EMPLOYMENT TRIBUNALS

Claimant: Miss S Holmes

Respondent: Tellemachus Limited

Heard at: Leeds **On:** 9 October 2019

Before: Employment Judge D N Jones

REPRESENTATION:

Claimant: In person
Respondent: Miss R Mellor, counsel

JUDGMENT

1. The respondent shall pay to the claimant the sum of £26.40, being outstanding holiday pay of £24 and an increase at 10%, being £2.40 as a consequence of the respondent's unreasonable failure to comply with the ACAS Code of Practice on Discipline and Grievance Procedures.

2. The claims for breach of contract and unauthorised deductions from wages in respect of the sum of £945 for agency recruitment fees and consequential losses is dismissed.

3. Having invited the parties to make representations about whether, of its own volition, the Tribunal should reconsider the judgment in paragraph 2 above and, after consideration of those representations, it is not necessary in the interests of justice to reconsider the judgment.

REASONS

Introduction

1. This is a claim for breach of contract and unauthorised deduction from wages. Although there was originally a complaint in respect of deductions made in respect of pension, this has subsequently been paid after the claim was issued and the claim now concerns the recoupment of a sum of £945 deducted from the claimant's last wage slip leaving her with net pay of £368.10 and the computation of the holiday pay owing.

2. In addition the claimant seeks consequential losses in respect of items set out in a remedy statement she helpfully prepared which are losses attributable to the financial hardship thrown onto her as a consequence of the unauthorised deductions including the computation of her entitlement to Universal Credit, Housing Benefit and the set-back in seeking other employment and the delay in having diagnosed a medical condition.

3. I heard evidence from the claimant. The respondent did not call evidence but I was provided with two substantial files of documents from both parties.

The law

4. Section 13(1)(a) and (b) of the Employment Rights Act 1996 (ERA) provide that an employer shall not make a deduction from the wages of a worker employed by him unless the deduction is required or authorised to be made by virtue of a statutory provision or the relevant provision of the worker's contract or the worker has previously signified in writing his agreement or consent to the making of the deduction. By section 13(3) of the ERA where the total amount of wages paid on any occasion by an employer to a worker employed by him is less than the total amount of the wages properly payable by him to the worker on that occasion (after deductions) the amount of the deficiency shall be treated as a deduction made by the employer from the worker's wages on that occasion.

5. Under the Extension of Jurisdiction Order (England and Wales) Order 1994, a claim may be brought for damages for breach of a contract of employment in the Employment Tribunal.

6. By regulation 14 of the Working Time Regulations 1998, an employee whose employment is terminated during the course of the leave year is entitled to payment in lieu of leave in accordance with a formula which provides for a pro rata payment of leave accrued but not taken. Under regulations 13 and 13A an employee is entitled to 5.6 weeks leave in a year.

7. By section 207A of the Trade Union and Labour Relations (Consolidation) Act 1992 a Tribunal may increase or reduce any award by up to 25% as a consequence of a party's failure reasonably to comply with the ACAS Code of Practice on Discipline and Grievance procedures.

8. I shall address the case law in respect of penalty clauses and the National Minimum Wage in my analysis below.

The facts

9. The claimant had been employed by the respondent on a temporary basis from 14 January 2019 until 24 January 2019 as a temporary administrator but she was provided with a permanent contract by the respondent on 28 January 2019 and she and her employer signed written terms and conditions of employment on 24 January 2019. The claimant was to receive a basic starting salary of £21,000.

10. Paragraph 14 related to holidays. The claimant was to receive 20 days per year and bank holidays which equated to 28 days which was the same as the claimant was entitled to under the Working Time Regulations 1998.

11. Paragraph 19 was headed 'recruitment costs'. It stated, "It is anticipated that during the course of your employment Tellemachus will incur significant costs relating to your recruitment. We estimate these to be 20% of your basic starting salary. In the event you resign your employment of the respondent for any reason

you agree to pay the cost to the respondent on the following basis: 75% in the event that you resign within 12 months of your start date; 50% in the event that you resign within 24 months of your start date and 25% in the event that you resign within 36 months of your start date".

