EMPLOYMENT TRIBUNALS

BETWEEN

Claimant		**Respondents**
Mr D Loader	AND	The Secretary of State for Business and Trade (1) Markline Construction Limited (In Administration) (2)

JUDGMENT OF THE EMPLOYMENT TRIBUNAL

HELD REMOTELY **ON** 24 May 2024
By CVP VIDEO

EMPLOYMENT JUDGE N J Roper

Representation
For the Claimant: **In person**
For the First Respondent: **Mr P Soni**
For the Second Respondent: **No Appearance Entered – Did Not Attend**

JUDGMENT

The judgment of the tribunal is that the claimant was not an employee of the second respondent company, and his application for payment by the first respondent from the National Insurance confirmed it is not well-founded and it is dismissed.

RESERVED REASONS

1. This is the judgment following a preliminary hearing to determine the employment status of the claimant. In this case the claimant Mr Darren Loader has brought a claim against the respondent, the Secretary of State, seeking payment from the National Insurance Fund. The respondent denies that the claimant was an employee and accordingly asserts that there is no liability to the claimant.
2. This has been a remote hearing which has been consented to by the parties. The form of remote hearing was by CVP Video. A face-to-face hearing was not held because it was not practicable, and all issues could be determined in a remote hearing. The documents to which I was referred are in a bundle provided by the parties, the contents of which I have recorded.
3. I have heard from the claimant, and I have heard from Mr Soni on behalf of the respondent. The primary facts were not in dispute. I found the following facts proven on the balance of probabilities after considering the whole of the evidence, both oral and documentary, and

after listening to the factual and legal submissions made by and on behalf of the respective parties.

4. The claimant Mr Darren Loader was a company director and shareholder in the second respondent company Markline Construction Limited. This was a family company, and the claimant was one of four directors and one of four equal shareholders who each held 25% of the shares. His work was effectively that of Finance Director with related duties.
5. The second respondent encountered financial difficulties and the directors decided to stop trading on 3 July 2023. The second respondent subsequently entered administration on 14 July 2023.
6. The claimant had signed a contract of employment with the second respondent, which was expressed to be a Director's Service Agreement. This was expressed to commence on 1 December 2016. In his originating application the claimant has recorded that his employment in fact commenced in November 2003. The Service Agreement contained the usual provisions to be found in the contract of employment, such as those relating to salary, holiday pay, sick pay, restrictive covenants and termination provisions. There was also a disciplinary procedure and a grievance procedure.
7. The salary payable under the Service Agreement was expressed to be £55,000 per annum, and the claimant worked a normal five-day week. However, the claimant did not receive that salary. The claimant's gross earnings which are recorded in his HMRC forms P60 were £14,765.96 to the year ending 31 March 2020; £9,999.96 to the year ending 2021, £9,999.96 to the year ending 2022, and £12,500 for the year ending 2023. As at the administration of the second respondent company, the claimant was subsequently paid £1,047.50 per month. This was the only salary paid by the second respondent company judging by its published accounts which recorded directors' salaries limited to £13,933 for the year ending 2021, and £10,000 for the year ending 2022. Meanwhile those accounts show that the claimant had drawn dividends of £41,753 to the year ending 2021; and £51,804 for the year ending 2022. The other directors had drawn similar dividend payments.
8. The claimant and his fellow directors choose to vary the payments they received from year to year depending upon the success or otherwise of the company, and according to what they and their accountants advised would be the most tax efficient way of drawing money from the company, whether as salary or dividends.
9. The claimant has also confirmed to the first respondent in his application for payment that he is not owed any money by the second respondent company.
10. The claimant was thus in a position to control how he received remuneration from the company. According to the claimant's HMRC forms P60 which he has disclosed, he did not pay any income tax as a PAYE employee. The first respondent asserts that the claimant has benefited from choosing to take the "optimum director's salary" or a threshold near it in order to take advantage of the most tax efficient way for a director to pay himself. This is not a benefit which is afforded to a bone fide employee who would not have that privilege. In addition the remuneration received by way of this limited salary was well below the National Minimum Wage level for the hours which the claimant worked.
11. Following the administration of the second respondent company the claimant applied to the first respondent Secretary of State for payment of his notice pay and statutory redundancy pay from the National Insurance Fund. That claim has been rejected.
12. The first respondent confirmed its reasons for rejecting the claimant's claim by email dated 4 August 2023. This recorded: "A key factor we consider is whether a director remunerated themselves as an employee or an officeholder. As per the National Minimum Wage Act 1998, a director must pay themselves the National Minimum Wage (NMW) if they are an employee. However, a director is exempt from the NMW if they choose to be remunerated as an officeholder and not class themselves as an employee or worker. The evidence you provided indicated you were not paid at NMW. As a director and shareholder of the company you were in a position to control in what form funds were received from the company."

