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Briefing Note – November 2018

UK: EMPLOYMENT UPDATE

This month we explore some key court decisions addressing whether a company is vicariously liable for the criminal acts of an employee in relation to the theft and publication of workforce personal data and whether non-executive directors can be pursued personally for a decision to dismiss a whistleblower in addition to the employer being liable for the dismissal. This briefing also rounds up some aspects of the Budget that employers should be aware of and start planning for.

Key issues

- Employer's vicarious liability for data protection breach by rogue employee
- Personal liability of non-executive directors who dismissed whistleblower
- Tax treatment of termination payments: employer's NIC liability delayed another year
- IR35 rule reforms will be extended to the private sector

Employer's vicarious liability for data protection breach by rogue employee

The Court of Appeal has upheld a decision that Morrisons (M) is vicariously liable for the criminal misuse of its payroll data by a (now former and imprisoned) rogue employee (S). A class action was brought against M by 5,500 current and former employees whose payroll data (including bank, salary and d.o.b.) was leaked online for less than 24 hrs by S, who was a senior auditor at the time.

The Court revisited the test for vicarious liability at common law established by the Supreme Court which focuses on: (i) what functions or "field of activities" have been entrusted by M as employer to the employee, S, (or, in everyday language, what was the nature of S' job); and (ii) whether there was sufficient connection between the position in which he was employed and his wrongful conduct to make it right for M, the employer to be held liable under the principle of social justice.

M argued that the online disclosure was the act that caused the harm, and this was not done in the course of S' employment; the data had been sent from his personal computer at home on a Sunday several weeks after he had downloaded the information at work onto a personal UBS stick in contravention of M's policies and procedures. In addition, M argued that S was disgruntled with it following an internal disciplinary process, his acts were motivated by the intention to cause harm to M and therefore to find M vicariously liable would render the court an accessory to S's criminal conduct.

The Court of Appeal was, however, of the view that S was acting in the course of his employment when he criminally disclosed the data online. As a senior auditor, sending the data to third parties was within the field of activities assigned to him by M. It observed that the time and place at which the act(s) occurred will always be relevant, though not conclusive, but that there are numerous cases in which employers have been held vicariously liable for torts committed away from the workplace; a very recent example being *Bellman v Northampton Recruitment Ltd*, in which an employer was found vicariously liable for the physical assault carried out by its managing director on an employee at an office Christmas party after party.

The Court's view was that S' position involved the handling and disclosure of the data (albeit it was meant to be to M's auditors); accordingly there was sufficient connection between his job and the data leak to make it right for M to be held vicariously liable.

The Court also rejected M's argument that vicarious liability should not arise as S' motive was to harm M rather than to achieve some benefit for himself or to inflict injury on a third party.

M also argued, unsuccessfully, that as there were 5,518 claimants, and the total number of employees whose confidential information was wrongly made public by S was nearly 100,000, a finding of vicarious liability would impose an enormous burden on M and could place a similarly enormous burden on other innocent employers in future cases. The Court of Appeal's answer to this Doomsday argument was 'insurance': employers can take out insurance against (potentially ruinous) losses caused by dishonest or malicious employees but the presence or absence of any such insurance should not be a relevant factor when assessing vicarious liability.

The level of compensation that M is liable to pay to the claimants has yet to be determined although the Court of Appeal did observe that as far as it was aware none of the claimants had suffered any financial loss. From M's perspective this decision certainly seems to be very harsh as it was not found to be in breach of the, then applicable, Data Protection Act 1998 (bar in one very minor respect) nor was it criticised for the way in which it had managed S; he simply went rogue with the specific intention of inflicting as much harm as he could on M which the court's decision has compounded. It is understood that M is likely to appeal to the Supreme Court.

It remains to be seen whether the Supreme Court will uphold this decision. In the meantime, employers may wish to consider what insurance options are available to them to address the scenario of a deliberate and pernicious leak of data whether relating to staff or clients.

[WM Morrison Ltd v various Claimants]

Personal liability of non-executive directors who dismissed whistleblower

An employee who makes a protected disclosure (blows the whistle) is entitled not to be subjected to a detriment by his employer, another worker of the employer or an agent of the employer on the grounds that he has blown the whistle. In addition, if the reason (or principal reason) for an employee's dismissal is that they made a protected disclosure, the dismissal is treated as automatically unfair.

The legislation provides that if a co-worker subjects an employee to a detriment they may be personally liable for any compensation awarded by the Employment Tribunal. There is no cap on the amount of compensation that can be awarded. In most cases, a claimant is likely to pursue the deepest pocket; i.e. the employer, however, a recent decision of the Court of Appeal illustrates that individual personal liability can be expensive in a case where two non-executives of the employing entity were held to be liable for just over £2 million.

C was employed as CEO by IPL. T and S were non-executive directors of IPL. C made a number of protected disclosures and three days after the final disclosure, C was summarily dismissed in an email from S. The evidence before the Tribunal demonstrated that T had instructed S to dismiss C. Both S and T considered that C's disclosures rendered him "a costly obstacle that needed to be dismissed".

