UK: Employment Update

Welcome to the June edition of Employment Update. This month we consider the implications of the Supreme Court's decision that LLP Partners are workers for the purposes of whistleblowing legislation protection and the wider ramifications of the ECJ decision that commission payments should be factored into holiday pay calculations.

Workers: LLP Partners are entitled to Whistleblowing protection

A worker has the right not to be subjected to any detriment by his employer on the grounds that he/she has made a protected disclosure (i.e. blown the whistle). A worker who succeeds with such a claim is entitled to be awarded compensation for any financial loss and, in addition, may recover compensation for injury to feelings. There is no cap on the amount that may be awarded. Detrimental treatment for these purposes can include termination of the working relationship. A worker is therefore better protected than an employee who is dismissed because they have made a protected disclosure as the employee is only entitled to financial loss compensation and not injury to feelings compensation.

Key issues

- Workers: LLP Partners are entitled to Whistleblowing protection
- Holiday Pay should reflect commission payments

The Supreme Court has ruled on whether an equity partner ("W") in a limited liability partnership ("LLP") is a "worker" for the purposes of bringing a whistleblowing detrimental treatment claim.

Under the terms of the LLP agreement between W and C & C LLP, W was required to devote her full time and attention to C&C's business. W also had an employment contract with a Tanzanian law firm, as such a contract was necessary to permit her to work in Tanzania. W reported to C & C that the managing partner of the Tanzanian firm had admitted to paying bribes in order to secure work and the outcome of cases. Shortly afterwards she was dismissed by the Tanzanian law firm and then expelled from the C & C Partnership. W claimed that her expulsion was a detriment on the grounds that she had made a protected disclosure.

The legislation defines a "worker" as someone employed under a contract where the individual undertakes to do or perform personally any work or services for the other party to the contract provided the other party is not a client or customer of any profession or business undertaking carried on by the individual.

The question of whether W was a worker was clearly not straightforward; the Employment Tribunal and the Court of Appeal considered that she was not, by contrast the Employment Appeal Tribunal and the Supreme Court considered that W was a worker.

The Supreme Court held that W was a 'worker' as she was not a professional or business undertaking specifically marketing her services as an independent person to the world in general as the LLP agreement prevented her from offering her professional services to anyone but C & C. W's work was, rather, an integral part of the C & C operation and they were in no sense her client or customer. Accordingly W was a worker for the purposes of pursuing a whistleblowing detriment claim.

The Supreme Court was clear that there was no 'magic' test that could be applied to all cases to assess whether an individual was a worker; instead in each case the wording of the statute had to be applied to the specific facts. It held that whilst subordination might sometimes be an aid to distinguishing workers from other self employed people it is not a freestanding and universal characteristic of being a worker.

The court considered it's conclusion that W was a worker entitled to the protection of the whistleblowing legislation was entirely consistent with the underlying policy of the legislation, which could be regarded as being particularly applicable to businesses and professions operating in the financial and legal services sectors.

Practical implications

- It is now clear that LLP members, regardless of the sector in which they operate, have the right not to be subjected to a detriment for whistleblowing.
- Detrimental treatment may cover a wide range of actions but could for example cover: expulsion from the LLP, enforced retirement, a reduction in drawings or profit share or a call on capital.
- In order to succeed with a whistleblowing detriment claim before an Employment Tribunal it has to be satisfied that the protected disclosure did not materially influence the 'employer's' detrimental treatment. To the extent practicable, LLP's should try and ensure that there is a clear document trail evidencing the reasons behind any particular course of action that might be viewed as detrimental.
- LLP's should consider extending any existing whistleblowing procedure to its members or creating a specific procedure for it's members.

Wider implications

'Workers' are also afforded a number of additional statutory employment rights: the right to paid leave; the right to receive the national minimum wage and the right not to suffer from unauthorised deductions from wages. In practice compliance with the statutory national minimum wage and holiday requirements is unlikely to be problematic for an LLP.

Workers are in many cases 'jobholders' for the purposes of pension auto-enrolment. However, whether or not LLP's are subject to auto enrolment obligations in relation to their partners is not entirely clear and further guidance may be forthcoming from the Pensions Regulator.

In the event that the auto enrolment regime does apply to LLP's in cases where the LLP does not currently have any employees, and therefore has no PAYE registration number, the staging date for auto enrolment will be 1 April 2017.

In any event, if an LLP is subject to auto enrolment and only the minimum statutory obligation is complied with then the sums involved are unlikely to be significant on an individual entitlement basis.

Does this decision have other implications? For example, does it mean that a non executive director (NED) might be regarded as a 'worker' for whistleblowing protection purposes? A non executive director is certainly providing his services personally. Is the company on whose board the NED sits a customer or client of a profession or undertaking carried on by the NED? That must be questionable? Perhaps less so if the NED holds a number of non executive positions and provides his services via a service company. Where, however, the NED is engaged under an agreement or other contract and has no other NED appointments, there must be a risk that he could be classified as a worker.

[Bates van Winkelhof v Clyde & Co LLP]

Holiday Pay should reflect commission payments

Employers are facing potentially substantial bills for miscalculated holiday pay, following a recent decision of the European Court of Justice....

The right to be paid annual leave is derived from the Working Time Directive (the Directive); however the Directive does not specify how holiday pay should be calculated. The method of calculating holiday pay has been left up to Member States; in the UK the Working Time Regulations cross refer to the Employment Rights Act 1996 (ERA) which sets out various formulae for calculating a week's pay depending on whether the employee has normal working hours or their pay varies according to the time or volume of work.

