[2010] UKUT 214 (TCC)

Appeal Number: FTC/16/2009

National Insurance Contributions – Contributions reduced by pay practice – pay practice not counteracted by Secretary of State – Resultant reduction in SERPS pension payable to appellant – Whether appellant retrospectively entitled to challenge past contribution levels – Whether error of law in First Tier Tribunal's rejection of that challenge.

UPPER TRIBUNAL
(TAX & CHANCERY CHAMBER)

JOHN ALEXANDER LITHGOW MASON Appellant

-v-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS Respondents

TRIBUNAL: THE HON LORD EMSLIE
JULIAN GHOSH QC

Sitting in public in Edinburgh on 24 and 25 March 2010

The Appellant in person

For the Respondents: Sean Smith, Advocate; Solicitor's Office, HM Revenue & Customs

DECISION

Introduction

[1] The appellant is a former electrician who spent many years working on offshore installations in the North Sea where the standard regime was "two weeks on, two weeks off". Between 1983 and 1998 in particular, the practice was for the vast bulk of salary to be paid in respect of the offshore (working) fortnight, with a small residue or "retainer" of £69 then following in respect of the onshore (rest) fortnight along with any tax rebates due. Grossly unequal payments would thus be received at approximately two-weekly intervals. A significant effect of these arrangements was that the primary (employee) national insurance contributions ("NICs") deductible from the large offshore payment were approximately halved because the statutory upper earnings limit ("UEL") for fortnightly NIC purposes was far exceeded. Less significantly, no NICs were deductible from the £69 "retainer" because that fell below the fortnightly lower earnings limit ("LEL"). Had salary been paid in two approximately equal shares, these effects would not have arisen. Equally, had salary been paid in one monthly sum rather than in unequal fortnightly instalments, the relevant statutory UEL would have been twice as high and would have led to a corresponding uplift in the deductible NICs.

[2] Although generally aware of such arrangements at the time, the appellant did not appreciate that they would adversely affect the level of his SERPS pension when, in the future, he came to retire. Having now reached retirement age, he is aggrieved to have lost out on pension entitlement due to former pay and NIC practices which he regards as artificial and unfair. He would, he says, have been better off unemployed during all onshore periods, since that would have blocked the uneven fortnightly salary payments which depressed his NICs to such an extent. Alternatively, had he realised the long-term detriment to his pension, he could have considered opting out of the statutory scheme and investing in private pension arrangements instead. On no view, according to him, should he now have to tolerate an inadequate SERPS pension caused by pay and NIC practices for which he personally carried no responsibility.

[3] As regards secondary (employer) NICs, these were also calculated by reference to gross salary received at particular intervals. Up to about 1986, these were also depressed by reason of the relevant UEL being far exceeded in offshore fortnights, but thereafter the UEL for secondary NICs was withdrawn so that the large offshore payment attracted a full deduction. However, the resultant increase in secondary NICs had no beneficial effect on the appellant's pension entitlement because, in terms of the statutory scheme, the level of a SERPS pension depends on the deductible amount of primary (employee) NICs alone. This has further enhanced the appellant's sense of grievance where, in his mind, the Treasury have had the benefit of full secondary contributions which ought by rights to have benefited him. A further sense of grievance arises from his perception that, under relevant regulations, the Secretary of State at all material times had power to intervene and regularise abnormal and artificial pay practices affecting the NIC regime. The Secretary of State's unexplained failure to act should not, in the appellant's view, work to his disadvantage, and it was surely not too late to rectify matters now.

[4] The appellant would even be prepared to pay "missing" NICs at this stage in order to secure the full pension to which he would have been entitled had fair and proper payment and NIC practices been enforced from 1983 to 1998. However, suggestions along such lines had been brushed aside by the respondents, who insisted that since payment of all NICs lawfully due had already been received there could be no question of reopening any calculation at this stage.

[5] On 16 July 2007, the respondents issued a Notice of Decision which bore to confirm that between 1983 and 1998 the appellant had paid all primary NICs lawfully due, namely a total of £12,156.69. This was challenged by the appellant before the Special Commissioners and latterly before the First Tier Tribunal which succeeded them under the Tribunals, Courts and Enforcement Act 2007. After sundry procedure, the Tribunal rejected the appellant's challenge, holding that the correct amount of primary NICs had been deducted in terms of the regulations applicable from time to time.