12. The claimant resigned her employment on 12 April 2019. She was required to provide one week's notice, by clause 6 of the contract. That expired on 19 April 2019 which happened to be a bank holiday, Good Friday. The claimant was not in fact working on that date. The respondent was tardy acknowledging the letter of resignation but it is not disputed before me that the notice expired on that date.

13. The respondent held a meeting with the claimant on 18 April 2019 and informed her that it intended to deduct a sum of £945 from her final salary payment because of clause 19 of the contract. She was told the reduction would have been 75% of the sum incurred to pay the agency, but as a gesture of goodwill that sum would be reduced by 50%.

14. The claimant submitted a written grievance to the respondent on 25 April 2019 in respect of a number of items including the recoupment of the £945. The respondent replied to the grievance on 30 April 2019 and dismissed it. The claimant submitted a response on 9 May 2019 which set out a detailed history. She challenged the decision to make deductions from her salary, complained that she had been bullied causing her to become ill and that this had led to her resignation. That was dealt with by way of an appeal and the respondent appointed an external advisor to consider all matters raised. The response of 17 May 2019 did not uphold the complaints save for repayment of a pension payment which had been deducted.

<u>The deduction of the recruitment fees</u>

15. The starting point is the written terms. They permit the respondent to charge a sum for recruitment costs. These are estimated at 20% of the salary but the actual charge is reduced by a percentage over a period of three years. It is payable in the event the employee resigns.

16. The claimant says that is a penalty. It deters an employee from leaving. She says no benefit arises for her in contrast to similar clauses which recoup training costs. I recognise the distinction and that training more obviously creates a potential to benefit the employee in the longer term. That said, there is some benefit to the employee in obtaining the employment and the benefits that brings.

17. But this is, in reality, a decision to distribute some of the costs of running the employer's business onto the employee. The provision is designed to compensate it, in a rather unsophisticated way, by projection of broadly estimated recruitment costs against the corresponding value the employee brings, similarly rather crudely evaluated, over a period of three years. It could have chosen to set the salary at a lower starting rate than £21,000 by the cost of recruitment, and then to increase it incrementally over a three year period, thereby reflecting the value to the employer of the claimant's continuing service. If it had been expressed in that way it would not have been seen as a deterrent from leaving but a reward for loyalty in remaining. Viewed as a choice in that context, the higher starting salary presents an immediate attraction. The financial consequences of choosing to leave early may be less obvious or apparent to the new starter. But structured in the way it was, in the early weeks of employment the average rate of pay would have been below the national minimum wage or possibly for no pay at all.

18. I must address the claim in two stages. Firstly, is the agreement one which is lawful, in respect of clause 19, under general principles of contract law? Secondly has any legislation overridden that, in this case by way of the National Minimum Wage Act and Regulations?

19. Does the rule concerning contractual penalty clauses apply? Penalty clauses are ordinarily concerned with payment to be made to one party in the event of a breach by the other. There was no breach of a contract in this case because the claimant lawfully terminated her contract by giving one week's notice.

