

Enfield Technical Services v Payne; Grace v B F Components

In *Tinsley v Milligan*, Lord Goff stated: “The principle [of illegality] is not a principle of justice; it is a principle of policy whose application is indiscriminate and so can lead to unfair consequences as between the parties to litigation. Moreover, the principle allows no room for the exercise of any discretion by the court in favour of one party or the other.” However, in the recent cases of *Grace* and *Payne* the Court of Appeal has limited the application of the doctrine of illegality in the employment context, perhaps because otherwise the outcome would have been unjust.

Felicia Epstein reports

Today’s complex situation in relation to employee status and who is an employee means that it is not always clear whether someone can be considered self-employed or whether, notwithstanding their intentions and those of their employer, they are employees. A person may believe that they are self-employed – and cause their tax affairs to be conducted as if they were self-employed – but in the eyes of the law be considered an employee and on that basis benefit from employment rights.

In *Hall v Woolston Leisure Services Ltd*, Peter Gibson LJ identified three categories of illegal contract:

- the contract is entered into with the intention of committing an illegal act
- the contract is expressly or impliedly prohibited by statute
- the contract was lawful when made but has been illegally performed, and the party seeking the assistance of the court knowingly participated in the illegal performance. To fall within the third category one must have knowledge of the illegal performance and participation.

Both *Grace* and *Payne* concerned the third category. The appeals, first to the Employment Appeal Tribunal and subsequently to the Court of Appeal, in these two cases were heard together as they both concerned applications to the employment tribunal by people who had been treated as self-employed but were later found to be employed. In both cases it was the employee in question who insisted on maintaining or entering into the self-employed arrangement.

Payne: the background

Both claimants later wanted to claim that they had been unfairly dismissed and needed the requisite one year’s minimal service before being eligible to make that claim. In *Payne*, Mr Payne worked as a sub-contractor for Enfield Technical Services. The Inland Revenue accepted that he was self-employed. However, the employer stated to a third party that Mr Payne was an employee. The tribunal rejected the employer’s submission that Mr Payne’s could not make a claim for unfair dismissal because his contract of employment was tainted by illegality.

Grace: the background

Mr Grace initially worked for B F Components on a self-employed basis but was later – a few months before his employment was terminated – required to sign a contract of employment. Mr Grace argued that he had established a continuous period of employment to qualify to claim unfair dismissal. The tribunal held that as Mr Grace knew that the Inland Revenue was not being paid by his employer and he actively participated in it, he could not claim unfair dismissal because he was party to the illegal performance of a contract.

The appeals considered

The Employment Appeal Tribunal, presided over by Elias J, dismissed the employer’s appeal in the *Payne* case, but allowed Mr Grace’s appeal.

The Court of Appeal dismissed both employers’ appeals. The employers relied on the statement of Underhill J in *Daymond v Enterprise South Devon* that:

“Where an employee has made a positive choice to operate arrangements which have the effect of depriving the Revenue of payment to which it is entitled, contracts giving effect to those arrangements will be unenforceable notwithstanding that the employee may genuinely have believed them to be lawful. The position might be different where the initiative came from the employer; but those are not the facts in that case.”

However, the Court of Appeal agreed with the EAT that this statement was too broad, and agreed with Elias J that the authorities do not:

*“Support the proposition that if the arrangements have the effect of depriving the Revenue of tax to which they were in law entitled then this renders the contract unlawful ... **there must be some form of misrepresentation, some attempt to conceal the true facts of the relationship, before the contract is rendered illegal** for the purposes of a doctrine rooted in public policy.” [emphasis added]*



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Pill LJ went on to state that he did not accept that a characterisation of the relationship held to be erroneous necessarily prevented an employee subsequently claiming the advantages of being, or having been, an employee.

A contract of employment may be unlawfully performed if there are misrepresentations, express or implied, as to the facts; such as when what is in fact taxable salary is claimed to be non-taxable expenses.

Pill LJ stated that the situation is, however, different where there is an error of categorisation unaccompanied by such false representations, even if the employee had claimed the advantages of self-employment before the dispute arose. Pill LJ stated that:

“A genuine claim to self-employment, unaccompanied by false representations as to the work being done or the basis on which payment is being made, does not necessarily amount to unlawful performance of a contract of employment.”

Applying these principles to the facts of the appeals before it, the Court of Appeal held that both Mr Payne and Mr Grace were employees and that there had not been any unlawful performance of their contracts of employment to prevent them from claiming unfair dismissal.

Clarifying the law

The decision of the Court of Appeal in *Payne and Grace* clarified the law of illegality in two respects:

- misrepresentation, either express or implied, or some intention to conceal facts is necessary for the doctrine of illegality to apply. An error in the classification of a contract is not sufficient to render the contract illegal
- participation of the employee – which can include being aware of the relevant facts, including that the employer is not paying National Insurance and tax on the employee’s behalf – does not in and of itself deem the contract illegal.

While the decision of the Court of Appeal was based on the particular facts of these two cases, it is likely to be of wider

application and so may cause practical difficulties for employers. This is because it creates situations of uncertainty for employers as to the position of those who work for them. These individuals can be incorrectly categorised as self-employed and benefit from tax advantages, and yet could potentially – perhaps at a much later date – claim employment status and employment rights.

In *Payne and Grace* the Court of Appeal noted that in many cases it would not be clear-cut whether a person is, or was, an employee or self-employed. Pill LJ noted that a decision about whether a relationship is one of employment or whether the person performing the services is self-employed will often be very difficult, and that predictions as to the side of the line on which a particular relationship will be held to fall are notoriously difficult to make.

Discrimination claims are different

It should be noted that the issue of illegality is dealt with differently in the context of discrimination claims. Discrimination claims can be allowed even if the contract has been performed illegally when the core of the complaint does not rely to the contract of employment. In *Leighton v Michael* the tribunal had decided that the employment contract had been performed illegally. Allowing the employee’s appeal, Mummery J in the EAT permitted a claim to be made for sex discrimination, stating that the illegality of the contract was irrelevant since a claimant did not need to rely on their contract of employment.

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Cases referred to:

Tinsley v Milligan [1994] 1 AC 340

Enfield Technical Services Ltd v Payne; Grace v B F Components Ltd [2008] EWCA Civ 393

Hall v Woolston Leisure Services Ltd [2000] IRLR 578

Enfield Technical Services Ltd v Payne; Grace v BF Components Ltd UKEAT/0644/06/MAA; UKEAT/0367/-6/MAA

Daymond v Enterprise South Devon UKEAT/0005/07]

Leighton v Michael [1996] IRLR 67