ADDLESHAW GODDARD

GENDER PAY GAP REPORTING

LESSONS TO LEARN FROM YEAR 1

In the first article of a two-part series, Amanda Steadman, Principal Knowledge Lawyer in the Employment, Incentives and Immigration Group, reflects on the lessons to be learned from the first year of gender pay gap reporting. In the next article, Amanda will provide tips on how to produce an effective report and consider the measures that can help close the gender pay gap.

1. Understanding the Year 1 reporting exercise:

The Equality Act 2010 (Gender Pay Information) Regulations 2017 (the **Regulations**) came into force on 6 April 2017 and compel certain private sector employers to report gender pay information on an annual basis. The first reports had to be published by not later than 4 April 2018 (**Year 1**).

With the publication date for the second round of gender pay gap reports fast approaching, it's a good time for employers to reflect on the key learning points to be drawn from the Year 1 exercise. Whilst some of these learning points come from our own experience at Addleshaw Goddard of advising clients on navigating the reporting process, there are now a number of useful materials produced by relevant stakeholders which provide insight into Year 1 reporting. These are:

- The BEIS Select Committee report on Gender Pay Gap Reporting[1] (**BEIS Report**) published on 2 August 2018. The BEIS Report was published further to an inquiry by the Select Committee in which they received 22 submissions of written evidence from interested parties and held two oral evidence sessions. The BEIS Report helpfully takes stock of the Year 1 gender pay gap reports looking at both the figures and the measures that employers proposed to help close their gaps. It also makes a number of recommendations to Government on how the regime could be improved and expanded.

- The Government published its response to the BEIS Report[2] (**the Government's Response**) on 17 January 2019. This sets out their position on the recommendations made in the BEIS Report.

- The Government Equalities Office (**GEO**) published the results of a survey conducted in 2018 entitled the Employers' Understanding of the Gender Pay Gap and Actions to Tackle It (**the Survey**). The Survey was published in January 2019 and looks at employers' understanding of the Regulations, their experience of reporting and the actions they are taking to close their gap. The research consisted of telephone interviews of around 900 in-scope private sector employers conducted between July and October 2018 and a further 30 follow-up qualitative interviews.

- The GEO has also published guidance[3] considering evidenced-based actions that employers can take to help close their pay gap. The intention is that employers can use this to help create more effective action plans. This guidance will be discussed in the second article in this series.

[1] Gender pay gap reporting – Thirteenth Report of the Session 2017-19, 2 August 2018.

[2] Gender pay gap reporting: Government Response to the Committee's Thirteenth Report, 17 January 2019.

[3] Reporting the gender pay gap and improving gender equality in organisations: evidence-based actions for employers.

- The Equalities and Human Rights Commission (**EHRC**) - the body responsible for enforcing the Regulations - published a report entitled Closing the Gender Pay Gap[4] (**EHRC Guidance**) which sets out the findings of research they have conducted in this area and it looks at steps employers can take to help close their gap.

2. What are the lessons from Year 1?

Employers took their reporting obligations seriously…

The Government had initially estimated that around 8000 organisations were in scope to report. By the 4 April 2018 deadline, 9,718 employers had submitted their figures. However, most of these reports were submitted quite late in the day: at the beginning of March 2018 only 1,691 companies had reported. Around 8,000 reported in the last 4 weeks.

Given that this was the first year of reporting, it was perhaps to be expected that most employers would wait to publish alongside their peers. This may change over the years to come, perhaps seeing employers align the publication of their figures to the publication of their annual report. Indeed, the BEIS Report called upon the Government to formally change the publication deadline to align with other reporting requirements rather than the tax year. However, the Government declined to do this on the basis that there is not another common reporting requirement which aligns with publication of the gender pay gap figures. In their view, it is preferable to have a ring-fenced date for gender pay information reporting, with the proviso that employers have flexibility to report early if they wish.

Despite the lateness of the reporting, the compliance rates as at 4 April 2018 looked promising. Yet the EHRC estimated that a further 1,456 in-scope employers had failed to meet the deadline. Following contact from the EHRC threatening enforcement action, a further 810 employers reported their figures, bringing the total number of Year 1 reports to 10,528. The EHRC confirmed there was a 100% compliance rate by 1 August 2018. The BEIS Report called upon the Government to turn this list of 10,528 in-scope employers into a definitive register of organisations that are required to report every year. However, the Government declined to do so on the basis that a rigid list could lead to unlisted but in-scope organisations concluding that they do not have to report.

