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Work Matters

Employment News

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Age Discrimination: What You Need to Know

By **Keely Rushmore**, Associate

Most commentators agree that in terms of the practical effect they will have in the workplace, the Employment Equality (Age) Regulations 2006, which came into force on 1 October 2006, are potentially among the most far-reaching pieces of U.K. employment legislation ever passed. This article summarizes some of the key aspects of the Regulations.

The right not to be discriminated against on grounds of age applies at all stages of the employment relationship, from advertising and recruitment to termination. The Regulations cover direct and indirect discrimination. Direct discrimination occurs when workers are treated differently on the grounds of age, such as a requirement that job applicants must be below 40. Indirect discrimination occurs when criteria are applied which place persons in a certain age group at a particular disadvantage when compared to other persons of a different age group, such as a requirement that all candidates for promotion must have 10 years' service. The Regulations also cover the victimisation of a worker as a consequence of him or her having taken action in connection with the Regulations and harassment on the grounds of age.

The Regulations apply to a wide range of individuals including employees proper, workers (i.e., those who contract to perform services personally but who are not in business on their own account), contract workers, office holders, partners, and members of limited liability partnerships.

Exceptions: Objective Justification

Differential treatment on the grounds of age will be lawful in certain circumstances—for example, where the employer can show that there is a genuine occupational requirement for someone of a particular age. It will also be lawful to discriminate if the employer

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can demonstrate that the difference in treatment is objectively justified. For this to apply the employer must show that he is pursuing a legitimate aim *and* that the measure in question is a proportionate means of achieving that aim.

National Default Retirement Age

The Regulations introduce the concept of a national *default* retirement age of 65. An employer may impose a lower retirement age, but only if he can objectively justify this. Prevailing opinion suggests that justifying a retirement age lower than 65 will be difficult unless, for example, the nature of the work makes this necessary, such as in a heavy manufacturing environment where there may be a legitimate concern to protect the health and welfare of the workforce. Even in these circumstances, however, a lower retirement age may not be a proportionate means of pursuing that aim because, arguably, the employer could deal with issues arising from employees who wish (or need) to retire earlier for health or welfare reasons on a case-by-case basis rather than enforcing a lower retirement age across the workforce.

Retirement: Duty to Consider

The Regulations include a new *duty-to-consider* procedure which employers *must* follow before dismissing an employee on the grounds of retirement. The procedure is as follows:

- The employer should notify the employee of his proposed retirement date between 6 and 12 months in advance (regardless of whether there is already a term in the individual's contract of employment confirming this) and inform him of his right to request to continue working beyond that date. Failure to provide this information within the correct timeframe may result in an award of compensation of up to eight weeks' pay (capped at the statutory maximum, currently £290 per week). In addition, if the employer does not provide this information at least two weeks before the proposed retirement date, the dismissal will be automatically unfair;
- An employee may ask his employer to consider continuing his employment beyond the proposed retirement date either indefinitely, for a specified period or until a specified date. Such a request may be made up to six months before the proposed retirement date;
- On receipt of such a request, the employer must, within a reasonable period, convene a meeting with the employee to discuss his request. The employer is unable to retire the employee before this meeting takes place; and
- The employer must provide the employee with a written decision as soon as reasonably practicable after the meeting, although reasons do not have to be given. The employee has a right of appeal against the decision and if he does appeal the employer must convene an appeal hearing within a reasonable period, although this may take place after the employee has retired. The employer is required to confirm the outcome of the appeal to the employee in writing.

There are transitional provisions which deal with those employees in respect of whom notice of retirement has been given prior to 1 October 2006, and those employees who will reach their retirement age within six months of 1 October 2006.

Removal of Upper Age Limit on Claims for Unfair Dismissal

The Regulations remove the upper age limit for bringing a claim for unfair dismissal (currently 65). This means that anyone, no matter what their age, will be able to bring a claim for unfair dismissal if they have the requisite length of service. Retirement will, however, be a new potentially fair reason for dismissal. Retirement is deemed to be the reason for dismissal where an employer gives the employee notification of the intended date of retirement in accordance with the *duty-to-consider* procedure outlined above and the employment ends on that date.

If the reason for dismissal is retirement, the dismissal will be fair if notification is given unless the employer fails to comply with the duty-to-consider procedure, such as the duty to consider the employee's request not to be retired and/or to consider an employee's appeal against the employer's decision not to continue the employee's employment.

Service-Related Benefits

Under a specific exemption in Regulation 32, employers are still able to award benefits to their employees on the basis of length of service save that, beyond five years' service, the employer must show that it *reasonably appears* to it that using length of service as a qualifying criteria for eligibility for employment benefits fulfils a business need, such as encouraging loyalty or motivating its staff.

There is also an express exemption for enhanced redundancy payments, provided they are based upon the formula used to calculate statutory redundancy payments in the Employment Rights Act 1996.

Pensions

The Regulations make it unlawful for the trustees and managers of occupational pension schemes to discriminate on grounds of age when carrying out their functions. A non-discrimination rule is implied into every occupational pension scheme which both binds trustees and managers and empowers them to amend the scheme rules so as to enable them to comply with the Regulations.

Certain rules and practices relating to pension schemes are expressly exempted from the Regulations. These include setting minimum and maximum ages for admission to schemes, using age criterion for actuarial calculations, and so on.

In response to concern within the pensions industry about the impact the Regulations will have on the operation of occupational pension schemes, the Government deferred the date on which the pensions aspects of the Regulations will come into force until 1 December and has widened the exemptions following consultations with industry bodies and other interested parties.

Next Steps...