Until recently, the way in which these formulae have been judicially interpreted has resulted in elements of actual remuneration such as commission and overtime payments being excluded from holiday pay calculations; the one exception is where the overtime is compulsory and guaranteed.

As reported previously there has been increasing doubt about whether the UK approach to calculating holiday pay is in accordance with the Directive. The European Court of Justice (ECJ) has now clarified what elements of remuneration should be taken into account when calculating holiday pay with potentially significant implications for some employers who operate commission and other incentive schemes and those who make overtime payments.

Background

Mr Lock's (L) remuneration consisted of basic pay and commission (the levels of which varied), both of which were paid monthly. L's commission accounted for approximately 60% of his remuneration. L brought a claim for holiday pay on the

basis that during his period of holiday he was not in a position to earn commission and accordingly his average commission earnings over the course of the year would be lower than they would have been had he not taken holiday.

Holiday pay calculation must not deter workers from taking holiday

The ECJ reaffirmed that workers must receive their normal remuneration for periods of annual leave as the purpose of paying annual leave is to put the worker in a position as regards to his or her salary comparable to their periods of work. The way in which holiday pay is calculated must not deter a worker from taking holiday so that the health and safety objective of the Directive is achieved.

The ECJ held that L may be deterred from exercising his right to paid annual leave if his holiday pay did not include commission because of the deferred financial disadvantage he would suffer following a period of annual leave during which he had not been able to earn commission. The fact that the reduction in remuneration occurs after the period of annual leave was irrelevant.

What aspects of remuneration should feature in a holiday pay calculation?

The ECJ explored what components of remuneration are to be classified as normal remuneration and therefore should be factored into a holiday pay calculation. It held that the following components should be included in the holiday pay calculation:

- any aspect of remuneration that is linked intrinsically to the performance of the work that the worker is required to carry out under the employment contract; and
- any components that relate to professional and personal status e.g. any allowances relating to seniority, length of service and professional qualifications.

The ECJ clarified that components of remuneration which are intended exclusively to cover occasional or auxiliary costs arising at the time of performance need not be factored into the holiday pay calculation.

The ECJ held that as L's commission was intrinsically linked to the performance of the tasks he was required to carry out under his employment contract, it should be taken into account in calculating his total remuneration in respect of his annual leave.

And back to the English courts

The case will now go back to the English courts to assess what method should be adopted to calculate the commission payable to L in respect of his annual leave.

It remains to be seen what approach will be adopted. In Lock the Advocate General considered that an average commission of a representative period would be appropriate and suggested a 12 month period. The English Tribunals may consider that a different period is more appropriate, perhaps the ERA 12 week reference period that is currently used when calculating a week's pay?

Overtime payments

The Employment Appeal Tribunal (EAT) is expected to hear two cases in July that will explore whether overtime, incentive and bonus payments should also be factored into holiday pay calculations in respect of the basic 4 week holiday entitlement on the basis that they form part of the employees' normal remuneration linked intrinsically to the work they are required to perform under their contracts.

The Employment Tribunal in both cases held that such payments should have been included in holiday pay calculations and the failure to include such payments amounted to an unlawful deduction of wages. In light of the ECJ's decision in Lock there must be a very strong prospect of the EAT upholding this finding.

What is the risk of latent wages claims in relation to unpaid holiday?

Claims for unpaid holiday pay may be pursued as unlawful deduction from wages claims in the Employment Tribunal. Such claims must be brought within three months of the deduction, or last in a series of deductions, with no limitation on how far back the series of deductions go.

If the English courts consider that it is possible to interpret our domestic legislation to give effect to requirements of the Directive, in principle some employers could face wages claims in relation to underpayment of holiday pay going back to the later of: the start of an employee's employment or the commencement of the Working Time Regulations (1 October 1998).

In practice, however, it may be difficult in some cases to establish a claim (at least over a extended period) in the absence of adequate record keeping on the part of employer and employee alike on what overtime and commission payments have been made and when holiday was taken.

It has been suggested that one way of limiting the scope of significant wages claims going back many years is to ensure that the next holiday payment includes elements referable to commission, overtime, or other personal allowances (as appropriate in the circumstances) in order to break the 'chain' of deductions. This would only be effective if the holiday pay calculation is correct and until such time as judicial or legislative guidance is provided there must be a risk that the calculation is incorrect because the wrong averaging period has been used.

Problem areas

It would appear that it is only pay in relation to the minimum 4 week holiday entitlement guaranteed by the Directive that must be calculated by reference to the ECJ's 'expanded' concept of normal remuneration that includes commission (and almost certainly overtime pay), but not the additional 1.6 week "gold plated" English holiday entitlement. This could lead to a two tier approach to holiday pay calculations and possible arguments about whether a particular period of holiday is basic holiday or 'gold plated holiday'.

If commission or overtime rates vary over the course of a year, how should an employer calculate what the normal rate of remuneration is for the purposes of paying holiday pay? Similarly, for a new employee, what should the holiday pay reference period be? It is to be hoped that some judicial guidance will be provided shortly on this issue.

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What should employers be doing?

At this stage employers do not need to alter their method for calculating holiday pay entitlement until English judicial clarification is provided on: (i) whether commission, overtime and personal bonus payments do need to be factored into holiday pay; and if so (ii) the reference period for carrying out any averaging calculations.

It would however be prudent to anticipate that certain commission, personal allowances and overtime payments are likely to have to be included in holiday pay going forward and also to make appropriate contingency plans both in this regard and in relation to the possibility of wages claims for back dated holiday pay.

[Lock v British Gas Trading Ltd & Ors]