13. The claimant then obtained an ACAS Early Conciliation certificate on 4 August 2023, and he presented his proceedings on 8 August 2023. The first respondent has defended the claim. The second respondent has not entered a response.
14. Having established the above facts, I now apply the law.
15. The relevant legislation is the Employment Rights Act 1996 ("the Act").
16. Under s166(1) of the Act - Where an employee claims that his employer is liable to pay to him an employer's payment and either— (a) that the employee has taken all reasonable steps, other than legal proceedings, to recover the payment from the employer and the employer has refused or failed to pay it, or has paid part of it and has refused or failed to pay the balance, or (b)that the employer is insolvent and the whole or part of the payment remains unpaid, the employee may apply to the Secretary of State for a payment under this section. S 166(2) - In this Part "employer's payment", in relation to an employee, means— (a) a redundancy payment which his employer is liable to pay to him under this Part, (aa) a payment which his employer is liable to make to him under an agreement to refrain from instituting or continuing proceedings for a contravention or alleged contravention of section 135 which has effect by virtue of section 203(2)(e) or (f), or (b) a payment which his employer is, under an agreement in respect of which an order is in force under section 157, liable to make to him on the termination of his contract of employment.
17. Under section 182(1) of the Act, on an application made to him in writing by an employee, the Secretary of State is satisfied that — (a) the employee's employer has become insolvent, (b) the employee's employment has been terminated, and (c) on the appropriate date the employee was entitled to be paid the whole or part of any debt to which this Part applies, the Secretary of State shall, subject to section 186, pay the employee out of the National Insurance Fund the amount to which, in the opinion of the Secretary of State, the employee is entitled in respect of the debt
18. Section 184 of the ERA applies section 182 to arrears of pay; accrued holiday pay and statutory notice pay (but subject to maximum amounts).
19. For the Secretary of State to be liable, any such claimant must have been an employee.
20. Employees are defined in section 230 of the Act. An employee is an individual who has entered into or works under (or, where the employment has ceased, worked under) a contract of employment. A contract of employment is defined as a contract of service or apprenticeship, whether express or implied, and (if it is express) whether oral or in writing.
21. I have considered the following cases to which I have been referred: Autoclenz Ltd v Belcher and Others [2010] IRLR 70 CA and [2011] UKSC 41; Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance [1968] 2 QB 497; Aslam Farrar & Others v Uber BV and Others 2202550/2015; Nethermere (St Neots) Limited v Gardiner [1984] ICR 612; Express and Echo Publications Ltd v Tanton [1999] IRLR 367. Consistent Group Ltd v Kalwak [2008] IRLR 505 CA; Firthglow Ltd (t/a Protectacoat) v Szilagyi [2009] ICR 835 CA; Ter-Berg v Simply Smile Manor House Ltd and Ors EAT [2023] 2; Buchan-v-Secretary of State for Employment [1997] IRLR 80 EAT; Neufeld v Secretary of State for Business Enterprise and Regulatory Reform [2009] IRLR 475 CA; Eaton v Robert Eaton Ltd and Secretary of State for Employment [1988] IRLR 83; Fleming v Secretary of State for Trade and Industry [1997] IRLR 682 CS; Rainford v Dorset Aquatics Ltd UKEAT/0126/20/BA; Secretary of State for Trade and Industry-v-Bottrill [1999] ICR 592, CA; Clark-v-Clark Construction Initiatives Ltd [2008] ICR 635, EAT; Rajah v Secretary of State for Employment EAT/125/95.
22. As confirmed in paragraphs 18 and 19 of Lord Clarke's judgment in Autoclenz in the Supreme Court: "18 : As Smith LJ explained in the Court of Appeal of paragraph 11, the classic description of a contract of employment (or a contract of service as it used to be called) is found in the judgement of McKenna J in Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance [1968] 2 QB 497, 515C : "a contract of service exists if these three conditions are fulfilled: (i) the servant agrees that, in consideration of a wage or other remuneration, he will provide his own work and skill in the performance of some service for his master. (ii) He agrees, expressly or impliedly, that in the performance of that service he will be subject to the other's control in a sufficient degree to make that other master. (iii) The other provisions of the contract are consistent with its

