacturing compared with those in the service sector from 1977 to 1985. Both rates show the same general trend over time in chart 1, but it is clear that layoffs in manufacturing dominate the picture. In addition, the ratio of manufacturing redundancies to service sector redundancies increases with rises in the overall numbers, indicating manufacturing’s disproportionate share of the sharp increase in redundancies in the early 1980’s. It should be noted, however, that systematic differences in the size of the establishments by industry may limit the usefulness of industry comparisons of confirmed redundancies. Redundancies in the service sector may be underrepresented because of the greater prevalence of small establishments than in manufacturing.

**Redundancies in Britain and the U.S.**

Although the British data are not strictly comparable with recent data on displaced workers in the United States, the incidence of redundancies can be compared.

Most redundant British workers who do not receive payments are ineligible because they have been employed for fewer than 2 years or, less often, they have reached retirement age (60 for women and 65 for men). Data from the United States suggest that from 1979 to 1983, approximately 11.5 million workers lost their jobs because of

![Chart 1. Payments, redundancies, and unemployment in Great Britain, 1977-85](chart.png)
Based on combinations of age and length of service. The actual structure of the extra payment programs can have a pronounced effect on the distribution of payments across age groups. Two programs in the auto industry offer an example. Company A provides 18 weeks’ pay in addition to the statutory payment. Company B uses a formula which reflects the statutory approach of giving more weight to years of service by older workers. For a worker made redundant at age 38 after 20 years of service, Companies A and B provide a total of 36 and 35 weeks’ pay, respectively. For a worker who is displaced at age 58 after 30 years of service, Company A provides 46.5 weeks’ pay while the payment from Company B would be for 68 weeks.

The impact of the two different approaches in this example varies with the age structure of the work force. For younger workers (and those with shorter tenure with the company) the plan in Company A is more generous (and more costly for the company). If, however, the work force is older, the extra payments in Company B are much more attractive. In a cutback, rather than a total closing of a facility, these higher payments for older workers, often combined with relaxed pension eligibility, create strong incentives for older workers to volunteer for redundancy. This has tended to reverse the traditional LIFO (last in, first out) order of redundancies as older workers with greater seniority volunteer for redundancy.

As noted, “super payments” are found in nationalized industries, particularly those tied to the European Coal and Steel Community. These payments tend to be well above the levels of other corporate payment plans. In addition, salary continuation plans can provide up to 2 years’ continuing salary (or salary supplements if the worker is reemployed at a lower paying job). In a 1980 personnel reduction in a Welsh steel company, for example, it was reported that male workers 55 and older received an average payment of £10,000; the lowest 20 percent received less than £5,000; and the highest 20 percent received more than £15,000. In addition, those workers received income supplements up to 90 percent of their former wage for the 2 years following their job loss. During this period, £18,000 was the maximum redundancy payment which a British steelworker could receive.

These redundancy payment levels reflect the effect of standards established by the European Coal and Steel Community and, to some extent, funds from the Community. As part of attempts to nationalize coal and steel production in Europe, Community funds have been used to ease the costs involved in closing less productive facilities. The contributions have been applied to early retirement packages, training, and redeployment as well as to redundancy pay. In 1979, it was reported that the coal industry received £4.67 million (an average of £1,240 per redundant worker). In the steel industry, £1.5 million was provided, £600 per worker.

Other nationalized industries which do not receive outside

<table>
<thead>
<tr>
<th>Year</th>
<th>Rate per 1,000 employees</th>
<th>Ratio of manufacturing to service</th>
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<tbody>
<tr>
<td></td>
<td>Manufacturing¹</td>
<td>Service</td>
</tr>
<tr>
<td>1977</td>
<td>13.8</td>
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<td>16.7</td>
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<td>1979</td>
<td>19.5</td>
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</tr>
<tr>
<td>1980</td>
<td>59.6</td>
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</tr>
<tr>
<td>1981</td>
<td>65.9</td>
<td>5.9</td>
</tr>
<tr>
<td>1982</td>
<td>46.7</td>
<td>5.9</td>
</tr>
<tr>
<td>1983</td>
<td>50.2</td>
<td>5.0</td>
</tr>
<tr>
<td>1984</td>
<td>28.4</td>
<td>4.2</td>
</tr>
<tr>
<td>1985</td>
<td>25.3</td>
<td>3.6</td>
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</table>

¹ Excluding construction, energy, and water supply.