[6] It is against that determination that the present appeal is now taken pursuant to section 11 of the 2007 Act. The main contentions advanced by the appellant before us were to the effect (i) that the First Tier Tribunal had erred in law, and had in particular acted contrary to the evidence, in holding that all NICs were correctly calculated by reference to fortnightly pay periods which were artificial and unjust; (ii) that in any event some of the primary NICs deducted were demonstrably wrong to a degree which called for upward revision of the appellant's SERPS pension; and (iii) that on a proper construction of relevant regulations the Secretary of State (and subsequently the respondents) could and should have taken action to rectify a glaringly unfair situation.

[7] What the appellant really wanted was for this Tribunal to substitute monthly, or four-weekly, pay periods for the fortnightly periods of which he complained. This should, he contended, have been achieved if the Secretary of State had acted properly at the time, but in any event the desired end result was consistent with "the most regular payment of all", namely the monthly crediting of a 4 per cent deduction from salary to the appellant's pension account. It was also supported by a variety of NIC-related discrepancies and anomalies which were evident from the payslips, bank statements, spreadsheets and comparisons produced. As a fallback position, the appellant maintained that such discrepancies and anomalies merited recognition in their own right as reflecting errors in the calculation of primary NICs from time to time. It is fair to say, however, that by comparison with a significant change in the applicable pay periods (which would be likely to have a major impact on his pension entitlement), the appellant showed rather less interest in the potentially unprofitable recognition of a limited range of calculation errors.

Discussion

[8] This is a somewhat unusual case, not least because of the form and nature of the decision by the First Tier Tribunal against which the present appeal is taken. That decision evolved over a period of some eight months (between October 2008 and June 2009), during which the appellant was given repeated opportunities to address a "difficult point" or "very difficult proposition" which, in the Tribunal's estimation, might potentially work in his favour. The thinking here was apparently that if the

"retainer" of £69 could be shown to have suffered NIC deduction in offshore fortnights, then its actual payment in onshore fortnights might somehow be ignored. When this ultimately came to nothing, the Tribunal proceeded to confirm its *interim* decision to the effect that the appellant's challenge to the calculation of his NICs was ill-founded and should be rejected on all grounds. There was, however, no detailed discussion of the appellant's "fallback" complaint that, even under a fortnightly regime, certain deductions had been wrongly calculated. As counsel for the respondent suggested, this may have been because, having continued the case for one very specific purpose, the Tribunal had not unreasonably considered all new materials submitted from that standpoint alone. Alternatively, as indicated by paragraph 12 of the final decision of June 2009, the Tribunal was simply unimpressed with calculation oddities "…that, at this distance in time, no-one can quite explain".

[9] Be that as it may, the Tribunal then went on to comment, at some length, on various matters which were acknowledged to be outwith its jurisdiction and on which no satisfactory evidence had been led, notably (i) the supposed origins and object of the pay practice of which the appellant complained; and (ii) the failure of the Secretary of State to exercise statutory powers of intervention in that regard. Both *interim* and final decisions (as well as associated directions) also included observations which were ostensibly designed to highlight the perceived nature and extent of the appellant's grievance; to assist him in the pursuit of a wider crusade elsewhere; and to encourage the respondents to consider the possibility of a negotiated settlement along non-statutory lines. To this end, particular stress was laid on the supposed unfairness of the appellant's having derived no benefit from the enhanced secondary NICs which were levied from his various employers following withdrawal of the relevant UEL in about 1986.

[10] For our part we are not disposed to speculate, without evidence, on the origins of the challenged pay practice which operated offshore in the North Sea between 1983 and 1998. Neither do we speculate or make assumptions as to whether this practice always disadvantaged the employees affected, bearing in mind that some may at the time have welcomed the opportunity to receive a higher gross pay which they might themselves invest. Equally it would in our view be inappropriate to speculate, without evidence, as to the reason or reasons why the Secretary of State did not at any stage exercise his discretion to review and reform the practice in question. In terms of the relevant regulations, the decision whether or not to intervene from time to time was one exclusively vested in the Secretary of State, and we can envisage no circumstances in which this Tribunal could have any legitimate input in that area. Along similar lines, we decline to comment on any possibility of a negotiated settlement of this dispute along non-statutory lines.