being a contract of service … Freedom to do a job either by one's own hands or by another's is inconsistent with a contract of service, though a limited or occasional power of delegation may not be". 19: Three further propositions are not I think contentious: i) As Stephenson LJ put it in Nethermere St Neots Ltd v Gardiner [1984] ICR 612, 623 "There must … be an irreducible minimum of obligation on each side to create a contract of service". ii) If a genuine right of substitution exists, this negates an obligation to perform work personally and is inconsistent with employee status: Express and Echo Publications Ltd v Tanton ("Tanton") [1999] ICR 693 per Peter Gibson LJ at p 699G. iii) If a contractual right, as for example a right to substitute, exists, it does not matter that it is not used. It does not follow from the fact that a term is not enforced that such a term is not part of the agreement: see eg Tanton at page 697G."

23. The Supreme Court has upheld the Court of Appeal in the Autoclenz decision, and the approach to be adopted where there is a dispute (as in this case) as to an individual's status. In short, the four questions to be asked are: first, what are the terms of the contract between the individual and the other party? Secondly, is the individual contractually obliged to carry out work or perform services himself (that is to say personally)? Thirdly, if the individual is required to carry out work or perform services himself, is this work done for the other party in the capacity of client or customer? And fourthly if the individual is required to carry out work or perform services himself, and does not do so for the other party in the capacity of client or customer, is the claimant a "limb (b) worker" or an employee?
24. In Autoclenz the Supreme Court has also discussed the cases where the written documentation may not reflect the true reality of the relationship. These include Kalwak and Szilagyi, and the Court of Appeal decision in Aurtoclenz. In paragraph 29 Lord Clarke preferred the approach of Elias J (as he then was) in Kalwak, and the Court of Appeal in Szilagyi, to that of the Court of Appeal in Kalwak. The question to be asked is what was the true agreement between the parties? It is important to look at the reality of the obligations and the reality of the situation. He referred in paragraph 30 to the judgment of Smith LJ in paragraph 50 of Szilagyi: "The kernel of all these dicta is that the court or tribunal has to consider whether or not the words of the written contract represent the true intentions or expectations of the parties, not only at the inception of the contract but, if appropriate, as time goes by". In paragraph 35 he concluded "so the relative bargaining power of the parties must be taken into account in deciding whether the terms of any written agreement in truth represent what was agreed and the true agreement will often have to be gleaned from all the circumstances of the case, of which the written agreement is only a part. This may be described as a purposive approach to the problem. If so, I am content with that description".
25. See Ter-Berg v Simply Smile Manor House Ltd and Ors for the correct approach to determining employment status following Uber BV v Aslam - the EAT held that the Supreme Court's decision in Uber did not displace or materially modify the Autoclenz approach. The reference in Uber to it being wrong to treat the contract as a starting point formed part of the theoretical underpinning for that approach. It did not mean that the written terms are, in every case, irrelevant, or could never accurately convey the true agreement of the parties. The EAT went on to hold that an employment tribunal did not err when it treated the written terms on which a dentist was engaged to work at a dental practice as the starting point in determining whether he was its "employee". The tribunal had looked beyond the written terms of the agreement and had considered the wider circumstances of the relationship between the parties as required by Autoclenz and Uber.
26. The position of shareholders and/or directors has been considered in a number of cases. The traditional view, which has been reinforced more recently, was that controlling shareholders were not under the control of the employer because they could block any attempt to dismiss. A director's level of control over the business undertaking generally led to a similar conclusion (see Buchan-v-Secretary of State in which the Claimant was the managing director and a 50% shareholder, but he was not deemed to have been an employee).
27. In Neufeld v Secretary of State for Business Enterprise and Regulatory Reform, the Court of Appeal held that there was no reason in principle why someone who is a shareholder

