



THE EMPLOYMENT TRIBUNAL

Claimants: (1) Mr Geoff Shaw
(2) Mrs Marie Shaw

Respondent: Active Products (UK) Limited

Held at: East London Hearing Centre (By video)

On: 8 February 2022

Before: Employment Judge Siddall

Representation

For the Claimants: In person
For the Respondent: Ms S Palmer

JUDGMENT ON PRELIMINARY HEARING

The decision of the tribunal is that:

1. The second claimant was an employee of the respondent from the 1 January 2014 until the date her employment terminated (to be determined).
2. Her contract of employment is not tainted by illegality.
3. The second claimant's claims of unfair dismissal and unlawful deduction from wages may proceed.
4. The contract of employment of the first claimant is tainted by illegality.
5. The claims brought by the first claimant for unfair dismissal and for breach of contract/unlawful deduction from wages in relation to notice pay, unpaid bonus or profit related pay cannot proceed and are hereby struck out.
6. The claims of the first claimant for unlawful deduction from salary in relation to any basic salary and any holiday pay due and owing up to the termination date can proceed.

REASONS

1. In this case the two claimants, who are husband and wife, bring claims for constructive unfair dismissal, unlawful deduction from wages and (in the case of the first claimant) breach of contract.
2. At a hearing on 29 October 2021 Judge Fowell decided that there should be a preliminary hearing to decide:
 - a. Whether the second claimant was an employee;
 - b. If so, whether the respondent was entitled to defend the claim on grounds of illegality; and
 - c. Whether an illegality defence also applied to the claim of the first claimant.
3. I heard evidence from both claimants and from Mr Marc Das, director of the respondent.
4. The facts I have found and the conclusions I have drawn are as follows.
5. Mr Shaw was recruited to join the respondent in 2005 and had the role of commercial director. The respondent's business was based in Essex but he would be based at his home near Warrington. He negotiated that he would receive a salary of £30,000 and his wife would receive a salary of £7000 per annum to provide him with administrative support. This recognised the fact that the first claimant would not be working at the respondent's premises and would require a certain amount of support for his sale work as a result.
6. The second claimant was given a letter dated 17 December 2004 setting out the terms of her employment, including a start date of 1 February 2005. She was to be paid a salary of £7500 per annum, had an annual leave entitlement of 20 days and was subject to a one month notice period.
7. The second claimant says and I accept that she provided her husband with admin support such as filing, booking his travel, shredding documents, internet research, buying competitor's samples and taking photographs of displays etc. This was in addition to more domestic tasks such as cleaning his office, making his lunch and filling the car with petrol.
8. This arrangement continued until 2007 when the second claimant ceased her employment to focus on looking after their children.
9. It is the claimants' case which I accept that by 2011/2012 the second claimant had resumed some work to support her husband's work activities. The first claimant registered his wife as a self-employed person. I have seen an invoice dated 14 February 2012 in which the second claimant charged the company the sum of £5,000. A list of duties is attached to the invoice. This includes some of the duties

that the second claimant had been carrying out previously, although the first claimant admitted that it had been somewhat exaggerated. I therefore find that during this period the work that the second claimant was doing was more limited than previously. It is the respondent's case and I accept that the sum of £5000 represented a portion of the first claimant's bonus which, it was agreed, would be diverted to his wife.

10. I understand that the first claimant wished to present a second such invoice around March 2013. I have seen an email from Mr Anil Das to the claimant and another stating that that he had spoken to the accountants who 'do not recommend the payment is made through your wives, due to HMRC issues.' He suggested that there could be difficulties for the company if this was treated as tax evasion. He recommended that the 'payment' was put into pension or into an ISA.

11. By late 2013 the first claimant was feeling significantly overworked. He requested additional support, and various options were discussed. A meeting took place between him and the directors which did not result in a resolution. The first claimant wrote to the respondent on 22 November 2013 and stressed that he was in dire need of additional support following the signing of a new contract.

