EMOLUMENTS – Receipts "from" office or employment – Payments in lieu of entitlements to "protective awards" – Redundancy proposals giving rise to obligation to consult in pursuance of TULR(C) Act 1992 s.188 – Employer did not go through consultation process and employees did not claim protective awards for such failure – Employer and trade union agreed that £2,500 he paid to each redundant employee "in recognition of any entitlements under the consultation process" – Whether the £2,500 payments were emoluments from employment – No – ICTA 1988 s.19

THE SPECIAL COMMISSIONERS

MIMTEC LIMITED Appellant

- and -

THE COMMISSIONERS OF INLAND REVENUE Respondents

Special Commissioner: STEPHEN OLIVER QC

Sitting in London on 9 April 2001

Mark Whitehouse and Naomi Crossman of K Legal, for the Appellant

David Wishart, of the Office of the Solicitor of Inland Revenue for Scotland, for the Respondents

DECISION

1. Mimtec Ltd, the Appellant, appeals against a determination made under Regulation 49 of the Income Tax (Employments) Regulations 1993 on 15 September 1998. This determined that Mimtec was liable to pay income tax of £34,500 in respect of emoluments of £150,000 for the year 1997/98.

Facts

2. Mimtec had for some years before the events of August and September 1997 carried on a manufacturing business from various different sites and through different divisions in Scotland. On 29 August 1997 Fullarton Computer

Industries Ltd purchased the entire share capital of Mimtec. Plans to rationalize the business were implemented; these involved closure of the two Mimtec divisions at Livingston. These were the Baird Road "IBM" Division and the Digital Business Division. More than a hundred employees worked in those divisions. The decision was taken that all should be made redundant. Following an announcement of the plans on Monday 1 September 1997 discussions with the appropriate trade union, the AEEU, began on 2 September.

3. On 4 September a "Staff Notice" was given to all the employees of the Baird Road Division. This confirmed that consultation had commenced on 2 September and that agreement had been reached in principle on the redundancy terms applicable to those affected by the closure. The Staff Notice summarized the agreement.

4. Further Staff Notices of 30 September were issued to the Baird Road IBM Division employees and to the Digital Business Division employees. The Staff Notice issued to the Baird Road employees reads as follows:

"This is to confirm that, following a mass meeting held on Tuesday 23 September 1997, acceptance was reached on a closure programme. This is based on the following:-

a. IBM BUSINESS HOURLY PAID EMPLOYEES AND ASSOCIATED STAFF

1. All employees will receive, by 28 September 1997, written confirmation of their redundancy package. This will consist of –

(a) A payment of £3,030 in recognition of any entitlements under the consultation process including pay in lieu of notice, etc. This is based on the current hourly rate of £4.22 plus shift allowance, and will be proportionately increased for employees on higher rates;

(b) Statutory redundancy following normal rules of calculation, i.e. full weekly wages (or equivalent) times completed years of service (inclusive of the consultation period). This would also agree subject to a 1.5 multiplier for age under the Act;

(c) The Company has agreed to match (b) on an ex-gratia basis;

(d) A further ex-gratia amount of one week’s pay per complete year of service;

(e) A retirement award (following the normal rules) for employees aged 60 and above.

2. In return for working normally until 3 October 1997, all

employees will receive full payment for all hours worked and outstanding holidays until that date.

3. A further £50 will be paid with their final pay to those employees who worked Sunday 21 and 28 September 1997. These payments are in addition to normal premium payments for these days.

..."

The Staff Notice issued to the Digital Business Unit employees on the same date reads, so far as is relevant, as follows:

"1. All employees will receive, by 26 September 1997, written confirmation of their redundancy package. This will consist of:-

(a) A payment of £2,500 in recognition of any entitlements under the consultation process, including pay in lieu of notice, etc. This is based on the current hourly rate of £4.22 plus shift allowance and will be proportionately increased for employees on higher rates.

(b)-(e) ...

2. The closure date for the Digital Business Unit is still unknown, therefore redundancy and payment dates were unknown. These will be advised as soon as they are known."