Source: “Recent Trends in Redundancies,” Employment Gazette, December 1986, Table 2.

The calculation of extra payments range from ignoring the limits used for statutory payments (for example, maximum wage level counted or number of years of service credited) to the addition of a fixed amount to supplements

closings or job cuts; 6.9 million (60 percent) had 2 years or more on that job. Displaced workers with 3 years or more on the job were analyzed in the U.S. data. Extrapolating from these data, however, we can estimate how many workers with 2 years or more who were below the British retirement age were displaced in each of the years from 1979 through 1983. These data and the comparable British data, based on redundancy payments, are displayed in table 3.

In both countries, the rates of displacement increased sharply in the early 1980’s. The British rates are considerably higher than those in the United States, particularly in 1981, when the British redundancies peaked. For the period covered, however, the British rates display some downward movement, while the U.S. rates continue upward.

Three payment levels

Statistics are available for the payments which are required by statute, but larger corporations typically provide payments which increase the total amount which a redundant worker receives. Payments can be roughly divided into three levels: (1) statutory payments; (2) “extra payments,” which are corporate plans which add to those statutory minimums; and (3) “super payments,” which are larger payments arising in nationalized industries, particularly those associated with the European Coal and Steel Community. It is estimated that somewhat more than one-half of those who are receiving redundancy payments have no corporate supplement. The average statutory payment in the 12-month period ending in March 1986 was £1,758. Most larger companies provide extra payments to supplement their statutory obligation. The amount of the payments varies with the wage level, seniority, and age of the work force affected, and this is usually not made public by companies. It is estimated that the extra payments tend to result in two to three times the level of payments mandated by law.

The calculation of extra payments range from ignoring the limits used for statutory payments (for example, maximum wage level counted or number of years of service credited) to the addition of a fixed amount to supplements...
support often have relatively large redundancy payments, but these public sector payments tend to be within the range of the most generous private sector plans. For example, the average payment for workers who were made redundant by British Shipbuilders in 1983 was about £7,500.26

Comparing two systems

The British layoff situation differs from that of the United States. Britain's redundancy rates have been two to three times greater than those in the United States. In addition, unemployment is more prevalent and regional unemployment is particularly severe. This is compounded by two factors which limit geographic labor mobility: the relative absence of a private sector rental market and very large differentials in housing costs among regions. On the other hand, differences in the social insurance systems result in less dependence upon the workplace for health insurance, eliminating one of the critical problems which displaced workers face in the United States.27

Another significant difference between the two countries is the Federal structure in the United States, which places individual States in competition for attracting business. Although some States and even cities have enacted plant-closing legislation, concern about discouraging business investment with possible increased regulation and costs has limited State-by-State initiatives.28

Given these differences, the Redundancy Payments Act provides one model for an interplay between the private policies of corporations and policies in the public sector. Addressing social welfare needs through corporate policy has been more characteristic of the United States than Britain.29 The Act officially recognized an employee's "rights" to a job and quantified those rights in terms of weeks of pay for years of service. It established a universal entitlement program administered by corporations but with the economic burden initially alleviated by partial reimbursement from a fund established with a surcharge to the existing social insurance tax.

Payments and personnel decisions

Early critics of the Act feared that the costs would discourage employers from imposing necessary redundancies. But, in practice, it appears that the payments have facilitated dismissals.30 The Act created an orderly process so that a manager could reduce a work force "with an easier conscience and reduced costs and arguments."31

The statutory program not only created a universal payment which was considerably beyond the general standards of the time, but it also appears to have stimulated the growth of private-sector schemes which built upon this base. Extra payments, a rarity before 1965, are now a normal part of the redundancy plans of medium-sized and larger firms.32

The Redundancy Payments Act has also had secondary effects on work force reductions. First, it changed the role of unions. Prior to the Act, unions typically resisted the imposition of redundancies. With the growth of redundancy payments, however, many workers have found the payment attractive enough to justify volunteering for redundancy. There has often been little rank-and-file support for opposing redundancies. The union role has shifted from fighting redundancies to bargaining for larger payments.