Employers should:

- Check whether their standard retirement age needs to be changed. If it is under 65, can it be objectively justified? If not, employers should be prepared to change it and amend any contractual documentation which refers to it;
- Review their recruitment process. This is an area where the Regulations are likely to have a significant impact;
- Review the basis on which benefits are offered to employees and assess whether they may fall foul of the Regulations;
- Audit their policies and procedures to ensure that they are compliant. Equal opportunities and other relevant policies should be amended to specifically cover discrimination on the grounds of age; and
- Consider whether to introduce an age diversity policy and/or the monitoring of the age profile of their staff to identify and address potential problems.

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Directors' Duties and Competing Businesses

By **Nick Jackson**, Associate

A recent High Court decision has confirmed that departing directors who make preparations to compete with their former employers before they leave run the risk of breaching their fiduciary duties, even if what they do falls short of competitive activity.

In *Shepherds Investments Ltd. v Walters*, Etherton J ruled that three former directors had acted unlawfully in setting up a competing business while they were still directors and employees of the claimant companies.

Although the defendants' new business did not start trading for some months after most of them had left, the judge held them to be in breach of their duties and highlighted the need for strict adherence to the common law rules governing fiduciary obligations. He also ruled that there was no legitimate basis for an argument that the directors' fiduciary obligations could be *trumped* by a rule of public policy against restraint of trade in the interest of promoting entrepreneurial activity.

In *Shepherds*, a claim was made by two investment companies against former members of their management team. As a result of their efforts to set up a new business during the currency of their employment, those managers were able to start trading with their new business earlier than would otherwise have been the case if they had waited until the termination of their employment. The defendants claimed that they had not engaged in actual competitive activity until after their departure. The judge rejected this. He found that their actions conflicted with the interests of their employer and so were in breach of their fiduciary duties and duties of good faith.

In so finding, the judge looked closely at the case law on the scope of a director's permitted activities when establishing a competing business. He found that the authorities underpinning the duties to act in good faith and in the best interests of the company demonstrate that these duties are flexible and fact-sensitive, and are capable of application in cases and situations where they have not previously been applied, reflecting the maxim that *equity operates on conscience*.

In practical terms, the *Shepherds* case means that a director who is contemplating leaving a company to

become involved in a competing business needs to consider very carefully whether any action he takes in preparation for his move would constitute a breach of his duty to the company, and also whether the establishment of the competing business is something that he ought to report to his employer.

Approaching Clients

Another recent example of this kind of case is *Item Software (U.K.) Ltd. v Fassihi*. Mr. Fassihi, who was a director of Item Software, secretly approached the company's main customer in an effort to divert a contract away to his own company. Although Mr. Fassihi's negotiations failed, Item Software discovered what Mr. Fassihi had attempted to do and dismissed him and brought a successful claim against him on the ground that he had acted in breach of his duties as a director and employee by trying to divert the contract to his own company. It was held that Mr. Fassihi had been in breach of his duty to disclose his wrongdoing. The Court of Appeal upheld the decision on the basis that Mr. Fassihi could not reasonably have come to the conclusion that it was not in the interests of his employer to know of his breach of duty. Mr. Fassihi could not have fulfilled his duty of loyalty other than by telling his employer of his plan to divert the contract away for his own benefit.

Setting Up a New Business

Further guidance on the issue came with *Balston Ltd. v Headline Filters Ltd.* Balston manufactured and sold glass micro-fibre filter tubes. Shortly before he resigned as an employee on 17 March 1986, Mr. Head, who was also a director, arranged a lease for new business premises although he insisted that he had not decided at that time whether to set up a business as a dealer in filtration products or as a manufacturer of filter tubes. He resigned his directorship on 18 April 1986.

Before his notice expired, he bought an *off-the-shelf* company and contacted a long-standing customer to let them know that he was leaving to set up in business as a supplier of filter tubes. That client subsequently placed an order with Mr. Head's new business on 8 May 1986, sometime before his notice was due to expire on 11 July 1986.

As part of his preparations, Mr. Head bought equipment and recruited employees which included some of his former colleagues from Balston. Mr. Head also started to make sample tubes and showed them to the customer on 14 July 1986.

Based upon these facts, the judge held that prior to 18 April, Mr. Head had not been in breach of duty by failing to disclose to Balston his intention to set up a business in competition. Nor were the steps that he took in preparation to set up the business before 18 April in breach. However, the judge decided that from when Mr. Head accepted a client order and began to poach Balston's staff, he was in breach of his duty of good faith.

The judge recognised that neither having an intention to set up in competition after a directorship has ceased nor taking preliminary steps to forward that intention constituted a breach provided that there was no actual competitive activity such as tendering or trading.

In *British Midland Tool Ltd. v Midland International Tooling Ltd.*, four directors of British Midland Tool Ltd. developed a plan to leave and set up a rival company. Following the resignation of the first of them, an advertisement appeared in a local paper inviting applications for jobs with a specialist cutting tool manufacturer. Shortly afterwards, the other three resigned, followed a few days later by 12 skilled workers. To add insult to injury, the new business was set up next door to British Midland Tool and gradually more employees left to join the new enterprise with the effect that British Midland Tool had to close down.

A successful claim was brought against the former directors alleging conspiracy to damage the company. The judge pointed out that, if a director is under a duty to alert his fellow board members to a commercial threat, then that the duty would be all the greater (and certainly no less) if he himself was planning to be part of that threat. The judge therefore concluded that a director who wishes to engage in a competing business and not disclose his intentions to the company ought to resign his office as soon as his intention has been irrevocably formed and he wishes to take preparatory steps.