[11] As regards the issue of secondary (employer) NICs, we doubt whether the appellant can legitimately claim prejudice arising out of the removal, in about 1986, of any effective UEL. If, under the statutory scheme, the amount of any SERPS pension falls to be calculated by reference to primary (employee) NICs alone, then in our view the level of secondary contributions is strictly irrelevant. The amount of a SERPS pension would, in other words, be the same whether secondary contributions were subject to a UEL or not. The employer's liability could be halved or doubled without affecting pension levels, and we suppose that if anyone had a grievance here it might be an affected employer rather than someone in the appellant's position. In

the same context, we doubt whether there is any legitimate point to be made regarding possible benefit to the Treasury on receiving unrestricted secondary contributions since the legislative changes in 1986. Even if, without evidence, the existence and *quantum* of any such benefit could be positively affirmed, it is in our view hard to see how that might relevantly affect the appellant's claim to an increased SERPS pension in this case.

[12] Putting such extraneous matters to one side, we now turn to consider the main issues which were in dispute at the hearing of this appeal.

The statutory background

[13] For virtually the whole of the 15-year period to which this appeal relates, the relevant provisions were contained in the Social Security (Contributions) Regulations 1979 ("the 1979 Regulations"), as amended by S.I. 1984/77 with effect from 6 April 1984. Under these regulations a key concept was the "earnings period"; that in turn depended on the identification of "regular intervals" at which an employed earner was actually paid; and broadly speaking it was the shortest of such intervals that would apply for NIC purposes.

[14] Regulation 3 (as amended) provided *inter alia* as follows:

> "*3(1) Where any part of [earnings paid to or for the benefit of an earner in respect of an employed earner 's employment] … is normally paid or treated under regulation 6 … as paid at regular intervals, the earnings period in respect of those earnings shall, subject to the provisions of paragraphs (2), (2A), (3) and (4) … be the period –*
>
> *(a) the length of which is –*
>
> *(i) in the case where there is one regular interval of 7 days or more, the length of that interval;*
>
> *(ii) in a case where there are regular intervals of different lengths each of which is 7 days or more, the length of the shorter or, as the case may be, shortest interval;*
>
> *(iii) in the case where the regular interval is less than 7 days or where there is more than one such interval, a week;*
>
> *(iv) in a case where there is one or more than one regular interval of 7 days or more and one or more than one regular interval of less than 7 days, a week,; and*
>
> *(b) which is one of a succession of periods of the same length beginning in the case of the first such period in any year on the first day of that year, and in the case of each subsequent period immediately upon the ending of the period which last precedes it.*
>
> *……* "

[15] The pre-1984 form of regulation 3(1)(a) did not expressly cater for a case where "parts" of an employed earner's earnings were paid at regular intervals but those regular intervals were themselves of different lengths. However, the focus was still on the shortest identified interval at which earnings were paid. In both amended and unamended forms, therefore, the regulation catered for circumstances where an employed earner's earnings were paid in "parts" at regular intervals. The nature and

quality of such "parts" (for example basic salary, overtime, holiday pay or pension contributions) did not matter: the question was simply whether earnings were *de facto* paid in "parts" and, if so, at what intervals.

[16] So far as relevant for present purposes, regulations 19, 21 and 22 further provided as follows:-

> *"19(1) For the purposes of earnings-related contributions, there shall be excluded from the computation of a person's earnings in respect of any employed earner's employment any payment in so far as it is –*
>
> *……*
>
> *(f) any payment of earnings in respect of employed earner's employment which a secondary contributor is required to make under regulation 3(2)(e) of the Occupational Pension Schemes (Recognition of Schemes)(No 2) Regulations 1973;*
>
> *(g) any payment by way of a pension;*
>
> *……*
>
> *21(1) The provisions of this regulation shall not apply for the purpose of any decision of the Secretary of State in so far as that decision relates to contributions based on payments made more than one year before the beginning of the year in which that decision is given.*
>
> *(2) With a view to securing that liability for the payment of earnings-related contributions is not avoided or reduced by a secondary contributor following in the payment of earnings any practice which is abnormal for the employment in respect of which the earnings are paid (hereinafter referred to as an "abnormal pay practice"), the Secretary of State may, if he thinks fit, determine any question relating to a person's earnings-related contributions where any such practice has been or is being followed, as if the secondary contributor concerned had not followed any abnormal pay practice, but had followed a practice or practices normal for the employment in question.*
>
> *……*
>
> *22 Without prejudice to the last preceding regulation, the Secretary of State may, where he is satisfied as to the existence of any practice in respect of the payment of earnings whereby the incidence of earnings-related contributions is avoided or reduced by means of irregular or unequal payments, give directions for securing that such contributions are payable as if that practice were not followed."*