…but found the reporting process difficult

The good news is that the majority of employers felt comfortable with the *theory* of gender pay gap reporting. Indeed, the Survey revealed that around 82% felt that they had a good understanding of what the gender pay gap was and how it was calculated. A further 88% said they understood the distinction between the gender pay gap and unequal pay. Only 2% said they had limited or no understanding of the gender pay gap.

Although the theory seems to have landed well, the *practice* of reporting has proven to be more challenging. The BEIS Report noted that businesses found the reporting process *"very difficult"* and many required external advice to navigate the process. This view was echoed in the Survey – only 35% said they found the process very or fairly straightforward and they received evidence that employers felt the reporting exercise to be a *"considerable burden"*.

That some employers struggled with the process was brought into relief by the fact that some employers published *"highly improbable, inaccurate or questionable"* data. The BEIS Report referred to media reports from late March 2018 which had identified some employers reporting mathematically impossible figures (e.g. one company reported a gender pay figure of 106.4% whilst another reported a gender bonus gap of -1123.60%). Others reported 0% gender pay gaps and others still had to resubmit their

[4] Closing the gender pay gap, 10 October 2018.

figures after media scrutiny. One retailer, for example, changed their figures three times at the end of 2017 after the Financial Times challenged the plausibility of their reported figures.

What did employers find challenging?

There are a number of reasons why employers struggled with the process. The Survey highlighted some common internal business reasons such as:

- The complexity of the workforce and associated pay structures (e.g. multiple divisions, bonuses schemes and the use of contract staff).
- Unsophisticated payroll systems.
- The availability of knowledgeable / experienced staff to undertake the process.

In addition, ambiguities in the Regulations (and the associated guidance) themselves caused difficulties. The Regulations and guidance are not exhaustive, leaving employers to reach their own conclusions on issues such as whether a particular form of payment or allowance should be counted or excluded. By way of example, some of the typical areas of uncertainty that we came across when advising clients are outlined in the box below.

- **Uncertainty about who counts as an "employee" and "relevant employee"**: the Equality Act 2010 definition of employee applies so as to determine whether an employer is in scope to report. This potentially captures LLP members, some self-employed contractors and overseas employees. Confusingly, slightly different rules apply to determine whose data has to be included in the reporting exercise. Navigating this was always going to be a time-consuming exercise for larger employers with complex structures. Clients spoke to us about the challenges of dealing with employees working overseas. Employers were expected to apply the sufficient connection test laid down in Serco Ltd v Lawson[5] and Ravat v Halliburton[6]. This requires the application of a multi-factorial test to reach a conclusion on the sufficiency of the connection of the employee to Great Britain. However, guidance on how to efficiently apply this test was scant. For example, the joint guidance from Acas and the GEO[7] (**Guidance**) simply says: *"Each case should be considered on its own facts and the employer will need to make a decision. Where there is uncertainty, they should consider seeking professional advice to help clarify the situation".* This left employers with a choice between investing a significant amount of time and money towards achieving full compliance, taking a more broad brush approach or perhaps not taking them into account all.

- **Understanding that bonus payments need to be counted for both reports:** bonus payments have the potential to be included in both the pay and bonus gap calculations. Whilst most employers were clear that they counted for the bonus gap, some missed the point that if they were paid in the relevant pay period they would also count towards the gender pay gap. There was also the added complication that if the bonus was paid in the relevant pay period but related to a longer period of time (e.g. an annual performance bonus) then it would

[5] Serco Ltd v Lawson [2006] UKHL 3

[6] Ravat v Halliburton Manufacturing and Services Ltd [2012] UKSC 1

[7] Managing gender pay gap reporting, ACAS and GEO joint guidance

need to be pro-rated according to a specified formula in order to work out the amount attributable to the relevant pay period only.

- **Identifying whether a particular payment is an "allowance" or a "bonus" or neither**: allowances are counted for the gender pay gap but not the gender bonus gap, whereas bonuses are counted for the gender bonus gap and potentially also counted for the gender pay gap. Misclassifying one as the other would result in erroneous gender pay information. The regime requires a forensic analysis of all the different payments made to staff to understand what they are and why they are paid. In some cases this will be straightforward. But for a business operating a complex reward structure, perhaps with various historic or legacy payments available to different cohorts of employees, it is easy to see how this process can become very time consuming and uncertain. In many cases, the employer is simply left to make a judgement call about how to treat a payment. And, of course, the danger with this is that different employers may make different judgement calls about the same kinds of payments which undermines the value of comparing figures.