Practical Issues

The key issue is usually to determine where the line is between lawful and unlawful preparatory activity. Although it is dangerous to generalise, the following have been held to be permissible:

- Identifying premises for a new business and negotiating a lease
- The purchase of an off-the-shelf company
- Negotiating and agreeing terms of employment with a competing business
- Entering into heads of terms for the formation of a company to carry on a competing business

At the other end of the spectrum, actual competitive activity such as competitive trading, competitive

tendering, competing with the former employer for equipment and staff, and accepting a loan from a customer have been held to be unlawful.

To a degree, until the *Shepherds* judgment, the question as to whether a director or employee had to go as far as actual competitive activity in order to step over to the wrong side of the line remained unanswered. There were plenty of examples of activities which did *not* cross the line as distinct from those which did.

In *Shepherds*, Mr. Justice Etherton held that the decision and reasoning in *British Midland Tool* were correct. In so far as there was any conflict between that case and *Balston*, the approach of *British Midland Tool* was to be preferred. In reaching this conclusion, the judge rejected the defendants' argument that rules of public policy preventing restraint of trade *trumped* a director's fiduciary duty and duty of good faith. Instead, he determined that a director is free to resign his directorship (thereby putting an end to his fiduciary duty) at any time notwithstanding the damage that the resignation may itself cause the company.

In offering examples of the moment at which a director might fall into breach, the judge suggested that the making of a decision to set up a competing business at some point in the future and discussing such an idea with friends and family would not *per se* be in conflict with the best interests of the company and the employer. Nor, he said, (depending on all the circumstances) would the consulting of lawyers and other professionals necessarily be inconsistent with a director's fiduciary duties and his duty of fidelity.

At the other end of the spectrum, it would be plain, he said, that soliciting customers and carrying on a competing business would be in breach of both duties. "It is the wide range of activity and decision making between the two ends of the spectrum which will be fact sensitive in every case", the judge concluded, suggesting that it would be too prescriptive to say that a director must resign once he has irrevocably formed the intention to engage in the future in a competing business.

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Are Payments in Lieu of Notice Taxable?

By **Emma Byford**, Associate

Whether or not to tax termination payments is a perennially difficult issue for employers. One category of severance payment, payments in lieu of notice (PILONs), have caused more difficulty than most. The case of SCA Packaging Ltd. v HMRC deals with the issue of the taxation of PILONs where there is no express right to pay in lieu in the employment contract.

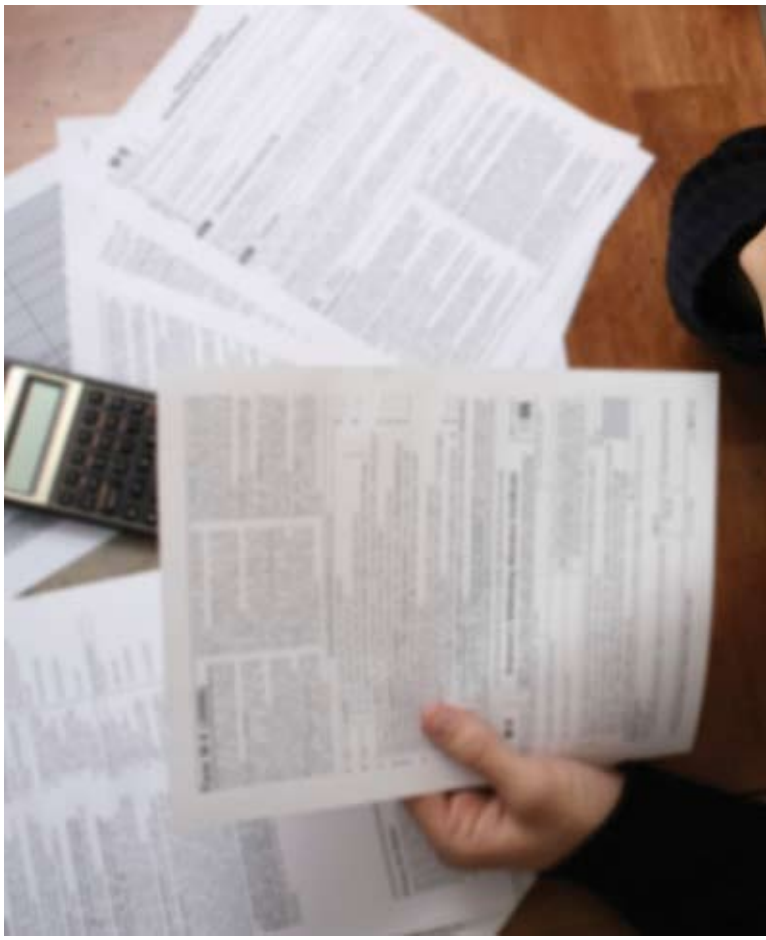
SCA made payments to a number of employees upon redundancy without deducting income tax or NICs, which included an amount calculated by reference to unexpired notice periods. The issue was whether the payments were *from employment* and thus taxable as earnings, as HMRC had determined in various notices issued to SCA.

The facts of the case were complex because there were three different groups of employees, each of whose contractual situation differed. The common feature was that none of the employees' contracts contained a PILON clause. Two of the groups of employees (both *non-office* workers) had signed a written statement (usually shortly after the commencement of employment) which stated (among other things) that the employees' main terms and conditions "will be in accordance with the provisions set out in the National/Local Agreements currently in force with the appropriate Trade Unions".

The written statement went on to specify which matters were subject to those documents and included "details concerning redundancy rights and procedures". One such trade union agreement was a Memorandum of Agreement, entered into in February 1992 by SCA and various trade unions. This set out the terms SCA should apply upon redundancy, including payment and in relation to existing employees stated that "payment will also be made of any unexpired period of notice as at the date of termination". A similar clause entitled new employees to "redundancy pay plus notice paid in lieu" subject to a four-week minimum payment.