Second, the Act changed the age profile of those affected by redundancies. Seniority traditionally dominated the order of redundancy selection. Age-based redundancy payments, combined with an increase in the use of liberalized pension eligibility, changed this by bolstering incentives for the older worker to volunteer for redundancy. This is especially true when the lump-sum payment represents more money than the worker has ever amassed at any one time.

In the years since the passage of the Redundancy Payments Act, there has been increased targeting of redundancies to older workers. Prior to the Act, only 19 percent of employers in a national survey indicated that age was a criterion in selection for redundancy. After the Act, that percentage doubled. By 1974, a study by the British Institute of Management concluded that age was "the most important single mechanism for redundancy selection."33

In addition to creating incentives for older workers to elect voluntary redundancy, there also appears to be informal, social pressure on older workers to "make way" for the young.34 Nevertheless, for the older worker who is still 10 or 15 years from retirement age, volunteering may mean extended unemployment with little chance of finding other work.

Statutory redundancy payments arose as an attempt to encourage labor mobility. They were a consolation prize designed to reduce employee resistance to industrial innovations. In a growing economy with low levels of unemployment, the payments were appropriate for such a role. As unemployment increased, however, redundant workers found that the loss of a job was not followed by reemployment and payments were quickly exhausted. With 13-

### Table 3.

<table>
<thead>
<tr>
<th>Year</th>
<th>Great Britain</th>
<th>United States</th>
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<tbody>
<tr>
<td></td>
<td>Number</td>
<td>Rate per 1,000 employees</td>
</tr>
<tr>
<td>1979</td>
<td>255</td>
<td>11.3</td>
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<tr>
<td>1980</td>
<td>491</td>
<td>22.2</td>
</tr>
<tr>
<td>1981</td>
<td>810</td>
<td>38.2</td>
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<td>1982</td>
<td>635</td>
<td>30.2</td>
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<tr>
<td>1983</td>
<td>608</td>
<td>29.7</td>
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</table>

1 Includes only those workers with at least 2 years of service and below retirement age for British workers (60 for women; 65 for men).

percent unemployment and some regional rates at triple that level, the statutory redundancy payment provides little economic security.

Redundancy payments were created as labor policy. But as long-term unemployment has become more common among the workers affected, they have become more closely associated with welfare policy. They have become, in effect, an element of the British income maintenance structure. This is not a role for which they were created and the statutory redundancy payments do little to address the economic needs of those facing long-term unemployment.

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1 House of Commons, Parliamentary Debates (Hansard), Apr. 26, 1965, fifth series, volume 711, column 33. The Hansard is the official record of proceedings in Parliament, recording debates and the text of Parliamentary actions. The Redundancy Payments Act was later incorporated into the Employment Protection (Consolidation) Act.

2 Hansard, Apr. 26, 1965, column 35.

3 The use of “redundancy pay” rather than “severance pay” was based on what the lawmakers felt was its greater precision. Before the passage of the Act, “redundancy” was not such a common term.

4 For example, the Cotton Industry Act of 1959 made government support of industries contingent upon compensating employees for their loss of employment. See Santosh Mukherjee, Through No Fault of Their Own (London, Macdonald, 1973), p. 43.


6 Mukherjee, Through No Fault of Their Own, p. 53.


8 Hansard, Apr. 16, 1965, column 37.

9 The Act does not require payments to workers who have reached retirement age, 65 for men and 60 for women, irrespective of whether they had planned to continue working beyond that age. This differential treatment of men and women has not yet been tested in court, although there have been successful challenges in the European court to the policy of different mandatory retirement ages based on sex.

10 In 1985, average weekly earnings were £164 for full-time working men and £101 for full-time working women. See Employment Gazette, July 1986, table 5.6, p. S50.


13 Consistent statistics on redundancies have only been available since 1977. See a discussion in “Statistics of Redundancies and Recent Trends,” Employment Gazette, June 1983, p. 245.

14 For a discussion of these data, see “Recent Trends in Redundancies,” Employment Gazette, May 1985, pp. 202–06.


18 This is based on the author's analysis of data provided by the Bureau of Labor Statistics in microcomputer format.