20. In the leading case on penalty clauses, **Cavendish Square Holding BV v Makdessi; Parking Eye Ltd v Beavis (Consumers' Association intervening) [2016] AC 1172**, the President of the Supreme Court said, at paragraph 12, "*In England, it has always been considered that a provision could not be a penalty unless it provided an exorbitant alternative to common law damages. This meant it had to be a provision operating on a breach of contract"* and at paragraph 13, "*This principle is worth restating at the outset of any analysis of the penalty rule, because it explains much about the way in which it has developed. There is a fundamental difference between a jurisdiction to review the fairness of a contractual obligation and a jurisdiction to regulate the remedy for its breach. Leaving aside challenges going to the reality of consent, such as those based on fraud, duress or undue influence, the courts do not review the fairness of men's bargains either at law or in equity. The penalty rule regulates only the remedies available for breach of a party's primary obligations, not the primary obligations themselves*". At paragraph 14 Lord Neuberger said, "*This means that in some cases the application of the penalty rule may depend on how the relevant obligation is framed in the instrument, ie whether as a conditional primary obligation or a secondary obligation providing a contractual alternative to damages at law. Thus, where a contract contains an obligation on one party to perform an act, and also provides that, if he does not perform it, he will pay the other party a specified sum of money, the obligation to pay the specified sum is a secondary obligation which is capable of being a penalty; but if the contract does not impose (expressly or impliedly) an obligation to perform the act, but simply provides that, if one party does not perform, he will pay the other party a specified sum, the obligation to pay the specified sum is a conditional primary obligation and cannot be a penalty*".

21. An important qualification to this peculiar distinction is then addressed by Lord Neuberger at paragraph 15: "*However, the capricious consequences of this state of affairs are mitigated by the fact that, as the equitable jurisdiction shows, the classification of terms for the purpose of the penalty rule depends on the substance of the term and not on its form or on the label which the parties have chosen to attach to it. As Lord Radcliffe said in* Campbell Discount Co Ltd v Bridge *[1962] AC 600, 622, "the intention of the parties themselves", by which he clearly meant the intention as expressed in the agreement*, *"is never inclusive and may be overruled or ignored if the court considers that even its clear expression does not represent 'the real nature of the transaction' or what 'in truth' it is taken to be" (and cf per* Lord Templeman in Street v Mountford *[1985] AC 809, 819)*.

22. The application of this test, even with the latitude allowed by the equitable jurisdiction, leads me to the conclusion that the penalty rule cannot apply to this case. This is not an obligation in the contract for the claimant to perform an act in default of which she shall pay a sum of money. The contract expressly permits her not to perform the act of remaining in work, by providing for its termination by the

giving of notice. The requirement to pay the recruitment fee falls into the second category described in paragraph 14 of the judgment in *Cavendish;* that is that if Miss Holmes does not perform, by terminating the contract herself and giving notice within three years, she shall pay to the respondent the sum defined in clause 19. Equity allows me to scrutinise this provision and construe it differently if it was not the true nature of the obligation. It does not allow me to rewrite the contact because I consider it a bad bargain, a course expressly forbidden by the principles described in paragraph 13 of the judgement of the Supreme Court President.

23. The respondent did not recoup 75% of 20% of the annual salary of the claimant as defined in clause 19. That would have been £3,150, 75% of £4,200. It used the agency fee of £2,520 as the cost of recruitment, 75% of which was £1,890. It reduced that by 50% because to £945. It said this was a gesture of goodwill. I am satisfied that would be permissible because clause 19 quantifies the cost as an estimate. I consider that provides sufficient certainty as a contractual term to allow a lesser rather than a higher charge.

24. If I am wrong about the term not engaging the penalty clause rule, I must consider whether it is unenforceable as a penalty. In my oral judgment in addressing this issue I considered that it was not. I had in mind the case of *Cleeve Link Ltd v Bryla* [2014] IRLR 86. The facts of that case had a similarity to those in this one although the employee was dismissed for gross misconduct. By so acting, the employee no doubt placed himself in breach of a fundamental contractual term, not least the term of trust and confidence. That is significant because damages would be payable for the employee's contractual breach, in contrast to this case in which the claimant resigned, so in principle the penalty rule could apply.

25. On the question of whether the sum payable was extortionate, the EAT held the issue was whether the term was essentially one of deterrence or a genuine pre-estimate. It held that because the maximum loss was reflected by the sums in the repayment agreement, it was a liquidated damages clause and not a penalty. In my earlier reasoning I considered that the quantification of the cost of recruiting the claimant was in the nature of a pre-estimate of loss and therefore, as in Cleeve, a liquidated damages clause.

