



EMPLOYMENT TRIBUNALS

Claimant

Respondent

v

Mr A Dowie

Riverside HiFi

Heard at: London South Employment Tribunal

On: 24 May 2019

Before: EJ Webster

Appearances

For the Claimant: In person
For the Respondent: (Counsel)

JUDGMENT

1. The Claimant's claims for unfair dismissal, statutory redundancy pay, breach of contract and unlawful deduction from wages are dismissed due to the illegality of the contract.

REASONS

The hearing

1. By an ET1 dated 6 October 2018 the claimant brought claims for unfair dismissal, breach of contract unlawful deduction from wages, notice pay and statutory redundancy payment. By an ET3, submitted to the tribunal on 21 September 2018, the respondent defended all the claims.
2. The tribunal was provided with one large bundle. At the outset of the hearing the claimant produced some additional documents namely signed statements from individuals regarding his character which I agreed could be added to the bundle as the respondent had been provided with a copy that morning.

3. Subsequently, during his cross examination of the witnesses the claimant produced more documents. The respondent objected to them being accepted. Those documents were pages of a diary which the claimant asserted demonstrated that he had been working when the respondent's digital diary did not. After some deliberation I accepted those pages as I felt that the prejudice to the unrepresented claimant of not allowing those documents outweighed the prejudice to the respondent who was legally represented throughout the hearing and beforehand and who was in a position to take instructions regarding the documents and respond accordingly. I allowed a witness to be released from oath in order to provide those instructions. I felt that it was in the interests of the overriding objective to allow the limited additional documents.
4. At the hearing I heard evidence from the Claimant, and for the respondent; Mr P Shah and Mr V Shah.

Issues

5. The issues were agreed with the parties at the outset of the hearing.

Illegality

6. Was the contract illegal under common law because part of the claimant's 'wages' were paid in such a way that both parties intended to avoid payment of tax and national insurance contributions?

Unfair Dismissal

7. What was the reason for the dismissal? The respondent asserts that it was redundancy which is a potentially fair reason for section 98(2) Employment Rights Act 1996. It must prove that redundancy was the reason for dismissal.
8. Did the respondent require fewer people to carry out the work that the claimant performed?
9. Was there any suitable alternative employment available for the claimant?
10. Did the respondent follow a fair procedure and consultation process when dismissing the claimant for redundancy?
11. Does the respondent prove that if it had adopted a fair procedure the claimant would have been fairly dismissed in any event? And/or to what extent and when?
12. If no fair procedure was followed would the respondent have dismissed the claimant in any event?
13. If the dismissal was unfair, would the respondent have been entitled to dismiss the claimant in any event by reason of gross misconduct?

Breach of contract

14. Was the claimant contractually entitled to be paid £900 net per week?
15. If yes, how much had the claimant been paid to date? The claimant asserted that he was owed in the region of £51,000. He understood that the tribunal could only award up to £25,000 in respect of breach of contract claims.
16. The claimant asserted that whilst he had received his notice pay he had received it at a lower rate than £900 net per week and was therefore still entitled to additional sums.

Unlawful Deduction from wages

17. The claimant claims that he was underpaid over the course of his employment in a series of unlawful deductions amounting to approximately £51,000. The respondent asserts that he was only entitled to an annual salary of £32,146 which was paid in full each month.
18. Was the claimant entitled to be paid £900 net per week and later £990 net per week?
19. If yes how much has the claimant been paid to date?

Both parties accept that the claimant was given goods as well as cash during his employment. The tribunal must therefore consider whether the payments received and owed (if owed at all) fall within the definition of wages as set out at s27 Employment Rights Act 1996.
20. When was the last date on which any deduction was made?

Factual Findings

Background

21. The respondent owns and operates an electrical installation business which installs music systems for its customers. Mr Paresh Shah and his son Mr Vineet Shah are directors and joint owners of the business.
22. The claimant worked for the respondent as an installation engineer. He originally worked for them on a self-employed freelance basis. He then began working for them on an employed basis in either 2003 and 2004. There is no written contract of employment.
23. The claimant was dismissed by the respondent on 26 July 2018. He attended a meeting with Mr V Shah and Mr N Dear at which he was told that he was being made redundant. It is accepted by the respondent that they did not write to him prior to the meeting telling him its purpose of the meeting or of his right to be accompanied at the meeting. They also accept that they did they carry out any consultation process.