12. Shortly after this the first claimant resigned.

13. It is not in dispute that the respondent wanted him to stay. Discussions took place. Eventually the first claimant wrote to the directors on 8 December 2013. This email seems to reflect, to some extent, discussions that had already taken place. He would get an increased salary, payment to his pension scheme, a bonus based on a percentage of turnover and profit related pay.

14. The first claimant proposed that the second claimant be 'fully employed' by the company – 'payment will be made to Marie from personal bonus and profit bonus which can be amortised over the full year as a monthly wage in arrears'. Tax and NI charges would be borne out of the bonus pot. If the first claimant's employment ceased then the second claimant would immediately resign.

15. The respondent agreed to this arrangement. It was not unusual within the company. The wife of another employee, T, was also on the payroll. It was the evidence of Mr Das that his own wife and the wife of his fellow director were also on payroll. In the case of the director's wives, Mr Das asserted that both of them were working in the business carrying out administrative tasks, issuing invoices, working on product lists and reporting to the office manager.

16. It is the evidence of the second claimant that whereas she carried out no duties for the company for a few years from 2007 onwards, she was doing some work to support her husband by the time the invoice was issued in 2012 and that this increased after 1 January 2014. She was providing very similar duties to those she performed when first employed by the company in 2005. She estimates and I accept that during this period her tasks took her 3-4 hours per day.

17. The second claimant did not know how much she was getting paid. She did not look at her payslips. The money was paid into a joint account. She was aware that the work she did would assist her husband by freeing up some of his time, which in turn might mean that he earned a larger bonus. She was not aware that the payments made to her were being diverted *from* his bonus.

18. The money paid to the second claimant varied according to how much bonus her husband received. If he received performance related pay it was paid out of that. In 2018/19 when the business dipped it was paid out of the turnover bonus to which he was entitled. On one occasion a pension payment was diverted from the first claimant into the second claimant's SIPP scheme. The bundle contains correspondence between the first claimant and the respondent setting out what bonus and profit related pay he had been awarded and what sums would be paid to his wife. The second claimant was not aware of the fluctuations in the amount she was being paid.

19. The discussions over what the second claimant would be paid were conducted entirely between the first claimant and the directors. They did not speak to the second claimant direct except at the occasional social event.

20. During the pandemic the second claimant was placed on furlough. A letter to her dated 30 March 2020 confirms that furlough leave would start on 1 April 2020. She was asked not to work anywhere. The letter states that 'as soon as business is back to normal, I will be in touch about your entry back into the company'.

21. During the furlough period the company claimed reimbursement of 80% of her wages from HMRC. It was the respondent's evidence that this was later repaid on grounds there had been a mistake in categorising the second claimant as an employee.

22. The employment of both claimants ended in circumstances that I will not go into here as it will be a matter for the tribunal that hears the full claim.

23. The respondent argues that the second claimant's employment was a sham and she never did any work for the company.

24. I find that the second claimant was an employee from 1 January 2014 to the date her employment terminated. I rely upon the following facts:

25. When she was placed on payroll on 1 January 2014 the second claimant did similar work to that which she had been doing between 2005-2007 when she was working under written terms of employment and received a fixed salary.

26. The wives of the company directors were also on the payroll and it was Mr Das' evidence is that this was because they were providing services to the company. The employment of the second claimant is therefore consistent with the practice adopted in relation to the wives of the directors.

27. I have noted that on one occasion a proposal to employ another family member was rejected on the grounds that this person, G was at university and there would be no benefit to the respondent. This suggests that the respondent was not prepared to place a person on payroll if they were not doing any work for the business.

28. The second claimant received payment for the services she provided. She was invited to join the respondent's pension scheme.

29. During lockdown she was placed on furlough and was given advice about not working for other companies. The respondent argues that this was a generic letter to all staff. The fact that a copy was sent to the second claimant suggests that she was being treated as an employee.