The BEIS Report concluded that the Regulations were confusing and that more detailed guidance was needed to help employers in the second year of reporting. They recommended that the Government work with the EHRC, business groups and other stakeholders to clarify outstanding areas of ambiguity and to publish revised Guidance.

How did the Government respond to this? Well, in a nutshell, they said "we've done enough". They highlight the fact that the Guidance was downloaded over 32,000 times and 71% of in-scope employers said they had read it. The Government also pointed to the fact that employers had a year to prepare and to the various methods of engagement they pursued such as attending seminars and webinars, writing to 40,000 employers to ensure they were aware of their obligations and providing an email query service.

Where does this leave employers? The Government says they believe there is a *"wealth of support"* which is *"sufficient to enable employers to report accurately".* However, they want employers to report with confidence and so have committed to gather stakeholder feedback and update the guidance if appropriate. Therefore, if you are struggling with how to treat a particular payment we would recommend that you seek advice from the GEO and/or Acas and ensure that you document how you have reached your final decision. This way, if your figures are ever challenged, you will be able to demonstrate that you have made a good faith attempt at compliance. We would also recommend that you feedback to the GEO on any areas where you feel more nuanced guidance is needed.

Gender pay gaps favoured men in almost every single region and sector

Overall, 77% of reporting employers had a median pay gap in favour of men, 14% had a median pay gap in favour of women and 9% had no median pay gap at all. The average median pay gap across all employers was 11.8%, although this was lower for very large employers (i.e. with 20,000+ employees) at 8.7%. Around 13% of all reporting employers had very high median gender pay gaps in excess of 30%.

There was a pay gap is in favour of men in *every region* of the country except Northern Ireland, with the worst gaps seen in London and the South East and the East Midlands. There was also a pay gap in favour of men in *every sector* of the economy, although the size of the gap varied significantly between different sectors. The construction and financial services sectors were the worst offenders. In their Year 2 reports, employers now have the option of benchmarking their figures against the Year 1 average for their sector, to demonstrate a better-than-average performance.

The breakdown of men and women by pay quartiles offered companies a more nuanced analysis of the nature of their own pay gaps. Overall, there was a higher proportion of men in the top quartiles and a higher proportion of women in the lower quartiles. The results supported the conclusion that it is harder for women to progress up the career ladder. Here, the BEIS Report concluded that a greater degree of granularity would be helpful. For example, a breakdown by deciles as opposed to quartiles would allow employers to track trends, monitor gaps more effectively and better indicate the presence of unequal pay. However, the Government has declined to introduce this change but say they are willing to consider potential changes after a period of consultation. There is no commitment yet to opening a consultation and so it seems the issue has been parked for now.   However, if you wished to produce a market-leading gender pay gap report, you could adopt the BEIS Report's recommendation and report on the distribution of men and women across pay deciles as well as quartiles.

The awarding of bonuses was fairly equal, but the bonus gap also favoured men

Overall the proportion of men and women receiving a bonus was fairly equal: 35.9% for men compared to 34.3% for women. However, the median bonus gap favoured men, reflecting the predominance of men in senior positions where bonuses tend to be higher. 53% of reporting employers had bonus gaps favouring men, 15% had bonus gaps favouring women and 33% reported no bonus gap.

The BEIS Report recommended that the Government revise the way bonuses are treated to secure fairer results. Presently, employers have to calculate by reference to the actual amount of bonus paid. Therefore, where an employer pro-rates a bonus award for a part-time employee, that figure must be used in the calculations. Given that more women than men work on a part-time basis this has the potential to skew results and inflate the gender bonus gap. Of course, employers have the opportunity to explain this in their narrative if they choose to produce one. However, the BEIS Report recommends that this anomaly be corrected so that the employer can compare like with like.

The Government has declined to take this recommendation forward. They note that the current approach was a *"conscious choice"* and allows employers to *"look at a person's working life in the round*". They advise unhappy employers to explain skewed results in their narrative and produce additional metrics if they wish to do so. Therefore, if you consider your bonus gap to be inflated because of a high proportion of part-time working women you may wish to produce a second bonus pay gap figure based on full-time equivalent bonuses which allow a like for like comparison.

