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Impact of the UK Employment Rights Act on UK transactions

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The impact of the Employment Rights Act 2025 on corporate transactions, plus what to expect in the next phase of reform.

The Employment Rights Act 2025 (ERA) represents a fundamental reform of employment law in the UK as we outlined in a previous update. Substantial reforms have already been introduced over a phased implementation timeline, with further measures expected in October 2026. This update focuses on the implications of the ERA in relation to employers, private equity sponsors and corporates operating in a transactional environment.

Unfair dismissal reform and senior executives

The ERA introduces a set of changes that are likely to have a significant impact at senior executive level, where dismissal risk, negotiation dynamics and compensation exposure are typically pronounced.

1. **Removal of the compensation cap**

From January 1, 2027, the compensation cap for statutory unfair dismissal claims (currently limited to the lower of 52 weeks' gross pay and £123,543) will be removed. For executives whose remuneration is heavily weighted towards bonus and long-term incentives, the cap has historically meant that statutory unfair dismissal claims were often secondary to contractual claims. However, removal of the compensation cap will result in statutory claims becoming a financially significant option, a material increase in the litigation risk for employers, and settlement dynamics potentially shifting in favor of executives.

In a private equity context, this gives rise to further considerations, for example, termination of management team members (including the operation of "good leaver/bad leaver" mechanics) may carry materially greater downside risks; employment related warranties and indemnities, particularly with respect to pre?completion terminations are likely to face enhanced diligence and negotiation; deal pricing, structuring and completion mechanisms may need to accommodate a higher potential exposure to employment claims.

2. **Reduction of the qualifying period**

With effect from January 1, 2027, the qualifying period for unfair dismissal protection will be reduced from two years' continuous service to six months' continuous service.

The new threshold shortens the period during which newly hired executives can be removed without statutory risk; increases pressure on employers to promptly assess performance and cultural fit; and may lead to more structured and intensive probationary processes.

For private equity sponsors, this is particularly relevant in acquisition-driven expansion strategies and post-acquisition management changes - new management teams will acquire statutory protection much earlier than under the current regime; the ability to test leadership hires post-completion without litigation risk will be reduced; and greater emphasis will be placed on pre-signing diligence of management capability and alignment.

3. **Extension of tribunal time limits**

From October 1, 2026 (subject to commencement regulations), the limitation period for bringing most employment tribunal claims is expected to be extended from three months to six months.

This change is likely to have procedural implications in the case of senior executive exits where negotiations tend to be complex and extended. The increased timeframe will enable more considered negotiations and legal advice, reduce the need for protective claims (i.e., claims issued in the employment tribunal to preserve a claimant's legal rights before the limitation period expires), and weaken the tactical advantage historically enjoyed by employers.

In a transactional context, this may have timing implications for deals involving management exits or reorganisations. For example, claims risk will remain "live" for longer following the executive's departure, extending the period of uncertainty around potential liabilities; there may be greater reliance on escrows, deferrals or indemnity protections where exits occur prior to or part way through a transaction; and buyers may seek more detailed disclosure around recent or ongoing disputes involving senior executives.

Practical implications for executives, employers and sponsors

These reforms are expected to reshape behaviour for executives, employers and sponsors.

- Executives will benefit from increased statutory protection but may face greater scrutiny in the early stages of employment, with greater focus on robust probationary period assessments.
- Employers and sponsors are likely to front-load risk management, with enhanced due diligence, more prescriptive performance frameworks and earlier intervention.
- Sponsors, in particular, will need to align employment strategy with deal strategy, including in relation to management incentivisation and exit planning.

Recap: key measures already in force

December 2025 (Royal Assent)

- Repeal of the Strikes (Minimum Service Levels) Act 2023.

This change, together with subsequent reforms, reflects a broader shift toward facilitating industrial action, which may increase operational risk in highly unionised sectors.

February 2026

- Repeal of most of the Trade Union Act 2016 including the removal of limitations on the duration of industrial action mandates, simplification of industrial action processes (e.g., ballots and notice requirements), and enhanced protections for industrial action participants.

These changes reduce friction for collective action and may contribute to a more active industrial relations landscape. This will be an important consideration in diligence and business planning.

April 2026: the first core implementation phase

April 2026 marked the most significant wave of reforms so far.

6 April 2026

- Increase in the maximum protective award for failure to inform and consult on collective redundancies (from 90 days' pay to 180 days' pay per affected employee).
- Introduction of "day one" family leave rights, removing minimum service requirements so that eligible employees can access paternity leave and unpaid parental leave from the outset of employment, increasing immediate workforce flexibility requirements.
- Strengthened whistleblowing protections, expanding the scope of protected disclosures (including, for example, reports of sexual harassment) and enhancing protections against detriment or dismissal, increasing the likelihood of issues being raised formally.

- Expansion of Statutory Sick Pay (SSP) by removing the lower earnings threshold and waiting period so that SSP becomes payable from the first day of absence to a broader category of workers, with direct cost implications for employers.
- Introduction of Bereaved Partners' Paternity Leave, creating a new entitlement to extended leave for bereaved partners following the death of a child's mother or primary adopter, requiring updates to employer's leave policies and procedures.
- Encouragement of voluntary gender equality and menopause frameworks by encouraging larger employers to adopt action plans addressing gender pay gaps and menopause support ahead of a move to mandatory requirements, reflecting potential increased regulatory focus on workplace equality in the future.
- Further simplification of trade union recognition by reducing procedural barriers to union recognition (including easing thresholds and processes).