24. The respondent states that they had had a significant downturn in work since the digitization of music and the significant increase in easy to install digital music systems. Due to this downturn they no longer needed a full time installation engineer. The claimant disagreed and stated that the dismissal had occurred because he had asked for the balance of the monies he says he was owed to be paid to him and that as a result Mr P Shah had decided he had to be dismissed. The claimant accepted that there had been a downturn in work but not so significant that it warranted his dismissal.
25. The respondent also asserts that the claimant's behaviour just prior to his dismissal amounted to gross misconduct and would have entitled them to dismiss him for this reason in any event. However they state that the real reason for dismissal was redundancy.

Contract and payments

26. The parties differ on the exact date that the claimant became an employee. I was not provided with payslips this far back. The claimant stated that he believed it was 2003 and the respondent asserted that it was 2004. I accept the respondent's assertion that it was 2004 on the basis that the claimant's records of payments and goods made to him are only provided from 2005 onwards.
27. The claimant asserted that at the time at which he became an employee as opposed to a freelancer, Mr P Shah agreed to pay him the equivalent of £900 net per week. This was based on the amount that the claimant states he was earning as a freelancer at that time. The claimant states that they agreed that he would be paid part of the money (initially £32,000 through PAYE) and that any shortfall would be made up by Mr P Shah in the form of lump sum cash payments and goods.
28. The respondent refutes this. They state that the claimant was only entitled to be paid £32,000 in wages. They state that the 'going rate' for an electrical engineer was only £25,000 and therefore the claimant's assertion that he could expect to be paid such a significantly higher amount was not plausible. The claimant's payslips record a £32,000 annual salary and this was all that he was entitled to.
29. The respondent did accept that over the period of his employment the claimant was given large amounts of money by Mr P Shah in various lump sum payments and by giving him goods at cost price or for free which he could then sell on to others. They also paid off the claimant and his partner's credit card totals and made direct payments to the claimant's son's nursery for his fees. Mr P Shah stated that all of these payments were loans and not intended to be payment for work done.
30. The claimant kept a record of the payments made or goods given to him against the running entitlement to £900 per week. This was at pages 260-269 of the bundle and ran from 2005 until 2015. This document was sent to Mr P Shah by email on 12 June 2015. At that point the total owed was stated as £77,414.43. No evidence was provided that suggested that Mr P Shah disagreed with this total at the time or found the existence of such a running tally of money received offset against money owed as being strange or incorrect.

31. The claimant accepts that it was 'naïve' of him to have allowed such a series and significant number of underpayments to continue for so long. He accepts that other than keeping Mr P Shah up to date with the tally, he did not ask for the money to be paid back to him until just before his dismissal. He stated that he trusted the respondent and expected that over the years he would, eventually, receive the money he was owed.
32. Mr P Shah and Mr V Shah both stated that all the payments and goods given were loans to fund the claimant's extravagant lifestyle. Mr P Shah said that he was a generous person and wanted to help the claimant out. The cash payments were, sometimes recorded as loans in the accounts. This was, according to Mr V Shah, on the advice of their accountant. Prior to them being recorded as loans it is not clear how they were classified in the accounts.
33. There was no evidence that any of these loans were ever repaid or requested to be repaid. There is no evidence that the claimant paid cost price or any price for many of the goods received and then sold on. The only explanation given for this was Mr P Shah's generosity.
34. I do not accept that as plausible. The value of the goods and payments made to the claimant over the years is many thousands of pounds. It was an ongoing situation and payments were made frequently though not with any regularity either in timing or value. These were not loans to tide over an employee in need. These were payments that were intended to compensate the claimant for the work he was doing albeit erratically. They were of a high value, they paid for important and valuable aspects of the claimant's life and he clearly relied upon them to an extent to incur costs and expenses he might not otherwise have incurred.
35. I accept the claimant's assertion that at the outset of his employment, he and Mr P Shah had agreed that he would be paid the equivalent of what he could earn as a consultant but that only part of that salary would be paid through the books and the PAYE system. I accept this because of the sheer volume and value of the payments (of all types) made and on the existence of the tally sent to Mr P Shah in 2015 which clearly records and echoes the claimant's understanding and representations to the tribunal as to how much he expected to be paid. The fact that this tally was not challenged by Mr Shah at the time demonstrates that there was a clear agreement between him and the claimant that the claimant was entitled to these monies at some point. This is enforced by the fact that at no point did the respondent ever try to get the 'loans' paid back.
36. However I do not accept the claimant's assertions that he did not know that tax and National Insurance payments were meant to be paid for these amounts. I do accept that he was not given payslips for many years so had no clear record of what tax and NI contributions were being made.
37. However I do not accept that he had understood that Mr P Shah was making all the necessary tax payments at source including his employee National Insurance contributions. This is simply not plausible given that he had previously worked as a self-employed contractor who was responsible for his own tax and NI contributions. He knew that part of the money he was being paid was being paid regularly and through the books and understood that the reason the rest of the