Incorporation of the Terms into the Employment Contract

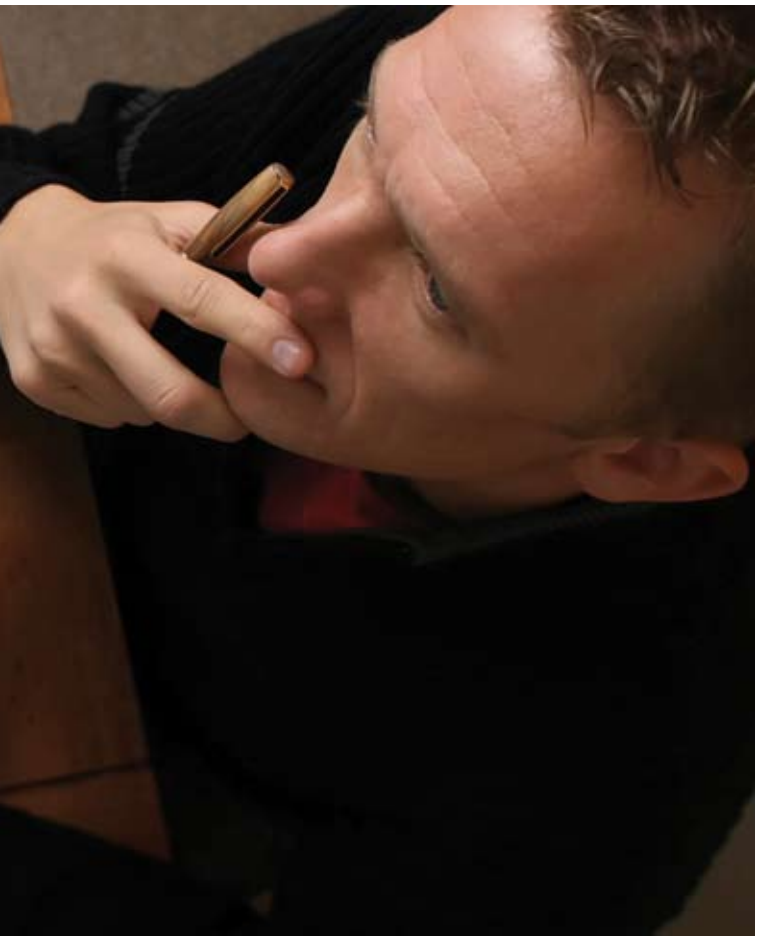
The Special Commissioner first had to consider, as a matter of employment law, whether the written statement and the Memorandum of Agreement were incorporated into the non-office workers contracts.



They held both to be incorporated because they touched directly on the relationship between employer and employee. In respect of the third category of workers (*office* workers), the Special Commissioner concluded the opposite, because it appeared from the information available to them (albeit that they only had evidence relating to one employee) that the office workers had not received the standard written statement, and the alternative written statement did not refer to either collective agreements or redundancy terms. Neither was the Memorandum incorporated through custom because the practice was not proven to be "reasonable, certain, and notorious" on the evidence available to the Special Commissioner.

Proper Construction of the PILON?

HMRC had argued that the PILON clause should be construed as giving the employer a right to terminate on short notice coupled with the obligation to make a payment to the employee, or in the alternative, as giving the employee a right to receive the payment if dismissed on short notice. The Special Commissioner did not agree with either interpretation and instead held that SCA was required to give notice to the employee but could *ask* the employee to accept (as



part of the orderly run down of the business) payment as an alternative. If the employee accepted this, then SCA would be obliged to pay, but if the employee did not accept, then the SCA had no right to terminate on short notice.

Was the PILON Derived from Employment?

The Special Commissioner then went on to consider the third and final question of whether the payment derived from employment. After considering a number of authorities, the Special Commissioner held that the agreement to accept short notice had the effect of varying, rather than abrogating, the employment contract. The fact that the acceptance would inevitably lead to the contract existing for a shorter period was irrelevant as the variation was still separate and distinct from termination. As a result, payment could be said to be made under the terms of the contract.

Nevertheless, the Special Commissioner did not stop there and went on to state that "the fact a payment is made under the terms of the contract does not seem to me to be an end to the matter: it does not inevitably lead to the conclusion that the payment was from the employment", and posed the further question "from whence did the payment come"?

The Special Commissioner's answer was that payment came from the employees' agreement to give up certain rights under the contract, and was taxable, distinguishing the case from *Henley v Murray*, where it was held that the payment for giving up the whole contract was not taxable as earnings.

In respect of the office workers (where the Memorandum of Agreement was not incorporated into their contracts), the Special Commissioner held that the payment was for the cancellation, rather than modification, of their contracts and did not therefore derive from employment. As a result, the payments made to such employees were not taxable as earnings. It seems that had HMRC provided evidence to rebut the assertion that the practice of following the procedure in the Memorandum was "reasonable, certain, and notorious", the outcome may have differed for at least some of the office workers.

One of the most interesting features of the case was the Special Commissioner's reaction to HMRC's argument that payments had been made by SCA habitually and should therefore be taxable in any event. The Special Commissioner simply stated "the fact that a payment is made habitually does not determine where it comes from" and went so far to say that "if a payment is habitually made for renouncing a right under contract or for abrogating a contract but does not become so notorious a part of the deal between employer and employee as to be a contractual term, the habitual nature of the payment does not affect a conclusion that the payment comes from the renunciation or the abrogation".

Conclusion

This case seems to be a double-edged sword for both HMRC and taxpayers. On HMRC's side, the Special Commissioner has widened the scope of what may be considered *contractual* PILONs by including agreements struck with trade unions. On the other hand, the Special Commissioner appears to expect a little more from HMRC—simply because a PILON is made under a contract does not, it seems, answer the question "from whence did it come"?