From a transactional perspective, increased redundancy exposure may affect restructuring costs in carve-outs and integrations whilst expanded SSP and leave rights feed directly into workforce cost assumptions.

7 April 2026

- Establishment of the Fair Work Agency.

The creation of a centralised enforcement body signals a more interventionist approach, increasing the importance of compliance both pre- and post-acquisition.

Upcoming: key measures coming into force

August 2026

- Introduction of electronic and workplace balloting.

This may increase participation in union processes, with potential implications for workforce dynamics.

From October 2026: the second core implementation phase

The next tranche of reforms under the ERA are expected to be implemented from October 2026 extending into 2027 with precise timings currently uncertain for many of the reforms. In addition to the unfair dismissal reforms mentioned above, the major reforms focus on workforce restructuring, workplace conduct collective labour rights, and employer accountability.

Redundancy, workforce restructuring and working patterns

- Reforms to dismissal and re?engagement practices ("fire and rehire") are expected to come into force from January 2027, under which dismissals used to impose adverse contractual changes will, in many cases, be rendered automatically unfair unless strict conditions are met thereby restricting employers' ability to make unilateral contractual changes and increasing reliance on negotiation and employee consent in restructuring and post?acquisition integration scenarios.
- Reforms to collective redundancy consultation obligations, including changes to how consultation thresholds are calculated across establishments (with the detailed mechanics not yet settled), raising the likelihood that the consultation obligations will be required more frequently in workforce restructurings.
- Reforms relating to predictable working arrangements and zero?hours contracts, expected to be introduced from October 2026 on a phased basis into 2027, which may restrict the use of variable hours arrangements and reduce workforce flexibility, with potential implications for operating models and cost assumptions.

From a transactional perspective, these reforms are likely to make workforce restructurings and post?acquisition integration more complex and time?consuming. Employers will have less flexibility to implement changes unilaterally, meaning that planning, engagement and negotiation with employees will become increasingly important.

Workplace conduct and harassment

- Strengthened duty to take "all reasonable steps" to prevent sexual harassment, expected to come into force from October 2026. The existing employer duty will be expanded so that organizations must take proactive and

demonstrable steps to prevent harassment before it occurs, rather than responding only after the fact, increasing the importance of training, policies and workplace culture initiatives.

- A new obligation not to permit third-party harassment, expected from October 2026, introducing liability where employers fail to take reasonable steps to protect employees from harassment by third parties (such as clients, customers or contractors), significantly widening the scope of potential exposure in customer?facing environments.
- Power to define “reasonable steps” through regulation, granting the government the ability to prescribe, via secondary legislation, the measures employers are expected to take to comply with their obligations, creating the potential for more prescriptive and evolving compliance requirements over time.

These reforms may result in workplace culture becoming a more material diligence and governance issue where buyers scrutinise harassment policies, complaints and investigation processes to avoid legal liability and reputational risk whilst post completion integration plans may require policy harmonization and training.

Trade unions and collective bargaining

- Expansion of trade union access rights, expected to come into force from October 2026, by extending unions’ ability to enter workplaces, communicate with workers and organize more effectively, reducing practical barriers to union engagement and increasing the likelihood of workplace organisation.
- Measures addressing unfair practices in union recognition campaigns will be introduced from October 2026 onwards, including enhanced protections against employer conduct that may undermine or interfere with recognition processes, making it easier for unions to maintain formal bargaining status.
- Further enhancements to rights and protections for trade union representatives, with additional changes expected from October 2026, including enhancing legal protections against dismissal or detriment and strengthening their ability to carry out representative functions within the workplace.
- Establishment of the Fair Pay Agreement Adult Social Care Negotiating Body, creating a sector?specific collective bargaining framework in adult social care, with a statutory body responsible for negotiating minimum terms and conditions, signaling a move towards more centralized, sector?level bargaining models (implementation phased from 2026 and operational impact from 2027).

From a transactional perspective, these developments may be particularly relevant in labour-intensive sectors (including healthcare, social care, logistics and retail), where unionization risk may form a more prominent part of pre-acquisition diligence, post-acquisition operational flexibility may be constrained, and sector-wide bargaining could impact margin assumptions and valuation models.

Workforce governance and compliance

- Duty to inform workers of trade union rights, expected from October 2026, introducing an obligation on employers to actively notify workers of their right to join a trade union, increasing transparency and making it easier for unions to engage with workforces from the outset of employment.
- Introduction of a procurement code addressing “two-tier” workforces, expected from October 2026 with implementation continuing on a phased basis, establishing a framework (initially focused on public sector and outsourced services) to prevent disparities in pay and conditions between transferred employees and new hires, with implications for outsourcing models, cost structures and integration strategies.
- Further tightening of tipping laws, expected from October 2026, strengthening existing rules on the fair allocation of tips, gratuities and service charges, including enhanced obligations around transparency and distribution, and increasing the risk of claims where practices are not compliant or clearly communicated.

In outsourcing and services transactions, the evolving “two-tier workforce” framework may affect cost models, TUPE strategies and workforce harmonisation planning, particularly in light of the government’s ongoing review of the TUPE regime.

Looking ahead

The ERA should be viewed as a cumulative reform program, the effect of which is to shift the balance of employment relationships in a more protective direction. Taken together, the reforms give more power to employees (including senior management), increased union influence, more prescriptive employer obligations and a heightened risk of enforcement. Their combined effect is to increase both the financial and operational significance of employment law risk.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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