EMPLOYMENT TRIBUNALS

BETWEEN

Claimants		**Respondent**
Mr C Edgecombe (1) Mrs K Edgecombe (2)	AND	The Secretary of State for Business and Trade

JUDGMENT OF THE EMPLOYMENT TRIBUNAL

HELD REMOTELY **ON** 28 November 2024
By CVP VIDEO

EMPLOYMENT JUDGE N J Roper

Representation
For the Claimants: **Mr A Welch, Accountant**
For the Respondent: **Mr P Soni**

JUDGMENT

The judgment of the tribunal is that the claimants were not employees, and their application for payment 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 claimants. In this case the claimants Mr Christopher Edgecombe and his wife Mrs Kelly Edgecombe have brought claims against the respondent, the Secretary of State, seeking payment from the National Insurance Fund. The respondent denies that the claimants were employees and accordingly asserts that there is no liability to the claimants.
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. Despite a previous case management order for the preparation of written witness statements, neither of the two claimants prepared a statement, and neither of the claimants were called to give evidence today. Their representative Mr Welch made submissions on their behalf which effectively conceded that “there was a viable case that directors should not be paid redundancy payments”, but which objected to the respondent’s assertion that

failure to pay at least the National Minimum Wage was a factor which had only lately been introduced by the respondent after the claimants had made their claims to the respondent's Redundancy Payments Service ("the RPS"). These assertions were consistent with the originating applications to this tribunal. I have heard from Mr Soni on behalf of the respondent. There was a detailed bundle of documents running to 164 pages which was agreed by the parties. Effectively, the primary facts were not in dispute. Bearing in mind all of the above, 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 two claimants are Mr Christopher Edgecombe and his wife Mrs Kelly Edgecombe. They were the owners and proprietors of a limited company namely Pocketfold Invites Limited (which is referred to in this judgment as "the Company"). The Company entered creditors voluntary liquidation on 6 September 2022. The Company had effectively been a husband-and-wife quasi-partnership. The claimants were both directors, and equal shareholders who held 50% of the shareholding each. The Company employed the claimant's son, and one other employee.
5. The various applications made by both claimants have in places been inconsistent. Following the liquidation of the company both claimants made an application to the RPS, and these were identical. The claimants confirmed that they did not hold a written contract of employment or any statement setting out any terms and conditions of employment.
6. In their online applications to the RPS for payments, both claimants confirmed that they had worked a 40 hour week at a fixed rate of £1,000 per month, giving an annual salary of £12,000. However, this was inconsistent with their directors' questionnaires, in which both claimants confirmed that they worked more than 50 hours every week. This was again inconsistent with the conclusion reached by the Insolvency Practitioner (who was appointed on the liquidation) who confirmed that both claimants worked 35 hours per week. This was all inconsistent with the relevant pay documentation, which evidenced that both claimants received an income below these figures claimed, and below the level of the National Minimum Wage ("the NMW"). The relevance of this point is that company directors are officeholders and under the National Minimum Wage Regulations 2015 are not entitled to receive the NMW for the work they do is an officeholder. This is because they are entitled to set their own rate of remuneration. However, if they are also an employee, then they must be paid the NMW for the work they do as an employee.
7. The HMRC Forms P60 for both claimants to the tax year ended 5 April 2022 show income of £8,784 with tax deducted of £40.80 and no National Insurance Contributions paid. The tax assessment for Mr Edgecombe to the year ended 5 April 2019 shows pay from all employments at £8,424, and for the subsequent tax year pay for all employments of £8,628. The tax assessment for Mrs Edgecombe to the tax year ended 5 April 2020 shows pay from all employments at £1,628. Despite these figures, in their online applications to the RPS dated 11 December 2022, both claimants claimed that they were not paid less than the NMW at any point in the last three years.
8. In their directors' questionnaires the claimants confirmed that they were the only directors in the company and they each held 50% of the company shares. They confirmed that they were not subject to any supervision or guidance, and that they were not subject to the company's disciplinary procedures. They confirmed that there was nobody within the company who could take disciplinary action against them. There is no evidence to indicate that there was any other person with which either claimant could agree or disagree to impose or accept a pay arrangement below the level of the NMW.
9. Both claimants did benefit from dividends. They confirmed in their directors' questionnaire that they received combined dividends of £40,000 per year. The tax assessment for Mr Edgecombe to the tax year ending 5 April 2019 show dividends of £33,908, and for the subsequent tax year dividends of £35,000. The tax assessment for Mrs Edgecombe for the tax year to 5 April 2020 shows dividends of £35,000. The unaudited financial statements of the Company for the year ended 30 April 2021 shows dividends paid and payable of £70,000 in 2020, and £20,000 in 2021. The statement also confirmed that the Company was significantly controlled by its sole shareholders, namely the two claimants.

10. Both claimants also operated a Director's Loan Account, which was cleared on the liquidation. In addition, they both provided a personal guarantee on a bank overdraft and other lending.
11. The claimants were thus able to 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.
12. The claimants were also able to control how they received remuneration from the Company. The first respondent asserts that the claimants have 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 directors to pay themselves. This is not a benefit which is afforded to a bona fide employee who would not have that privilege.
13. Having established the above facts, I now apply the law.
14. The relevant legislation is the Employment Rights Act 1996 ("the Act").
15. 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.
16. 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
17. Section 184 of the ERA applies section 182 to arrears of pay; accrued holiday pay and statutory notice pay (but subject to maximum amounts).
18. For the Secretary of State to be liable, any such claimant must have been an employee.
19. 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.
20. 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.

21. 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.”
22. 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?
23. 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".
24. 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.

25. 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).
26. 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).

27. 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.
28. 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).
29. 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.
30. 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?
31. 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.
32. Against this background my conclusion is as follows.
33. In the first place it is clear that the fact that the claimants were directors and shareholders does not preclude them from also being employees. However, in this case there was no written contract of employment, and no statement setting out terms and conditions of

employment, and the claimants were not subject to any supervision or guidance, and nor were they subject to the Company's disciplinary procedures. There was nobody within the Company who could take disciplinary action against them, and no other person with which either claimant could agree or disagree to impose or accept a pay arrangement below the level of the NMW.

34. The claimants also chose 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 claimants were clearly in a position which enabled them to control what payments they received and when.
35. In addition, I agree with the respondent's assertion that the claimants chose not to have the relationship treated as one of a genuine employee, simply by dint of the fact that their chosen salaries fell short of the National Minimum Wage. There is a legal requirement for employers to pay all employees at least the NMW. If the claimants had chosen to be treated in this way the salaries which would then fall due would have been subject to tax and National Insurance, whereas the sums which the claimants chose to receive did not necessarily meet those thresholds. It has been argued on behalf of the claimants that this was a condition which was only imposed by the respondent after the claimants had submitted their claims. I do not agree without submission. It is one of many factors which assist in reaching a conclusion as to employment status, and as such is a point which the respondent has been able to argue ever since the introduction of the NMW.
36. In conclusion I find that there was no genuine employment relationship in place at the time the Company entered liquidation, which is the relevant time when the first respondent is potentially liable for payment. Accordingly, the claimants' claims 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 28 November 2024

Judgment sent to Parties on
14 December 2024 By Mr J McCormick