Similarly, HMRC may now have to reconsider its advice in Tax Bulletin 63 (2003), where it states that PILONs which are an automatic response to termination may be taxable. For the time being, this case seems to offer little by way of clarification for those practitioners and employers seeking to ensure PILONs are not taxable as earnings. Nevertheless, as it seems likely that HMRC will appeal this decision, we can at least be sure that this is not the end of the story.

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Sexual Orientation Discrimination: Latest Developments

By **Karen Ferries**, Associate

The Employment Equality (Sexual Orientation) Regulations 2003 make discrimination against workers on grounds of sexual orientation unlawful since 1 December 2003. Here is a look at how the law has operated thus far.

The Regulations define *sexual orientation* widely as a sexual orientation towards persons of the same sex (lesbians and gay men), persons of the opposite sex (heterosexuals), or persons of the same and opposite sex (bisexuals).

Discrimination on these grounds can take four forms: direct or indirect discrimination, victimisation, and harassment. Direct discrimination occurs where a person is treated less favourably due to their actual or perceived sexual orientation. Indirect discrimination arises where a *provision*, *criterion*, *or practice* (PCP) which is applied generally, puts persons of the one sexual orientation at a disadvantage when compared with other persons of another sexual orientation, and which cannot be justified on objective grounds—that is, the employer cannot show that the PCP is a proportionate means of achieving a legitimate business aim.

Harassment on grounds of sexual orientation occurs when a person, on grounds of sexual orientation, engages in unwanted conduct which has the purpose or effect of violating the claimant's dignity, or creating an "intimidating, hostile, degrading, humiliating, or offensive environment" for the claimant. Victimisation occurs where the claimant is treated less favourably on the grounds that he has brought proceedings, given evidence, asserted rights, or made allegations in relation to the Regulations.

Case Law

As yet there are no appellate court decisions on the Regulations. However, there are numerous employment tribunal decisions which illustrate how the Regulations are being applied. Some of these cases are described below.

Whitfield v Cleanaway U.K.

This case, heard in January 2005, was the first successful case to be brought under the Regulations. Mr. Whitfield was a gay office manager at the waste

disposal company Cleanaway U.K. He resigned after enduring months of barracking and derision from his sales manager, who continually referred to his sexuality.

Mr. Whitefield was dubbed *Sebastian* (after a camp sit-com character) and referred to as queer, dear, and queen. He was presented with a pink-lettered T-shirt at a conference in front of 60 colleagues, and ridiculed for ordering a Kir Royale drink. He claimed constructive dismissal on the grounds of sexual orientation. The Stratford employment tribunal found the claimant had been subjected to "sustained harassment" and awarded him £34,345 in compensation.

This case is a useful illustration of the sort of workplace language and behaviour which, post-December 2003, is likely to expose the maker and his employer to successful claims for discrimination on grounds of sexual orientation.

Whitehead v Brighton Marine Palace and Pier Company Ltd.

Mr. Whitehead is gay and worked for Brighton Marine Palace and Pier Company as an arcades operations manager. He made various complaints about his manager and then went off sick. The manager then wrote him an uncompromising letter informing him that he would only be paid statutory sick pay while absent.

When he came back to work Mr. Whitehead was told by a colleague that the manager had referred to him as a "chutney ferret" who lived in "Chutney Towers". When he heard this, Mr. Whitfield walked out and sued for constructive unfair dismissal, direct sexual orientation discrimination, and harassment.

The tribunal found that the comments made by the manager, even though spoken to a third party, amounted harassment on the grounds of sexual orientation, and justified Mr. Whitehead's resignation and claim for constructive dismissal. Mr. Whitehead was awarded £9,215 in compensation.

Brooks v Findlay Industries U.K. Ltd.

Mr. Brooks was a homosexual who tried to keep this a secret at work but his manager found out and thereafter mocked him for it. His manager also told the head of HR and eventually the whole workforce learned about Mr. Brooks' sexuality. This led to further banter, leg-pulling, and inappropriate language. Mr. Brooks declined to pursue a grievance because he felt it would only make things worse. Some time later he learned that his employment was to be terminated.

Mr. Brooks then sued for sexual orientation discrimination. The tribunal found that he had been subjected to direct discrimination and harassment and that the spread of rumours about his sexuality constituted harassment. The tribunal also found that the company should have acted in response to the harassment and taken the issue more seriously. The tribunal held that this amounted to direct discrimination because managers would not have treated a hypothetical comparator in the same way. In addition, it did not help that the company's equal opportunities policy made no reference to sexual orientation discrimination.

Gismondi v Durham County Council

Mr. Gismondi was the Group Bookings Coordinator at Durham's Gala Theatre. He was repeatedly referred to as "gay boy" by his manager, a press officer for Durham City Council. He resigned and claimed constructive dismissal and sexual orientation discrimination.

His claim succeeded and in its judgment the tribunal lambasted the council. It found that Mr. Gismondi had been bullied and harassed due to his sexual orientation. The tribunal said that the council's failure to protect Mr. Gismondi "ought to cause them considerable shame", and added that the process adopted by the council was "an utter shambles". It went on to find that the council had "signally failed in their duty to an employee who has been bullied and harassed, contrary to their own express policies". It also commented: "it is hard to envisage conduct more likely to shatter the trust and confidence of an employee in his employer".

Implications of the Regulations

As claims of this nature are likely to increase, it is advisable for employers to take steps to minimise their exposure to claims by making their employees aware of the Regulations, putting in place appropriate policies and procedures, and providing training. ACAS has published guidelines for employers and employees called "Sexual Orientation and the Workplace" which may assist.