26. After having given judgment, it struck me that I may not have fully appreciated the impact of the decision in *Cavendish*. I invited the parties to make representations about whether I should reconsider the decision. As I indicated in the invitation, that was not a criticism of anyone other than myself, as counsel for the respondent had properly drawn my attention to the authorities and submitted *Cleeve* had to be considered in the light of *Cavendish*.

27. On this matter, Lord Neuberger said, ''*The real question when a contractual provision is challenged as a penalty is whether it is penal, not whether it is a pre-estimate of loss. These are not natural opposites or mutually exclusive categories. A damages clause may be neither or both. The fact that the clause is not a pre-estimate of loss does not therefore, at any rate without more, mean that it is penal. To describe it as a deterrent (or, to use the Latin equivalent, in terrorem) does not add anything. A deterrent provision in a contract is simply one species of provision designed to influence the conduct of the party potentially affected. It is no different in this respect from a contractual inducement. Neither is it inherently penal or contrary to the policy of the law. The question whether it is enforceable should depend on whether the means by which the contracting party's conduct is to be influenced are*

"unconscionable" or (which will usually amount to the same thing) "extravagant" by reference to some norm.' (per Lord Neuberger at [31])'.

28. I am satisfied my earlier reasoning was erroneous because I was treating the question of whether the sum recouped was a genuine pre-estimate of loss as a natural opposite to it being a penalty. I am now satisfied that the clause was unconscionable or extravagant. I must consider it as at the time the parties entered into the agreement. At that time, had the claimant considered the possibility of leaving she would have believed she faced the prospect of paying back £3,150 in the first year of her employment. If she had left in any period up to 7 weeks, if the costs had been as estimated as 20% of the annual salary, it would have wiped out any earnings at all. The claimant says that there would have been no recoupment fee if she left within six weeks because of the agreement between the agency and the respondent and that had she resigned in that period as she had originally intended, there would have been no recoupment charge. That may have been correct, if the term had been put into effect in the same way, but for these purposes I am considering the contractual clause which estimates the recruitment cost of 20% of salary. Excluding holiday pay the actual sum paid to the claimant after the sum of £945 was deducted for April 2019 was £185 for 3 weeks' work for a 40 hour week. That is an average net hourly rate of £1.54. The structuring of the repayment in this way, by clause 19, had such a dramatic and deleterious effect to the principle of the wage bargain in modern times that I consider it to be extravagant and unconscionable. Had I not already held that the penalty clause rule had no application, I would have ruled that this clause was unenforceable. That does not assist the claimant, given my principal finding. Therefore at common law clause 19 is not assailable.

29. The claimant argues that the consequence of this deduction on her earnings, whereby it is reduced below the national minimum wage, leads to the result that the clause is unlawful by defeating Parliament's intention of guaranteeing a level below which wages shall not fall below. As I have indicated for the month of April the claimant received a wage which was but a small proportion of the hourly rate under the National Minimum Wage Act 1998 and the National Minimum Wage Regulations 2015.

30. I consider I am bound by an authority of the Employment Appeal Tribunal as to the effect of Regulation 12, in the case of ***HMRC and Lorne Stewart Plc [2015] IRLR 187***. Regulation 12(1) provides that deductions made by the employer in the pay reference period or payments due from the worker to the employer in any pay reference period for the employer's own use and benefit are treated as reductions except as specified in paragraph 2 and Regulation 14. Paragraph 12(2)(a) provides: "The following deductions and payments are not treated as reductions…deductions or payments in respect of the worker's conduct, or any other event, where the worker (together with another worker or not) is contractually liable".

31. His Honour Judge Shanks determined that upon the employee's voluntary resignation training fees could be recouped, notwithstanding they reduced the payment below the level of the national minimum wage. He held that in the language used 'conduct' would mean misconduct of the employee, but although 'any other event' would mean some form of conduct of the employee that would include a voluntary resignation. Miss Holmes' answer to that is the recoupment fees were not for her benefit. I am not satisfied that submission assists her because Regulation 12(1) is specifically considering recoupment for the employer's benefit. In those

circumstances I cannot find that the provision was rendered unlawful because of the National Minimum Wage Regulations.