Sub-paragraphs (b)-(d) of the latter Staff Notice are in the same form as that issued to the Baird Road IBM Business employees. In the case of the IBM Business employees the amount of £3,030 referred to in sub-paragraph (a) comprises £2,500 for entitlements under the consultation process and £530 contractual pay in lieu of notice. The tax position of the £530 pay in lieu of notice and of the payments referred to in sub-paragraphs (b)-(e) is not in dispute. The same goes for the payments in paragraphs 2 and 3 of the IBM Business Staff Notice (which are treated for all purposes as emoluments).

5. The payments referred to in paragraph 4 above were duly made and the operations of the Baird Road plant were terminated and the first dismissal took place prior to the expiry of the 90-day consultation period referred to in section 188 Trade Union and Labour Relations (Consolidation) Act 1992. I refer to that Act as TULRCA. Payments to the employees in respect of the IBM Business were made on 10 October 1997 and payments made to the employees in the Digital Business were made between 3 October 1997 and 23 December 1997. I was provided with

a schedule describing payments made to the employees in all of the various categories.

6. I heard evidence from Mr Stuart Deans. He was one of the employees made redundant. He had been employed since September 1993 as a payroll supervisor at Livingston on one month's notice to either side. The terms of his employment did not include any provision entitling him to payment in lieu of notice.

7. Mimtec appealed against the determination on 23 September 1998.

The Issue

8. At issue in this appeal is the tax treatment of the payments of £2,500 made on redundancy to each employee. The payment is, as noted above, described as paid "in recognition of any entitlements under the consultation process, ... pay in lieu of notice, etc.". Mimtec contends that the payments are chargeable to income tax under section 148 of Income and Corporation Taxes Act 1988. ("ICTA"). The Commissioners of Inland Revenue ("the Commissioners") contend that the payments are emoluments from employment chargeable under section 19 of ICTA. This reads as follows:-

"(1) Tax under this Schedule shall be charged in respect of any office or employment on emoluments therefrom which fall under one or more of any of the following Cases : ..."

Given the level of payments (all below £30,000) the consequence, if Mimtec is right, is that there is no tax to pay (apart from that in respect of the retirement allowance paid to a small number of employees): see section 148 of ICTA.

9. The payments in dispute here owe their existence to certain provisions of TULRCA. The relevant statutory provisions are contained in the Appendix to this Decision. Sections 188-192, previously contained in the Employment Protection Act 1995 sections 99-107, had been passed to give effect to Council Directive 75/129/EEC. The basic obligation imposed by section 188 is for the employer to consult trade union representatives about the handling of any proposal for redundancy which affects any employees. Section 188(2) provides that the consultation process is to include consultation about ways of avoiding dismissal, reducing the number of employees to be dismissed and mitigating the consequences of the dismissals. Section 188(1A) directs that the consultation is to begin in good time and, in any event, where the employer is proposing to dismiss 100 or more employees, at least 90 days before the first of the dismissals takes place. Failure to comply with the requirements, in section 188, to consult may lead to a complaint to an employment tribunal which may make

a "protective award" (section 189) in respect of individual employees. Section 190 provides that when an employment tribunal has made a protective award, every employee to which it relates is entitled "to be paid remuneration by his employer for the protected period". Section 192 gives an employee the right to present a complaint to an employment tribunal "on the grounds that he is an employee of a description to which a protective award relates and that his employer has failed, wholly or in part, to pay him remuneration under the award".