Employers should bear in mind that failure to get to grips with sexual orientation discrimination can result in claims, tribunal hearings (which are often lengthy in discrimination cases), awards of compensation (there is no upper limit on compensation), lost management time, legal fees, resignations, and a negative working atmosphere.

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Maternity Law Update

By **Will Winch**, Associate

The Maternity and Parental Leave etc. and the Paternity and Adoption Leave (Amendment) Regulations 2006, which came into force on 1 October, make far-reaching changes to maternity rights.

The new rules affect employees whose expected week of childbirth is on or after 1 April 2007, or whose child is expected to be placed with them for adoption by that date or, in cases of overseas adoption, a child who enters the U.K. on or after 1 April 2007.

The key changes to the existing maternity rules are as follows:

- Statutory maternity pay will be payable for 39 weeks rather than the current 26 weeks, with six weeks at 90% of average weekly earnings and 33 weeks at the prescribed SMP rate (currently £108.85 per week);
- An employee who qualifies for ordinary maternity leave (i.e., an employee who has notified her employer by no later than the end of the fifteenth week before the expected week of confinement (EWC) of her pregnancy, her EWC, and the date on which she wishes her maternity leave to start) will now also qualify for additional maternity leave;
- The period of notice which the employee is required to give to her employer of her intention to return to work (if earlier than the end of her additional maternity leave) is extended from 28 days to eight weeks;
- An employee who gives the required eight weeks' notice and who then decides to return to work *earlier* than the original return date, must give her employer not less than eight weeks' notice of the new return date;
- An employee who gives the required eight weeks' notice and who then decides to return to work *later* than the original return date, must give her employer not less than eight weeks' notice ending with the original return date;
- Similar rules apply regarding notice for employees on statutory adoption leave;
- An employee on maternity leave may agree with her employer to carry out up to 10 days work during her maternity leave without bringing her maternity leave to an end. For these purposes, *work* includes training and any other activity undertaken to assist the employee in keeping in touch with the workplace; and
- The small employers' exemption has been removed so that the employee has a right to return to the same or a similar job regardless of the size of the organisation for which the employee works. If the employee is prevented from so doing in these circumstances the dismissal will be automatically unfair.

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Pro-Rating Bank Holidays for Part-Time Workers: Is it Necessary?

By **Carl Vincent**, Associate

For some time, there has been debate about whether the Part-Time Workers (Prevention of Less Favourable Treatment) Regulations 2000 prohibit an employer from treating full-time and part-time workers differently in respect of bank holidays. In the case of McMenemy v Capita Business Services, *the Employment Appeal Tribunal has examined the difficult question of whether part-time employees who do not work on Mondays are entitled to a pro rata apportionment of extra time off in respect of bank holidays which always fall on a Monday.*

Of the U.K.'s eight bank holidays, four always fall on Monday (Easter Monday, May Day, Spring Bank Holiday, and August Bank Holiday). One always falls on a Friday (Good Friday), and the other three vary. In *McMenemy* the employee worked on Wednesdays, Thursdays, and Fridays, and the employer operated seven days a week. At first instance, the tribunal found that the part-time employee suffered a detriment compared with full-time workers, in that he did not receive the benefit of Monday bank holidays. But it held that the reason for this was not his status as a part-time worker, but simply because he did not work on Mondays and accordingly his claim was dismissed.

On appeal by the employee, the Employment Appeal Tribunal upheld this decision. In doing so it placed considerable emphasis on the fact that the employer operated a seven-day a week business and that full-timers who worked five days a week, but excluding Mondays, also did not receive time off for those bank holidays.

Nonetheless, this decision provides some support for employers who do not give part-time workers additional pro rata time off (or pay in lieu) in respect of bank holidays. This is because the central reasoning of the decision was that the less-favourable treatment was not *on the grounds* that the employee in question was part-time. Rather, the reason was the employer's policy of giving paid time off for bank holidays provided it was a working day in the first place. To illustrate the point, the operation of this policy would work to the advantage of a part-timer for whom Monday was a working day in that he would do proportionately better than a full-time colleague.

However, it remains to be seen whether the same approach would be taken with a five-day-a-week business (rather than seven) where all full-timers receive the benefit of bank holidays. Many commentators, including the author of the DTI guidance note, take the opposite view.

In addition, the EAT in *McMenemy* did not deal with justification as it was not necessary to do so. Under the Regulations, an employer has a defence to less favourable treatment if it can objectively justify the differential. Were justification an issue, it is arguable that an employer would be justified in restricting the benefit of time off for bank holidays to people who *actually work* on those days, even if doing so has a detrimental impact on part-time workers.

Finally, it should be appreciated that the employment contract will have a bearing on the issue. In a case such as *McMenemy*, the outcome turned on the Regulations. But where the employment contract itself provides for parity, e.g. by stating that employees are entitled to benefit from bank holidays pro rata to their hours of work, the contract will prevail. The way to avoid such an outcome is to have the term as to holidays which provides: "You are entitled to all those statutory holidays (in England and Wales) which coincide with your working days", or similar.

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Case Roundup

Agency Workers

In *Cable & Wireless v Muscat*, the Court of Appeal confirmed that an agency worker could, by virtue of an implied term, be an employee (and, on the facts in Cable & Wireless, was an employee) of an end-user client in a typical tripartite agency/temporary worker/end-user case.

Polkey Reductions

When calculating loss for the purposes of assessing compensation, employment tribunals have a wide discretion to make a *Polkey* reduction (i.e., a finding that a dismissal would have occurred, or probably occurred, in any event, even if a fair procedure had been followed). In *Gover v PropertyCare Ltd.*, the Court of Appeal confirmed this principle and also held that a Polkey reduction is a matter for the impression and judgment of the tribunal and the principle underlying it is part of the tribunal's overriding obligation to award compensation that is *just and equitable*.