The earnings period issue

[17] Against that background, the first question for determination is whether a fortnightly earnings period or pay interval was the correct basis on which to calculate all of the appellant's NICs between 1983 and 1998. According to him it was not, and even without intervention by the Secretary of State the available evidence made it clear that a monthly pay period was the only viable conclusion. At certain points, NIC deductions appeared inconsistent with a fortnightly pay period; some fortnightly payments related to periods longer or shorter than 14 days; holiday pay and other extras sometimes appeared in fortnights to which they did not relate; and it was said

to be significant that the crediting of pension contributions had taken place on a strict monthly footing.

[18] In reply, counsel for the respondents submitted that the appellant had failed to demonstrate any error of law on the part of the First Tier Tribunal, and in particular had failed to displace the fortnightly pay periods which, on the evidence, the Tribunal had been entitled to affirm. Even if (which was not admitted) calculation errors could be identified from time to time, that could not and did not affect the pay periods on which earnings limits and calculations depended. Fortnightly payments were confirmed by the appellant's own bank statements, and also by virtually all of the payslips which he had been able to produce. If payments of salary were actually made and received at such intervals, it could not matter how many working days might be reflected in each of them. Nor could it matter whether individual payments included holiday pay, travel, accommodation or course fees, nor indeed whether pension deductions were processed immediately or after a delay. All in all, it was open to the Tribunal to reach the conclusion it did, and the appellant had failed to show otherwise.

[19] In our judgment the respondents' argument here is clearly to be preferred. The appellant very fairly conceded that, in general terms, he worked (and was paid) on a "two weeks on, two weeks off" basis throughout his years of employment offshore. This was confirmed by his own bank statements covering much of the period between January 1994 and June 1998 (productions A578-A631, some of which were duplicated elsewhere). Fortnightly pay periods, including the deferred "retainer" of £69, were also borne out by payslips relative to various periods between November 1991 and October 1997 (productions A634-A644), and the only available contract of employment (production 74/5, dating back to 1993) was silent on the matter. *Prima facie*, therefore, the appellant's own evidence appears to us to prove, rather than disprove, the fortnightly pay periods by reference to which his NICs were calculated.

[20] The fact that some fortnightly payslips may have related to 5 or 16 days work (productions A641 and A643) cannot in our view be thought sufficient to disturb that conclusion, bearing in mind that regulation 3 of the 1979 Regulations is clearly concerned with normal payment intervals and not with periods worked. Similarly, the fact that extras such as holiday pay, travel and subsistence, course fees and incentive bonuses may have been credited in an offshore or onshore fortnight cannot in our view have any effect on the length of the relevant pay interval or earnings period. Even where only one week's NICs may appear to have been deducted in a given fortnight (for instance on payslip A643), we are again unable to see how this could have had the effect of altering the fortnightly pay periods as such, especially where preceding or succeeding payslips were missing (so that the full pattern of payments could not be ascertained) or where a given deduction occurred at the beginning or end of a tax year. And although two isolated payslips from 1988 (productions A632-A633) may appear to contain no reference to deduction of a "retainer", we are not persuaded that any relevant inference can be drawn from that fact alone. Different employers might deal with fortnightly payments in different ways; none of the adjacent payslips was available for scrutiny; the payments in question might have been intermediate (i.e. between fortnights), as sometimes happened in later years; and in the whole circumstances we are unable to regard these payslips as having the evidential significance for which the appellant contended.

[21] As the appellant himself described to us at the hearing, there might be many reasons for an apparent excess or shortfall on any given payslip. Sickness, unpaid leave or weather delays might reduce earning capacity, whereas extra work, bonuses and other additional payments might augment payments received. The documentary evidence confirmed significant variations in both offshore and onshore fortnightly payments, and against that background we are not persuaded that any legitimate inference can be drawn from the bare annual figures brought out in P14 certificates. A number of such certificates (productions A557-A577) were used by the appellant in the preparation of spreadsheets A653/4, but for the reasons given we cannot accept that this exercise is entitled to much weight. It was, in any event, an attempt to show that secondary NICs had been deducted monthly on the appellant's whole salary including the £69 "retainer", but as the appellant very fairly conceded at the hearing the figures "…did not really add up to what he was trying to prove".