Large pay gaps may undermine a claim to be an "employer of choice"

How have employees responded to the publication of gender pay information? 81% of employers reported little or no reaction from their employee population, 17% reported a limited reaction to them and only 2% reported a widespread reaction from staff. This was true even where the gender pay gap figures were high (i.e. 20% or higher) – even then only 7% reported a widespread reaction. This news may be of some comfort to employers who were nervous that the publication of the figures would trigger grievances and/or act as a gateway to equal pay claims.

Whilst employees don't seem particularly willing to rock the boat with their employer over the gender pay gap, there are some hidden reactions that businesses should note. In October 2018, the EHRC reported the results of a survey of over 2,500 employees working for in-scope employers. It revealed that:

- 58% of women said they would be less likely to recommend their present employer as a place to work if they had a large gender pay gap.

- 56% of women said that a large gender pay gap would reduce their motivation and commitment to their employer.

- 60% of women said they would feel less proud of working for an employer with a large gender pay gap.

- 61% of women said they would take an organisation's gender pay gap into consideration when applying for a role.

This tells us that larger pay gaps do not sit well alongside a claim to be an "employer of choice" and may deter top talent from staying in post and applying for roles. To offset this, employers with larger pay gaps may wish to amplify their communications with staff, emphasising the actions that are proposed to help close the gap.

Voluntary narratives and action plans haven't taken off as well as hoped

During the evolution of the legislation, there were calls from bodies such as the TUC for employers to be *obliged* to publish both a narrative explaining their figures and an action plan outlining how they intended to close their gap, perhaps also including targets. The logic was that making this a compulsory element of the regime would force an employer to tackle the issue. The concern was that merely reporting figures would not drive change and would – after an initial flurry of interest – fade from public view.

However, the Government elected not to mandate the publication of a narrative and/or action plan. Indeed, there is no obligation to take any measures to close the gap at all. The Government's view is that transparency will be enough to drive change – on the basis of "what gets measured gets managed". Nonetheless, the Government strongly encouraged employers to voluntarily publish a narrative and action plan. Relevant stakeholders such as the CIPD and The Fawcett Society also encouraged employers to do so.

So, how did employers respond to that challenge in the first year? It has been a bit of a mixed picture:

- **Narratives:** around 40% of employers provided a narrative report explaining their figures (estimates range from 30% in the BEIS Report to 50% in the Government Response and the EHRC Guidance). Further, the BEIS Report also notes that the quality of reports was *"very variable".*

- **Action plans:** only around 20% of employers went further and published an action plan on how they intended to close the gap.

- **Targets:** fewer still set targets for reducing the gap - estimates suggest somewhere between 5% and 11% did so.

In each case, larger employers (those with 500+ staff) were *more likely* to publish these things than a smaller in-scope employer.

The BEIS Report recommended that the Government force employers to publish both a narrative and a forward-looking action plan, with the focus on setting specific, time-bound steps which will be taken to close the gap.

So, how did the Government respond? They have declined to make this a mandatory requirement on the basis that it might result in a *"prescriptive format"* of limited value. They prefer to give employers the freedom to produce narratives and action plans that are relevant to their situation. Employers wishing to have a market-leading gender pay gap report should ensure that they include an explanatory narrative and set objectives and targets and report progress against them each year.

Summary of key learning points from Year 1

1. Consider whether the time is right to align the publication of your gender pay gap figures to the publication of your annual report.

2. If you are struggling with how to treat a particular payment seek advice from the GEO and/or Acas and document how you have reached your final decision.

3. Communicate feedback to the GEO and/or Acas on any areas where you feel more nuanced guidance is needed.

4. Consider whether it is helpful to benchmark your Year 2 pay and bonus gap figures against the Year 1 average for your sector.

5. If your bonus gap is inflated because of a high proportion of part-time working women consider producing a second bonus pay gap figure based on full-time equivalent bonuses which allow a like for like comparison.

6. Consider reporting on the distribution of men and women across pay deciles as well as pay quartiles.

7. If you have a large pay gap (20% or above) consider amplifying communications with staff, placing emphasis on the actions that are proposed to help close the gap.

8. Consider supplementing your figures with both an explanatory narrative and an action plan setting out future objectives and targets and report progress against them each year.

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