Collective Redundancies

Effective 1 October, the law on collective redundancies changed to bring U.K. legislation in line with the ECJ decision in *Junk Kuhnel* in the form of the *Collective Redundancies (Amendment) Regulations 2006*.

The amendment operates by way of a change to s193 of TULR(C)A 1992 and makes it clear that employers must notify the Secretary of State at least 30 (or 90 as the case may be) days *before any notice of redundancy has been issued*, rather than before notice of redundancies takes effect. Oddly however, the DTI does *not* intend to amend s188 of TULR(C)A 1992 (the parallel provision requiring employers to inform and consult employee representatives) as it believes that obligation to inform and consult "in good time" and at least 30/90 days before the first of the dismissals takes effect is not inconsistent with *Junk*.

Rolled-Up Holiday Pay

In *Caulfield v Marshalls Clay Products*, the ECJ ruled that rolled-up holiday pay is *prima facie* unlawful. However, if the holiday pay element of the rolled-up payments is a genuine addition to the hourly rate and sufficiently transparent, the employer can set off those payments against money due for the specific period when leave is actually take—so it is felt that the decision actually makes little difference in practice.

Statutory Grievance Letters

Canary Wharf Management v Edebi is a decision on whether a letter of complaint from an employee qualifies as a statutory grievance letter enabling an employee to bring a tribunal claim. The issue in the case was whether the employee had raised a disability discrimination complaint in his grievance letter (as well as complaining about other matters). The court said that there were no set requirements for the format of grievance letters; they could take the form of a resignation letter or a solicitor's letter and they could also deal with other issues.

However, there were limits to what qualified. The letter must inform the employer of the employee's *complaint*. And the complaint so referred to must be essentially the same as the tribunal claims which follows on from it. Whether this has occurred must be analysed in a non-technical way. The test is whether, on a fair reading of the letter—and having regard to the context—the employer could be expected to appreciate that the relevant complaint was being raised.

Or, in the words of Elias P: "It seems to me that the objective of the statute can be fairly met if the employers, on a true reading of the statement and having regard to the particular context in which it is made, can be expected to appreciate that the relevant complaint is being raised".

On the facts of the case, the judge held that the grievance letter, albeit containing a variety of lengthy complaints about the employee's health, did not raise an issue which an employer could reasonably understand had arisen under the disability discrimination act. Thus his disability discrimination claim was not allowed to proceed.

Compensatory Award – Deductions

Knapton v ECC Card Clothing Ltd. is a case dealing with the assessment of compensatory awards by employment tribunals. It is authority for two propositions:

- If an employee chooses to draw his pension early, following dismissal, the value of his pension benefits should *not* be deducted from any compensatory award; and
- If his remuneration package includes life insurance, the compensatory award should *not* include compensation for the cost of purchasing that insurance, to the date of the hearing, unless the employee actually purchased alternative insurance cover. Assuming the employee has not died, he has suffered no financial loss by being uninsured.

Equal Pay

In *Cadman v Health and Safety Executive*, the European Court of Justice ruled that employers do not need to provide specific justification for using length of service as a criterion in a pay system, even where that results in unequal pay between men and women unless the worker can provide evidence which raises serious doubts as to the appropriateness of rewarding experience in this way, having regard to the particular job in question.

Harassment

The House of Lords ruled in *Majrowski v Guy's & St Thomas's NHS Trust* that an employer can be vicariously liable, in an appropriate case, for the statutory tort of *harassment* under the Protection From Harassment Act 1997. For this to occur, the tort must be committed by an employee in the course of his employment, i.e., there must be a sufficiently close connection between the wrongful act and what the employee was authorized to do at work.

Sex Discrimination

In *Way v Crouch*, the EAT ruled that an employment tribunal has jurisdiction in a sex discrimination case to make an award of compensation against an employer and a manager who has *knowingly aided* an act of sex discrimination on a joint-and-several basis. The significance of an award on a joint-and-several basis is that the claimant may enforce the whole award against one or other of the defendants. N.B: this point arises in discrimination cases only and does not apply to unfair dismissal cases.

Recovering Tax from Ex-Employees

By **Charles Wynn-Evans**, Partner

Does an employer need an express indemnity to recover tax which it has paid on behalf of an employee?

The recent high court case of *McCarthy v McCarthy & Stone* concerned the exercise of share options by a former employee and director of a company, and the payment of tax due on the gains made by the employer. The employer then attempted to recover the tax it paid over to HM Revenue & Customs from the former employee without the benefit of an express indemnity clause.

For income tax purposes, income from employment includes *general earnings* (such as salary) and *specific employment income* (which includes share-related payments and benefits). PAYE is the statutory system of deducting income tax at source so as to secure, as far as is possible, that an employee's income tax liability is satisfied by the deductions made. This means that the employer effectively acts as an unpaid tax collector. The same principle applies in respect of national insurance contributions.

An employee who is allowed to acquire shares on terms more favourable than those available to the public is taxed on the value of the benefit he receives, subject to various exemptions for particular types of scheme. Where an employee makes a gain by exercising options over shares and the shares purchased are readily convertible, i.e., saleable, the employer must operate PAYE.

A problem arose in this case because Mr. McCarthy's employment had terminated when the options were exercised. The company was compelled to pay over income tax and employee national insurance on the gain to the Revenue and seek to recover this from Mr. McCarthy. It could not do so pursuant to an express right because an indemnity was lacking in its documentation.

Litigation followed. Mr. McCarthy sought a declaration that he was entitled to exercise further options. The company counterclaimed alleging that it was entitled to the £197,931.33 in tax and national insurance contributions it had paid arising from the share options which Mr. McCarthy had exercised (and which he refused to reimburse). The company applied for summary judgment on its counterclaim.