and director of company cannot also be an employee under a contract of employment, not that by virtue of the shareholding giving them control of it that they cannot be an employee. It was held:

a. Whether or not a shareholder/director is an employee is a question of fact. There are in theory two issues: whether the putative contract is genuine or a sham and secondly, where genuine, that it is a contract of employment (para 81);
b. In cases involving a sham, the task is to decide whether such document amounts to a sham. This will usually require not just an investigation into the circumstances of the creation of the document, but also the parties purported conduct under it. The fact that the putative employee has control over the company and the board, and was instrumental in the creation of it will be a relevant matter in the consideration of whether or not it was a sham (para 82);
c. An inquiry into what the parties have done under the purported contract may show a variety of things: (i) that they did not act in accordance with the purported contract at all, which would support the conclusion that it was a sham; or (ii) that they did act in accordance with it, which will support the opposite conclusion; or (iii) that although they acted in a way consistent with a genuine service contract arrangement, what they have done suggests the making of a variation of the terms of the original purported contract; or (iv) that there came a point when the parties ceased to conduct themselves in a way consistent with the purported contract or any variation of it, which may invite the conclusion that, although the contract was originally a genuine one, it has been impliedly discharged. There may obviously also be different outcomes of any investigation into how the parties have conducted themselves under the purported contract. It will be a question of fact as to what conclusions are to be drawn from such investigation (para 83);
d. In deciding whether a valid contract of employment was in existence, consideration will have to be given to the requisite conditions for the creation of such a contract and the court or tribunal will want to be satisfied that the contract meets them. In *Lee*'s case the position was ostensibly clear on the documents, with the only contentious issue being in relation to the control condition of a contract of employment. In some cases, there will be a formal service agreement. Failing that, there may be a minute of a board meeting or a memorandum dealing with the matter. But in many cases involving small companies, with their control being in the hands of perhaps just one or two director/shareholders, the handling of such matters may have been dealt with informally and it may be a difficult question as to whether or not the correct inference from the facts is that the putative employee was, as claimed, truly an employee. In particular, a director of a company is the holder of an office and will not, merely by virtue of such office, be an employee: the putative employee will have to prove more than his appointment as a director. It will be relevant to consider how he has been paid. Has he been paid a salary, which points towards employment? Or merely by way of director's fees, which points away from it? In considering what the putative employee was actually *doing,* it will also be relevant to consider whether he was acting merely in his capacity as a director of the company; or whether he was acting as an employee. (para 85);
e. We have referred in the previous paragraph to matters which will typically be directly relevant to the inquiry whether or not (there being no question of a sham) the claimed contract amounts to a contract of employment. What we have *not* included as a relevant consideration for the purposes of that inquiry is the fact that the putative employee's shareholding in the company gave him control of the company, even total control. The fact of his control will obviously form a part of the backdrop against which the assessment will be made of what has been done under the putative written or oral employment contract that is being asserted. But it will not ordinarily be of any special relevance in deciding whether or not he has a valid such contract. Nor will the fact that he will have share capital invested in the company; or that he may have made loans to it; or that he has personally

> guaranteed its obligations; or that his personal investment in the company will stand to prosper in line with the company's prosperity; or that he has done any of the other things that the 'owner' of a business will commonly do on its behalf. These considerations are usual features of the sort of companies giving rise to the type of issue with which these appeals are concerned but they will ordinarily be irrelevant to whether or not a valid contract of employment has been created and so they can and should be ignored. They show an 'owner' acting qua 'owner', which is inevitable in such a company. However, they do not show that the 'owner' cannot also be an employee (para 86).