32. In the circumstances I find that the respondent was entitled to rely upon Clause 19 and that it fell within the entitled deduction which I have set out in Regulation 13(1A) of the Employment Rights Act 1996.

33. I am not satisfied anything terms on the question of it being deducted after payment of tax as opposed to it being a non-taxable deduction. This is referred to by the claimant in her remedy statement and her further representations in respect of the reconsideration. The respondent says that the deduction was made from the gross figure before tax and national insurance was calculated for payroll purposes.

34. I note that the assessment of tax and national insurance on the April payslip was the first month on the financial year. That would be based upon a number of assumptions about an employee's earning upon which HMRC create a personal tax code. The effect of the sum being deducted from a gross or net figure would be corrected upon a challenge to HMRC as to it being an allowable deduction for tax purposes or by reassessment of tax at the end of the financial year. I am not satisfied this issue falls within the jurisdiction of this tribunal under section 13 of the ERA.

35. The claimant also raised some issues concerning data protection mishandling. These would be matters for the Information Commissioner and the First Tier Tribunal.

36. I do not make any finding about other consequential losses because these were conditional upon the claimant succeeding in her claim in respect of the recruitment fee deduction.

37. I turn therefore to holiday pay and this is to a large extent is agreed. The claimant worked for 12 weeks and she was entitled to a daily rate of pay of £80.77.

38. Although the dispute between the parties seemed to turn upon whether she was entitled to take off the Good Friday, I am satisfied that is not determinative of this case because the claimant was owed for other holidays. The Good Friday could be deemed to be one of the other days for which she was ultimately paid because the respondent paid the claimant a sum of £428.08 in relation to holiday. It did that by reference to the guidance on the Government Department website

39. Because the claimant worked for 12 weeks she was entitled to a pro rata equivalent of 28 days per annum, see Regulation 14 of the Working Time Regulation 1998. That equates to 0.538 days per week which for 12 weeks would be 6.46 days. She had taken one day's holiday in March and was therefore entitled, on leaving her employment, under the Working Time Regulations to 5.46 days. The respondent calculated she was entitled to 5.36 by rounding down pursuant to the guidance on the website but that was an underpayment of £24.

40. I am satisfied that the respondent breached the ACAS Code of Practice on grievance procedures. It held an appeal of the grievance but did not invite the claimant to attend an appeal meeting. That was not in conformity with paragraphs 42 and 44 of the Code.

41. Miss Mellor submitted the Code did not apply because the claimant was a former employee and the Code applies only to employers and employees. Whilst I am not aware of any authority on the point, I was not satisfied the Code was intended to be so strictly interpreted. The grievance was closely connected to the

end of the claimant's employment and she could not have brought it during her employment because it related to her last pay slip. If she had presented a complaint about an earlier wage slip during her employment the Code would apply, which leads to an unsatisfactory and anomalous result, if construed as submitted.

42. For the unreasonable failure to comply with the Code I shall increase the award by 10%, £2.40. It would be inappropriate to award a higher increase because there had been substantial compliance otherwise.

43. Under rule 70, a tribunal may reconsider of its own volition or upon the application of a party its judgment if it is necessary in the interests of justice to do so. I considered that this might be such a case, for the reasons I have explained. I have considered the representations of the parties and am satisfied it is not necessary to do so. That is because although I have altered my opinion on one issue, it does not affect the outcome because of my primary ruling.

44. I recognise that the case involved some technical and difficult legal issues and the claimant did not have the benefit of representation. The authorities which were provided by the representative of the respondent at the hearing are ones upon which the claimant has now been able to consider and comment, in her further representations and I have fully taken into account what she and the respondents' representatives have said.

Employment Judge D N Jones

Date: 21 October 2019