Short summary of contentions

10. The basis for the contention for the Commissioners, presented by Mr Wishart, is that the £2,500 payments were emoluments within section 19. They were payments to which the employees were entitled. They were made in recognition of the employees' rights conferred by TULRCA to receive payment as a result of Mimtec's failure to carry out the consultation process. Specifically, Mr Wishart argued, the payments had been made to the employees in recognition of Mimtec's contingent obligations under section 192 which, together with section 190, formed part of the contractual relationship between Mimtec and its employees. Payments made under section 192 are expressed as remuneration; consequently payments, such as the present, made in substitution for section 192 remuneration are, on the strength of the decision in the House of Lords in Mairs (Inspector of Taxes) v Haughey 66 TC 273 and [1993] STC 569, to be treated as such. And, if the payments were not made in pursuance of Mimtec's contractual obligations to its employees, they were at least so directly connected with their employments and so much part and parcel of the employer-employee relationship (see Knox J in Hamblett v Godfrey 1997 TC 694) as to make the payments arising "from the employment" (see Lord Radcliffe in Hochstrasser v Mayes 38 TC 693) the argument for Mimtec, put shortly, was that the source of the £2,500 payments was redundancy; they were not paid in accordance with any contractual rights embodied in the employment contract. For that reason the payments were not taxable as emoluments within section 19 of ICTA.

Conclusions

11. Were the £2,500 payments emoluments "from" the employment's of the individual employees of Mimtec who had been made redundant? In the words of Lord Radcliffe in Hochstrasser v Mayes (supra at 707) were they made to each of them "in return for acting or being an employee"; or, in Lord Templeman's words in Shilton v Wilmshurst 64 TC 78, were they paid to each of them "for being or becoming an employee"?

12. The £2,500 payments were made to the employees, not as the result of carrying through the procedures laid

down by sections 188-192 of TULRCA, but "in recognition of any entitlements under the consultation process": see the words of the Staff Notices set out in paragraph 4 above. This feature brings into play the principle stated by Lord Woolf in Mairs v Haughey supra at 343 as follows:

"It is inevitable that if a payment is made in substitution for a payment which might, subject to a contingency, have been payable that the nature of the payment which is made in lieu will be affected by the nature of the payment which might otherwise have been made. There will usually be no legitimate reason for treating the two payments in a different way".

Here "the payment which might otherwise have been made" (to use Lord Woolf's words) will be the amount representing the entitlement of the employee in question under the protective award. The critical issue, therefore, is whether, assuming it to have been paid as a protective award, this amount would have ranked as an emolument from the recipient employee's employment. To resolve this, I return to the relevant provision of TULRCA.

13. A protective award defined in section 189(3) will be made by an employment tribunal where the employer has failed to comply with the requirements imposed by section 188 and where a complaint has been presented alleging non-compliance. Among the requirements in section 188 are that –

- the employee shall have proposed to dismiss as redundant 20 or more employees within 90 days or less (subsection (1)),
- the employee shall, where (as here) the proposed is to dismiss 100 or more employees, have started the consultation process at least 90 days before the first of the dismissals takes place (subsection (1A)),
- the consultation shall have been with "the appropriate representatives" as defined in subsection (1B),
- the consultation shall have included consultation about ways of avoiding the dismissals (subsection (2)) and
- the employer shall have disclosed the reasons for the proposals.

The rights and obligations contained in section 188 are triggered by the proposal to dismiss. They have nothing to do with the employee's rights or duties as continuing employee. And the right to be consulted is not a personal right of the particular employee; it arises from the duty

imposed on the employee "to consult all the persons who are appropriate representatives" (see subsection (1)). In principle, it seems to me, the right to any compensation made as a protective award under section 190 arises from the employer's failure to go through the consultation process in the prescribed manner. The decision of the Employment Appeal Tribunal in Spillers-French (Holdings) Ltd v USDAW [1980] 1 All ER 231 (Chairman, Slynn J) is in point here. The Tribunal was there dealing with the predecessor provisions to sections 188-192. The Tribunal concluded, at 239c, that the function of the protective award was "to compensate". It then asked the question: "to compensate for what?" The Tribunal's answer was: "to compensate for the failure to consult".

14. Drawing the threads together so far, it seems to me a protective award, if made, would not rank as an emolument within section 19 of ICTA. This follows from the fact that Act (TULRCA) is the source of the right. The right to the award does not arise unless there is a redundancy and a failure on the employer's part to comply with its obligations under section 188 of TULRCA. Without more those features would, in my view, have excluded protective awards, had they been made, from ranking as emoluments. They would not have been amounts "paid in return for" the recipient employee's "acting as or being an employee" (to quote Lord Radcliffe's words in Hochstrasser v Mayes).