money was being paid differently and through different channels was to avoid tax. He also accepted that part of his payments were being made in ad hoc ways through goods and direct payments to pay off credit cards both for him and his partner as well as school fees for his child. It is not plausible that he thought that tax contributions were being made by the employer on his behalf for these ad hoc 'payments'. The claimant understood that these methods of paying him were financially advantageous to him and the respondent because they were not being taxed. No other explanation is plausible in the circumstances.

38. I find that he understood from the outset that the express and explicit intention behind the splitting of his payments between salary that was put through the PAYE system and other payments that were not - was to avoid tax and other deductions.
39. At the point at which the claimant became an employee, he was told by Mr P Shah that this was necessary because their company accountant had advised them to do this. I find that there was a clear awareness by both parties at that time that tax and NI contributions would impact on the claimant's income and the overheads or costs of the respondent. Both could lose out financially if the claimant had to be paid everything through the books. I conclude that it was for this precise reason that they agreed to split the payments so that the respondent's overheads would not increase and the claimant could continue to take home the net pay he had been able to earn as a self-employed person. Both agreed to the situation and both understood its purpose.
40. I find that the main purpose of the contract was for the claimant to be employed by the respondent. However I find that the contract was an illegal contract as the payments agreement was formed with the intention and purpose to avoid the relevant PAYE tax payments and deductions.
41. Given this conclusion it has not been necessary to find any further facts in relation to the events surrounding the claimant's dismissal.

The Law

42. Contracts can be illegal at common law if the contract is illegal in the way that it was performed. In the case of Newland v Simons and Willer (Hairdressers) Ltd 1981 IRLR 359 the EAT held that where both employer and employee knowingly commit an illegal act by way of a fraud on HMRC then the contract is prohibited by statute or common law.
43. Whether or not an employee can enforce the contract if part of its purpose is held to be unlawful is considered by the Court of Appeal in the case of Hall v Woolston Hall Leisure Ltd 2001 ICR 99. There the Court found that an employee may be prevented from enforcing a contract if they knowingly participate in the illegal performance. The question is whether a tribunal can consider an employee's collateral rights (e.g. a statutory redundancy payment or unfair dismissal damages) if they are relying upon an illegal contract. The Court of Appeal held that it was a question of fact and should be based on whether there was a sufficient degree of participation by the employee so as to render the entire contract unenforceable.

44. Where an employee has proposed unlawful tax arrangements the approach taken by the courts has been different. In the case of Salvesen v Simons 1994 ICR 409, EAT, it was held that where an employee has chosen to make payment arrangements which avoids paying money to HMRC, then the contracts set out those arrangements are unenforceable even if the employee genuinely believed them to be lawful.
45. The Supreme Court Judgment in Colen and Anor v Cebrian (UK) Limited [A1/2003/0379] also considered to what extent an employment contract tainted by illegality can be enforced. Lord Justice Waller, at paragraph 23 of that Judgment says as follows:

“If the contract was unlawful at its formation or if there was an intention to perform the contract unlawfully as at the date of the contract, then the contract will be unenforceable. If at the date of the contract the contract was perfectly lawful and it was intended to perform it lawfully, the effect of some act of illegal performance is not automatically to render the contract unenforceable. If the contract is ultimately performed illegally and the party seeking to enforce takes part in the illegality, that may render the contract unenforceable at his instigation. But not every act of illegality in performance even participated in by the enforcer, will have that effect. If the person seeking to enforce the contract has to rely on his illegal action in order to succeed then the court will not assist him. But if he does not have to do so, then in my view the question is whether the method of performance chosen and the degree of participation in that illegal performance is such as to ‘turn the contract into an illegal contract’.

.....

Of course much may depend on the question whether the party seeking to enforce the contract needs to rely on the illegal performance in order to succeed.”

Conclusions

46. It is not clear whether the claimant suggested the payment arrangements to ensure he took home £900 net a week or if Mr P Shah suggested the arrangement. I find it likely that Mr Shah told the claimant that he had to start paying him as an employee because that was what his accountant had told him
47. and that the claimant and he bargained somewhat to find an arrangement that ensured the claimant was paid what he viewed as fair wage in his pocket but that Mr Shah did not have to pay as much in taxes to guarantee that amount of money. It was clearly, by the nature and manner of the payments made, a relatively informal arrangement albeit one that was intended to compensate the claimant at some point for the work that he did at a higher rate than his basic wages through PAYE.
48. I think it is more likely that Mr P Shah suggested the arrangement on the basis that it was his accountant that advised him to change the method of payment and given the way in which payments were then made in an erratic and clearly not particularly financially fair way.
49. I conclude, that on balance, this contract was illegal from the outset as this payment arrangement was knowingly and willingly entered into by both parties in order to allow them both to avoid paying as much tax.

50. The claimant knowingly and willingly entered into the arrangement to ensure that he and the respondent did not have to pay tax or NI on the additional sums he received from Mr P Shah. Whilst I accept that he did not get sent payslips for much of his employment, he did not expect any of these sums to be reflected in the payslip hence his practice of recording the goods and payments made by the respondent to him in his spreadsheet. He kept a record because he knew that there was no other record of these payments as they were being made off the books. I do not accept that he thought that Mr P Shah was paying the tax, it is simply not plausible given his clear records and his knowledge of tax liabilities from when he had been self-employed and responsible for his own tax payments. Further it is not clear how he expected tax to be paid on payments made in the form of goods or direct payments to credit card companies or schools.
51. If I am wrong and this was a legal contract at the outset but by its performance became illegal then I must consider whether the claimant has to rely upon the illegal part of the contract (i.e. the payment arrangements) for his claim. The issue of what payments he is owed forms the majority of the value of the claimant's claim and goes to the heart of his case against the respondent.
52. The main thrust of the claim before me was the monies he said were owed to him as part of this unlawful arrangement both as a breach of contract and as an unlawful deduction from his wages.
53. I have to consider whether the claimant was actively involved with the arrangement and I conclude that he was. This is not a situation such as that in Hart v PG Bones Ltd (first instance ET) where the tribunal held that it was unconscionable for an employer to seek to deprive the employee of his right to enforce a contract when he had only been paid tax as a self-employed person at the employer's insistence. Instead this was a situation where the employee entered into an arrangement where he was partly paid through the books and partly paid in a way which he knew reduced any tax and National Insurance (including employee NI payments) payable and which he willingly participated and profited from for many years.
54. The contract was either an illegal contract or a contract tainted by illegality that the claimant knowingly and willingly participated in. He is therefore not entitled to rely upon it to bring any claim whether that be under contract law or statute and for this reason all the claimant's claims fail.
55. I note that Mr P Shah and the respondent also willingly and knowingly entered into this contract with the express intention of avoiding paying HMRC the relevant tax contributions. They have benefitted from the illegality because the contractual arrangement they entered into with the claimant cannot be enforced. I anticipate that HMRC may be interested in the findings I have made with regard to the lawfulness of all the parties' tax arrangements to date.

Employment Judge Webster

Date: 21 June 2019