Summary Judgment

Under the court rules, the court may enter a summary judgment if it considers that the defendant has no real prospect of successfully defending the claim and there is no other compelling reason why the case should go to trial.

The company argued for summary judgment on three grounds: (1) that McCarthy had an express obligation to reimburse, (2) that alternatively there was an implied term to this effect, and (3) it had a right to repayment under the law of restitution. The judge found for the company on the basis of ground (3), the restitutionary right to repayment.

The judge held that the Company was entitled to reclaim amounts it had paid on the employee's behalf for tax and national insurance because three conditions were met, namely:

- The company was compelled, or was compellable by law, to make the payment
- The company did not officiously expose itself to the liability to make the payment
- The company's payment discharged a liability of the *defendant*

McCarthy relied on a technical argument, turning on tax law, that the third of these limbs was not satisfied because the payment was not his liability. The judge disagreed, first citing s.59A TMA 1970, which states a taxpayer must pay the Revenue any tax assessed payable over and above the amount deducted at source, and second, ruling that the mere fact that the law is designed so that the Revenue obtains the tax payable earlier than it might otherwise do or from someone other than the ultimate taxpayer was irrelevant.

A Victory for Employers?

The existence of a possible restitutionary right in this area has been mooted for some time and *McCarthy* provides support for the proposition, although this was only a summary judgment case (i.e., it was decided on the papers and did not go to trial). The issue most often arises in the context of severance arrangements. Once the employee has gone, if the employer has not deducted the correct amount of tax from any payment made on termination, the employee has gone and there are usually no further payments due to the employee from which it can deduct the monies it has paid over to the Revenue on his or her behalf.

Despite this decision, it remains advisable for employers in share option deeds and termination situations to continue to seek an express contractual indemnity for the repayment of income tax and national insurance paid to the Revenue on behalf of the employee, rather than rely on the law of restitution.

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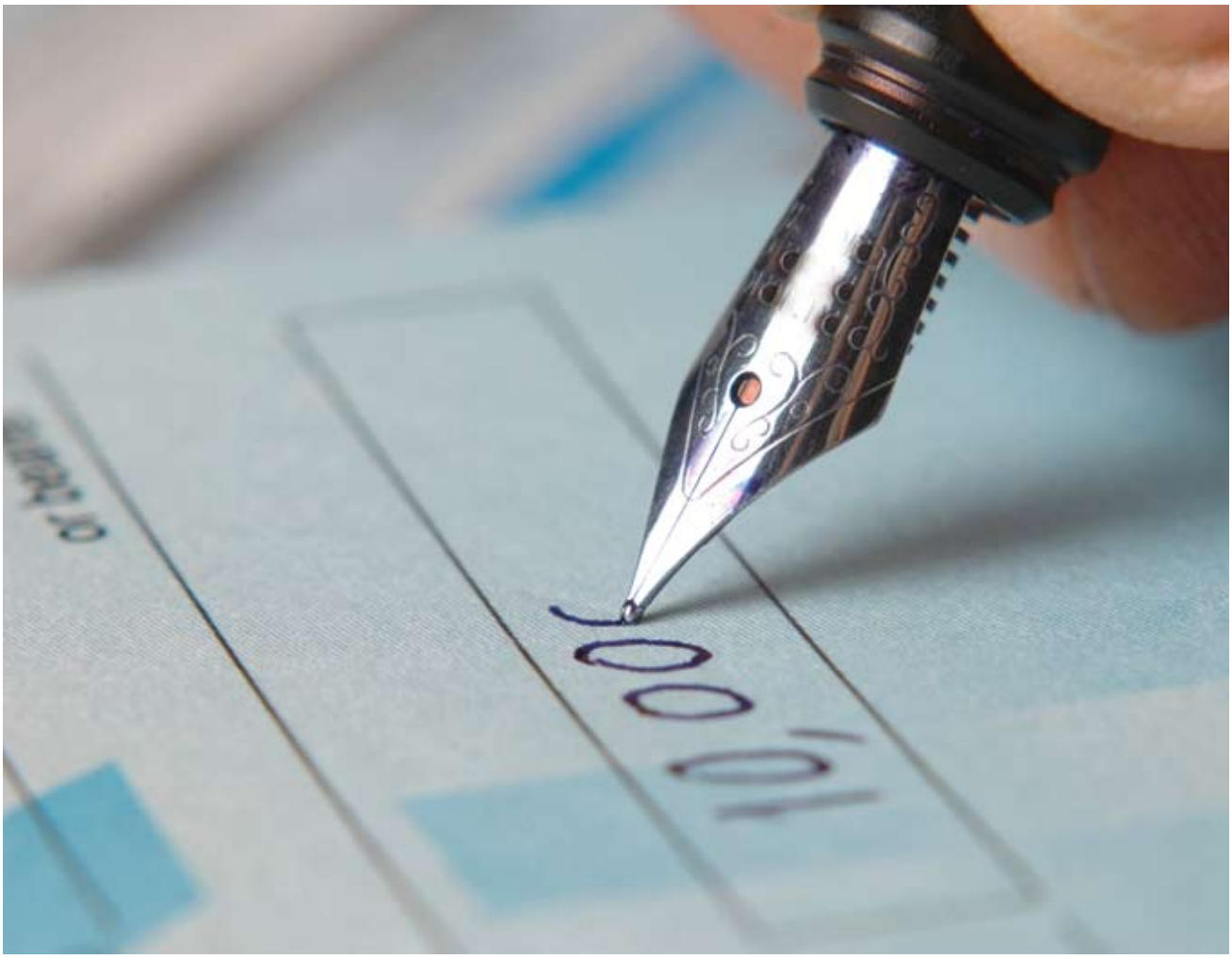

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