28. In Eaton v Robert Eaton Ltd and Secretary of State for Employment, it was ruled that normally a director of a company is normally a holder of an office and not an employee. Evidence is therefore required to establish that the director was in fact employed.
29. In Fleming v Secretary of State for Trade and Industry, the Court of Session held that whether or not a person is an employee is a question of fact. The fact that a person is a majority shareholder is always a relevant factor and may be decisive. However the significance of the factor will depend on the circumstances and it would not be proper to lay down any hard and fast rule. In that case the Claimant was not found to have been an employee because, amongst other things, he had personally guaranteed loans, had no written contract and had decided not to draw a salary in the hope of saving the business).
30. In Rainford v Dorset Aquatics Ltd, it was further said that: “Although there was no reason in principle why a director/shareholder of a company could not also be an employee or worker, it did not necessarily follow that simply because he did work for the company and received money from it he had to be one of the three categories of individual identified in s. 230 (3) of the Act. Overall, the tribunal's conclusion that the appellant was not an employee or worker was one of fact based on relevant factors and was not perverse.” That was a case involving a claimant who had been a director and a 40% shareholder who was found to have been neither an employee nor a worker. The Claimant had drawn a ‘salary’ which was subject to PAYE and NI deductions, on the advice of the company accountants.
31. In Secretary of State for Trade and Industry-v-Bottrill, (as applied in Sellars Arenascene Ltd-v-Connolly [2001] ICR 760, CA) Lord Woolf MR suggested that Tribunal’s should consider the following questions:
    (a) Was there a genuine contract between the business and the shareholder? One which was not a sham?;
    (b) If so, did the contract actually create an employment relationship? Of the various factors which had to be considered, the degree of control is important. It was not just a case of looking at who had the controlling shareholding. A Tribunal had to consider where the real control lay; what role did any other directors/shareholders actually take?
32. In Rajah v Secretary of State for Employment, it was held that the relevant date for the purposes of who the secretary of state is liable to make payments out of the National Insurance fund is the date when the company became insolvent, and not the position it was two, five or ten years previously.
33. Against this background my conclusion is as follows.
34. In the first place it is clear that the fact that the claimant was a director and shareholder does not preclude him from also being an employee. However, the claimant’s Service Agreement no longer had contractual effect for at least the three years running up to the second respondent company’s administration. To that extent it was a sham. The claimant was not paid the salary which was ostensibly due under that agreement, and he has confirmed he is not owed any money by the second respondent company. The claimant and his fellow directors choose to vary the payments they received from year to year depending upon the success or otherwise of the company, and according to what they and their accountants advised would be the most tax efficient way of drawing money from the company, whether as salary or dividends. The claimant was clearly in a position which enabled him to control what payments he received and when.
35. In addition, I agree with the first respondent’s assertion that the claimant chose not to have the relationship treated as one of a genuine employee, simply by dint of the fact that his chosen salary fell short of the National Minimum Wage. There is a legal requirement for

employers to pay all employees at least the NMW. If the claimant had chosen to be treated in this way the salary which would then fall due would have been subject to tax and National Insurance, whereas the sums which the claimant chose to receive did not necessarily meet those thresholds.

36. In conclusion I find that there was no genuine employment relationship in place at the time the second respondent entered administration, which is the relevant time when the first respondent is potentially liable for payment. Accordingly, the claimant's claim to the effect that the first respondent has wrongly refused to make the necessary payments from the National Insurance Fund is not well-founded and it is hereby dismissed.

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Employment Judge N J Roper
Dated 24 May 2024

Judgment sent to Parties on
18th June 2024

For the Employment Tribunal