15. Can that conclusion stand in view of the words used in sections 189(3), 190 and 192? The effect of a protective award is that the employer is ordered "to pay remuneration" for the protected period. That, argued Mr Wishart for the Commissioners, showed that the employee who received his entitlement under those sections following an award by a tribunal was being paid the amount of remuneration found to be due to him separate and distinct from any redundancy payment or compensation from loss of office. In my view, the fact that TULRCA expresses the award in terms of a payment of remuneration cannot of itself give the payment the status of an emolument for income tax purposes. The award is, as I interpret the provisions of TULRCA, compensation calculated by reference to remuneration that would otherwise have been paid for the "protected period" had the emoployer gone through a proper consultation process and started consulting at the commencement of that period. The award is not, contrary to the argument for the Commissioners, a payment in satisfaction of a right conferred on the employee by TULRCA to have his employment period extended by 90 days prior to the first dismissal. The 90 days is a component in the calculation of the compensatory award.

16. The Commissioners relied on EMI Group Electronics Ltd v Coldicott 71 TC 455 with particular reference to the judgment of Neuberger J which was upheld in the Court of

Appeal. At 481 the judge said –

"The terms on which an employment contract can be brought to an end seem to me to be self-evidently an inherent part of the contractual relationship".

That case was concerned with the question of whether a payment in lieu of notice, provision for which was made in the recipient's employment contract, was an emolument from his employment. Here, as the example of Mr Deans shows, the contracts of employment of none of the redundant employees contained any provision for "protective awards" on redundancy. Nor have sections 188-192 of TULRCA been incorporated by implication into the employment contracts of the Mimtex employees. It is true, as Mr Wishart pointed out, that section 288 of TULRCA treats as void any agreement that excludes or limits any provisions of that Act. But that is not the same as saying that the TULRCA provisions are to be treated as incorporated in the Mimtec employees' employment contracts. For those reasons I do not think that the EMI Group Electronics decision assists the Commissioners.

17. I turn finally to the argument for the Commissioners that irrespective of the actual terms of the contract of employment, the rights under TULRCA were at the very least directly connected with the employment. In Hamblett v Godfrey 59 TC 694 at 713, Knox J said:

"Secondly the rights in respect of which payment was made, for reasons which I have already given, were in my judgment, part and parcel of the employer and employee relationship

Similarly, in the Court of Appeal, Purchas L J stated at 723:

"The rights, the loss of which was being recognised, were rights under the employment legislation and the right to join a union or other trade protection association. Both these rights, in my judgement are directly connected with the fact of the taxpayer's employment. If the employment did not exist, there would be no need for the rights in the particular context in which Miss Hamblett found herself. So I start from the position that those are rights directly connected with the employment."

In contrast to the statutory rights to join unions etc, which are conferred on persons who are employed, the right to a protective award under TULRCA is given because the person in question, e.g. the Mimtec employee, has been deprived of his employment by redundancy without proper consultation. The right to the award arises because the employer and employee relationship has been terminated. TULRCA is the source of the protective awards, not the employer and employee relationship. Thus, had they been made, they would not have ranked as emoluments within

section 19 of ICTA.

18. Reverting to the actual £2,500 payments made to the Mimtec employees these, as I have already noted, were described in the Staff Notices as made "in recognition of any entitlements under the consultation process …". As payments in lieu of protective awards they should not, in the light of Lord Woolf's observations in Mairs v Haughey quoted in paragraph 12 above, be treated in any different way from the protective awards themselves. It follows therefore that the £2,500 payments should not be taxed as emoluments under section 19 of ICTA. Liability arises, if at all, under section 154 of ICTA.

19. For those reasons I allow the appeal.

20. For the record I mention that, although the hearing was in London, the appeal belongs in Scotland.

STEPHEN OLIVER QC

SPECIAL COMMISSIONER

Released: 16th May 2001

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