30. I accept that some tasks that were carried out by the second claimant were domestic. However, I also take note of the fact that the first claimant was working in a sales capacity from home, some distance from the office. I accept that he needed administrative support. He complained about a lack of support in November 2013, and when a solution could not be agreed he resigned. I accept that the second claimant was put onto payroll in order to address this issue. I find that the work carried out by the claimant went beyond domestic tasks and was of actual benefit to the respondent, given that the first claimant was working remotely.

31. The respondent argued that they had no contact with the second claimant. She was in effect only working for her husband. I do not find that this is inconsistent with the second claimant being employed by the respondent. The first claimant was a senior member of staff. The second claimant reported to her husband and was under his control in terms of the work she carried out. In effect the second claimant was carrying out a similar role to anyone who might have been employed within the office to provide him with sales and administrative support. I find that placing the second claimant on the payroll was not a 'sham'. She was genuinely working for the company and was receiving pay for her services. Whatever arrangements the respondent entered into with her husband over her pay, I find that there was a real need for her services. The diversion of his bonus payments do not, in this case, lead to a conclusion that she was not a genuine employee of the respondent.

32. I go on to consider whether the second claimant's contract of employment was nevertheless tainted by illegality, making it unenforceable?

33. I find that the first claimant genuinely needed support and wished his wife to be employed by the respondent for this purpose. It is strange then that the first claimant did not negotiate for the second claimant to be paid a separate salary for the work she was doing, as she had received in 2005. I queried why the first claimant, for example, did not forego the salary increase he was awarded in 2014 in order that his wife should receive a fixed salary. In his reply, the first claimant focussed on the fact that he needed support. But the arrangement that he reached simply meant that in gross terms, the same amount of salary was going to his household. The difference was that by diverting some of his bonus to the second claimant, his tax bill was reduced. There was no loss to the company as the

additional NI costs for employing her came out of the bonus he had been allocated. The first claimant acknowledged that there was both a tax saving for him and a benefit to the respondent in avoiding additional NI costs.

34. Whereas I have found that the second claimant was genuinely working for the respondent, I find that the purpose of the arrangements made to pay her was plainly to reduce the first claimant's tax bill. It was an arrangement entered into by himself and the directors in the full knowledge of this – as Mr Das said 'we both knew it was wrong'. I have noted that the amount of pay that the second claimant was not fixed. It varied not by the amount of work that she did, but by the amount of profit related pay or bonus that the first claimant was awarded. I can see no other reason for entering into such a strange arrangement save for avoiding tax.

35. In the case of **Patel v Mirza** [2016] UKSC 42 the Supreme Court provided guidance on whether a claim could continue where there is evidence of illegality. The court should take into account: the underlying purpose of the law that had been breached, and whether that purpose would be enhanced by the claim being refused; any other relevant public policy which might be affected by the denial of the claim; and whether denial of the claim would be a proportionate response to the illegality (bearing in mind that punishment is a matter for the criminal courts).

36. The court should also consider whether there is a sufficient causal link between the illegal conduct and the claim being made to the tribunal.

37. The Court of Appeal considered the illegality defence in the context of an employment situation in the case of **Hall v Woolston Hall Leisure Limited** [2001] 1WLR 225. It was found that for an employer to succeed in a defence of illegality, the employee would have to have both knowledge of and participation in the illegality.

38. I have noted that the second claimant did not know how much she was being paid nor did she look at her statements. Everything went into the joint account. She was aware of her change of status from self-employed to employed although this was sorted out by her husband. In answer to questions about her knowledge of what was going on, she agreed that she considered that the work that she was doing would lead to an increase in her husband's bonus. However, I find that she was not aware that her pay was being diverted from her husband's bonus entitlement. The second claimant might be described as naïve in taking such little interest in the amounts she was being paid. I find her to be a credible witness however who was careful to answer the questions put to her truthfully even when the answers did not assist her case. I find that she did not have knowledge of the tax evasion that was occurring and nor did she participate in it. She simply left everything to be sorted out by the first claimant.

39. Her claim for unfair dismissal and arrears of wages can therefore continue.

40. The first claimant was fully aware of the arrangement. It does not matter whether it was proposed by him or the company. The fact is that the respondent did not agree to pay the second claimant a salary over and above his remuneration.