[22] Taking all of these considerations into account, we have no reason to think that the First Tier Tribunal's conclusion on earnings periods was unsound or tainted by any error of law. On the available evidence this was a conclusion which, in our opinion, the Tribunal was well entitled to reach. The appellant's earnings were clearly paid in "parts", and on a straightforward application of regulation 3(1)(a)(i) such "parts" were paid at "regular intervals" of 2 weeks.

[23] Even the pensions deduction argument, on which the appellant placed some emphasis and which he sought to clarify after the hearing, does not seem to us to cast any doubt on the matter. For NIC purposes it might perhaps be argued that pension contributions should be excluded from any computation of the appellant's earnings in terms of regulation 19(1)(f) or (g) of the 1979 Regulations. But even if that were not so (and we heard no submissions on the matter), the payslips appear to show that the 4 per cent pension contributions formed part of the salary which suffered NIC deduction in both offshore and onshore fortnights, thereby tending to confirm the fortnightly pay regime which the appellant sought to challenge. Alternatively, if applying pension contributions to the appellant's account on the 6^{th} of each month were to be classed as intermediate payments of salary, then payment intervals (and hence the appellant's "earnings period") would appear to be shortened even further. On no view could we regard these arrangements as justifying the substitution of a monthly pay regime instead. Significantly, perhaps, one of the tests suggested by the appellant ("the most regular of all pay intervals") bore no relation to the actual terms of regulation 3 of the 1979 Regulations, and to our mind the notion of a monthly cycle of irregular payments does not sit easily with the evidence of a fortnightly pay regime to which we have referred.

Simple miscalculations

[24] At one point during the hearing it seemed to us that the appellant's arguments in this regard might have some merit. However, the sums involved would have been small; there could in our view be no question of isolated errors being extrapolated across wider periods for which no evidence was produced; and accordingly any such errors would have been unlikely to have a material effect on the level of the appellant's SERPS pension. As the hearing progressed, however, it became clear that there were no calculation errors which we could properly sustain. Even for 1997/8, where bank statements and many payslips were available, we consider that the

evidence fell short of demonstrating that errors were in fact made. By way of illustration, adjacent single-week primary NICs may readily be equated with the "correct" deduction of two weeks' NICs in one fortnight followed by Nil in the next. Moreover, as already explained, we cannot attach significance to isolated one-week deductions where adjacent payslips were missing, or where these occurred at the beginning or end of a tax year. Similarly, for reasons already discussed, we are unable to identify relevant calculation errors from the appellant's spreadsheets based on P14 certificates, nor from isolated payslips from 1988, nor indeed from the payslip from 1992 (A637) which was said to show holiday pay credited, at an intermediate date, without NIC deduction.

[25] Before the First Tier Tribunal, arguments alleging miscalculation of NICs appear to have come forward at a late stage when the focus was on one outstanding issue concerned with earnings periods. Nevertheless, these arguments were briefly dealt with at paragraph 12 of the final decision, and having reviewed the evidence we are not persuaded that the Tribunal was guilty of any error of law in that regard.

Secretary of State's discretion

[26] For the reasons previously given, we see no merit in the appellant's attempts to rely on regulations 21 and 22 of the 1979 Regulations. These conferred on the Secretary of State, and on him alone, an unfettered discretion to counteract abnormal pay practices if he chose. Unfortunately for the appellant that power was never exercised, and we cannot see any basis on which the First Tier Tribunal, or indeed this Tribunal on appeal, could competently purport to exercise, or to direct anyone else to exercise, such a power now. A further difficulty for the appellant here is that the power under regulation 21 could not be exercised retrospectively beyond one year, and the power under regulation 22 would appear to be forward-looking. Once again, therefore, the appellant's contentions must be rejected.

Conclusion

[27] On the whole matter, and taking all of the above considerations into account, we have reached the conclusion that this appeal must be refused. The appellant presented his arguments before us with commendable restraint and fairness; he provided us with a clear explanation of the sense of grievance which led him to institute Tribunal proceedings in the first place; but in the end he was unable to persuade us of any error of law by the First Tier Tribunal which alone might have justified a conclusion in his favour.

THE HON LORD EMSLIE

JULIAN GHOSH QC
TRIBUNAL JUDGES

RELEASE DATE: 22 June 2010