The Court of Appeal has now upheld the decision that T's instruction to S to dismiss C, and S's implementation of it, were actionable detriments on the part of both S and T. As S shared T's view that C should be dismissed, he was not merely acting as T's messenger. The Court rejected the argument that S was no more than a

"mouthpiece"; observing that it is not uncommon for more than one person to be party to a decision to dismiss. Indeed, it had been a board decision (both T and S being directors of IPL). In such a case one individual may take the leading role, but that does not mean that the other participants are not also responsible for the act in question.

Accordingly, S and T were jointly and severally liable for the compensation awarded in respect of the financial loss flowing from C's dismissal. The fact that C could also pursue an unfair dismissal claim against IPL did not relieve S and T of their liability.

In most cases pursuing an individual employee/worker will usually be less attractive financially than pursuing the employer. Of course, there may be tactical advantages; for example in a case where the employer is regulated by the FCA and/or PRA and pursuing a successful whistleblowing detriment claim against an individual who is a senior manager or certified person may have implications on the employer's ability to continue to certify them as fit and proper.

A detriment claim also has the advantage that compensation for injury to feelings can be awarded which it cannot for a whistleblowing unfair dismissal claim against the employer. In this case the employer was insolvent, and the two individuals, S and T, apparently had deep pockets so a personal claim was an obvious choice.

[Timis and Sage v Osipov]

Tax treatment of termination payments: employer's NIC liability delayed another year

Changes were introduced to the tax and national insurance contribution (NIC) treatment of termination payments with effect from 6 April 2018. In broad terms the changes required payments made in connection with termination that are not otherwise chargeable to tax to be split into: (i) termination payments benefitting from an exemption to tax for the first £30,000 (Termination Payments); and (ii) post-employment notice pay that is liable to be taxed as earnings (PENP payments).

Termination Payments are not currently subject to either employee or employer NIC's; however, as part of its tax reforms the Government has always intended that legislative changes will result in employer's NIC's applying to Termination Payments to the extent they exceed £30,000. The recent Budget has delayed the introduction of this by a further year; it will now take effect from 6 April 2020.

As PENP payments are taxable as earnings both employer and employee NICs are payable on such payments; as they are on payments in lieu of notice paid pursuant to an express contractual PILON clause, or, where there is no PILON clause, but the employer has an established practice of making auto PILON payments (in each case the payment being treated as earnings from employment).

IR35 rule reforms will be extended to the private sector

In May 2018, HM Treasury launched a consultation aimed at increasing compliance with the IR35 legislation governing off-payroll working in the private sector. Under the IR35 regime, in broad terms, where an individual supplies their services via an intermediary (often a personal services company (PSC)) the intermediary must determine whether the individual should be regarded as employed or self-employed but for the intermediary in the relationship between the individual and end user of the services. In circumstances where it would be an employment relationship then the intermediary is under an obligation to deduct and account for appropriate tax and NIC's. If they fail to do so there is currently no liability for the private sector end user.

HMRC believe that non-compliance with the IR35 regime is very high; accordingly the IR35 regime for public sector end users has already been amended so that the end

user is now under an obligation to assess whether the IR35 rules apply (i.e. whether the individual would be its employee but for the (PSC) intermediary), and, if they conclude that the rules apply they must then deduct tax and employee NIC's from the fee (less permissible expenses) and also pay employer NIC's. A penalty regime applies where there is a failure to operate the IR35 rules.

In the recent Budget the Government announced (unsurprisingly) that it is going to roll out the public sector IR35 rules to the private sector. Specific details are not yet known as the Government proposes to carry out a further consultation on the detailed operation of the new rules. No specific timeframe has been established, only that it will be published "in the coming months" and that the new rules will come into effect on 6 April 2020.

The Budget statement indicated that the new IR35 regime will only apply to medium and large businesses; it is believed that it is the intention to use similar criteria to define small businesses as those found in the Companies Act 2006. It was also made clear that the change to the IR35 rules will not be retrospective and that an HMRC enquiry will not be automatically triggered by payments under the new regime where the intermediary may not have been operating the IR35 rules prior to April 2020 in respect of the same arrangement; although it is likely that HMRC may wish to scrutinise whether the intermediary was in breach.

In preparation for the new IR35 regime companies would be advised to:

- audit their existing use of PSC and other intermediary arrangements;
- assess what the employment status of the individual being supplied is likely to be using the HMRC Check Employment Status for Tax (CEST) service and/ or legal advisers where any such arrangements (or similar arrangements) will continue beyond April 2020;
- take the opportunity to provide input to HMRC to help it improve and refine CEST. (Anecdotally is understood to be an unhelpful resource where the factual matrix is not straightforward. Given the plethora of case law and varying judicial approaches adopted in relation to the question of employment status it is unsurprising that there is no straightforward (and reliable) tool to determine employment status.);
- give thought to whether the contractual terms of such arrangements need to be amended in any way;
- anticipate some intermediaries/individuals pushing for higher fees.

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