The money was simply diverted out of money he would otherwise have received, with the result that he paid less tax. The respondent also avoided incurring any additional national insurance costs in employing the second claimant.

41. I go on to consider the principles set out in the case of **Hall v Woolston Hall Leisure Limited**. The first claimant clearly had knowledge of the payment arrangements that he agreed for his wife which had the effect of reducing his tax bill. He actively participated in the arrangement as is shown by documents in the bundle setting out the various negotiations between him and the respondents over how much bonus he would receive each year and how much would be paid to his wife.

42. I find that the contract of employment of the first claimant is tainted by illegality.

43. In accordance with **Patel v Mirza** I find that there is a clear public policy in ensuring that tax is accounted for properly to HMRC, and that parties should not enter into schemes to wrongfully avoid a tax liability that is due. Such a policy would be enhanced by refusal of the first claimant's claims. I have then considered carefully the question of proportionality.

44. Having read the contents of the bundle and other correspondence over disclosure supplied by the first claimant to the tribunal, I have noted that a significant part of his claims for unlawful deductions from his wages and breach of contract relate to his claims for payment of unpaid bonus and profit related pay. It is these elements of his remuneration package, for the most part, that were being paid illegally.

45. To the extent that the first claimant's claim seek to enforce a contract that was being performed illegally, those claims should not proceed as a matter of public policy. I find that it would be proportionate to refuse those claims.

46. Any claim for unpaid bonus or profit related pay therefore cannot proceed.

47. I have considered carefully whether any of the first claimant's other claims should proceed. These include his claims for unfair dismissal, for arrears of his basic salary from November 2020 to March 2021, for holiday pay and notice pay.

48. This is not a case where tax avoidance applied to the whole of the first claimant's remuneration arrangement. There is no evidence to suggest that, for example, he was wrongly representing that he was self-employed, or that he was not paying tax at all on his basis salary and any part of his bonus that was not being diverted. I have asked myself therefore whether it is reasonable to 'sever' any claim in relation to these elements and allow the other claims to proceed.

49. This presents problems however. If the diversion of salary to the second claimant related only to that part of his remuneration that represented profit related pay, the matter might be straightforward. The reality is not so easy. On occasion the diversion of salary came out of the 'turnover' bonus. On another occasion, a pension payment was diverted to the second claimant.

50. I have concluded that the diversion of money from one element of the salary package to avoid tax cannot be divorced from the contract as a whole. The arrangements to pay the first claimant bonuses and other benefits were wholly infected by the illegality.

51. I find that the claim for breach of contract in relation to notice pay cannot proceed as this would amount to a claim to enforce a contract that was being operated illegally.

52. I turn to the claim for unfair dismissal. This does not appear to arise out of the pay arrangements but out of a dispute between the directors and the first claimant at the end of the furlough period. I have considered whether it is proportionate to refuse that claim.

53. The first claimant claims constructive unfair dismissal. To succeed in that claim, he must show that the respondent was in fundamental breach of his contract of employment – a contract that was being performed illegally. I find that the same public policy considerations apply to this claim and it should not be permitted to proceed.

54. I find however that two of the first claimant's statutory claims should proceed.

55. The first is his claim for his basic salary from 1 November 2020 to the date his employment ended. This date is in dispute. As I have said, tax was being deducted from most of the first claimant's salary. If he establishes that his employment continued after 1 November 2020 I find that it would be disproportionate to prevent him from claiming his wages under section 13 of the Employment Rights Act 1996.

56. Secondly the first claimant claims pay for accrued annual leave. Again, I conclude that it would be disproportionate to refuse the right to claim any such pay as falls due.

57. The full merits hearings of the claims of both claimants has already been listed for 12 April 2023 and that hearing will remain in place to deal with the claims that are proceeding. I have issued a separate case management order to fix a timetable leading up to that hearing.

**Employment Judge Siddall
Date: 9 February 2022**