



EMPLOYMENT TRIBUNALS

BETWEEN

Claimant
MR G RYBICKI

AND

Respondent
AERO ENGINEERING LTD (IN
CREDITORS VOLUNTARY
LIQUIDATION) (R1)

THE SECRETARY OF STATE
FOR BUSINESS AND TRADE (R2)

JUDGMENT OF THE EMPLOYMENT TRIBUNAL

HELD AT: BRISTOL ON: 8TH MARCH 2024

EMPLOYMENT JUDGE MR P CADNEY
(SITTING ALONE)

MEMBERS:

APPEARANCES:-

FOR THE CLAIMANT:- IN PERSON

FOR THE RESPONDENT:- MS J WHALLEY

JUDGMENT

The judgment of the tribunal is that:-

1. The claimant was not at the date of the insolvency an employee of Aero Engineering Ltd (in Creditor's Voluntary liquidation (R1)) within the meaning of s230 Employment Rights Act 1996.
2. The claimant's claim that the Secretary of State (R2) is liable to make payments to him pursuant to s166/182 Employment Rights Act 1996 is not well founded and is dismissed.

Reasons

1. By this claim the claimant brings claims against R1 for a statutory redundancy payment, notice pay, unpaid wages and unpaid holiday pay. He asserts that he was an employed director. It has not entered a response, and has not participated this hearing. It is however, in creditor's voluntary liquidation and has no assets and could not therefore meet any judgment entered against it.
2. He also pursues the claims against the Secretary of State (R2) for payments from the National Insurance Fund pursuant to s166/182 of the Employment Rights Act 1996. R2 accepts that R1 is insolvent within the meaning of those sections but disputes liability on the basis that the claimant was not an employee of R1.
3. The only dispute being pursued and determined in this hearing is that between the claimant and the Secretary of State (SoS).
4. The claimant and SoS have agreed that I should decide the issue in principle of whether the claimant was an employee of the first respondent, and if so the parties will seek to agree any amounts owed. This arises from the claimant's acceptance in cross examination that the information supplied to the SOS by him, particularly in relation to sums received from AEL was inaccurate in some respects and clarification would be needed.

Facts

5. The claimant provides consultancy services to the aerospace industry, including in depth organisational analysis and recommendations. He set up the first respondent Aero Engineering Ltd (AEL) on 4th September 2013 for the purposes of supplying those consultancy services. He was the sole shareholder, sole director, and sole employee of the company. As a result of the requirement for consultancy services diminishing during the covid 19 pandemic and associated lockdowns AEL entered into creditor's voluntary liquidation on 21st September 2022.
6. The claimant made an application to the Secretary of State (SoS) for statutory payments pursuant to s166/182 ERA 1996 which were rejected on the basis that the claimant was not an employee of AEL.
7. The claimant's evidence is that the both the incorporation of AEL and the terms of his employment, were on the advice of his accountant. He was advised to become an employee of the company and pay himself a modest salary which would allow him to take any further profits as dividends in the event the company was successful. On 24th September 2013 he entered into a Director's Service Agreement. It provided that:
 - i) He was an employee with the title Director (Clause 2);

- ii) He was not permitted to undertake “..work outside the company, which in the reasonable opinion of the Board, may interfere with the proper performance of your duties..” (Clause 5);
 - iii) His salary was initially £7,950 per annum (Clause 6);
 - iv) His hours of work were 9.00 am- 5.00pm Monday – Friday (Clause 8);
 - v) He was entitled to 68 days annual leave (Clause 10)
8. The most recent P60s show income from employment of £9498.84 (2021), and £9562.80 (2022). The balance of income taken from AEL was taken when possible in the form of dividends. The claimant accepts that his salary as an employee equates to approximately £5.00 per hour and that at all stages during his employment he was paid below the national minimum wage. He states he was not advised by his accountant that the company had any obligation to pay the national minimum wage to him as an employee.
9. His employment with the company was primarily for the purpose of fulfilling consultancy contracts it had entered into, in the main with Rolls Royce; and attempting to obtain further consultancy contracts ,
10. The basis for his being granted 68 days annual leave was that the pattern of consultancy work normally left gaps between contracts which would be used as annual leave.
11. As is obvious that the only person who could control or direct his work was himself; the only person who could discipline him, if for example he failed to attend work during normal working hours, was himself; and equally the only person who could hear any grievance was himself. The claimant accepts this, and gave evidence that it felt very odd sending himself a letter placing himself on furlough during Covid 19 lockdown.
12. Because of the drop off in work the claimant obtained paid employment with In-Space Missions Ltd from 5th July 2021. He accepted that this was full time employment in a Project Manager role with a standard 37 hour week. He was asked how he could simultaneously be employed full time by both In-Space Ltd and AEL he stated that he had no work through AEL and that in his spare time he continued to seek contracts for AEL without success which resulted in the CVL in September 2021.

Secretary of State's Liability

13. The liability of the Secretary of State to make any payment derives from the Employment Rights Act 1996 as set out below:
- i) Section 166 of the Employment Rights Act 1996 (“ERA”) provides:

s166 Applications for payments.

(1) 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.

(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.

...

ii) Section 182 of the ERA provides:

182 Employee's rights on insolvency of employer.

If, 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.

iii) Section 184 of the ERA applies section 182 to arrears of pay; accrued holiday pay and statutory notice pay (but subject to maximum amounts).

iv) For the Secretary of State to be liable the Claimant must be an employee:

S. 230 of the Employment Rights Act 1996 provides

“230 Employees, workers etc

(1) In this Act “employee” means an individual who has entered into or works under (or, where the employment has ceased, worked under) a contract of employment.

(2) In this Act “contract of employment” means a contract of service or apprenticeship, whether express or implied, and (if it is express) whether oral or in writing.

(3) In this Act “worker” (except in the phrases “shop worker” and “betting worker”) means an individual who has entered into or works under (or, where the employment has ceased, worked under)—

(a) a contract of employment, or

(b) any other contract, whether express or implied and (if it is express) whether oral or in writing, whereby the individual undertakes to do or perform personally any work or services for another party to the contract whose status is not by virtue of the contract that of a client or customer of any profession or business undertaking carried on by the individual;

and any reference to a worker's contract shall be construed accordingly.

(4) In this Act “employer”, in relation to an employee or a worker, means the person by whom the employee or worker is (or, where the employment has ceased, was) employed.

(5) In this Act “employment”—

(a) in relation to an employee, means (except for the purposes of section 171) employment under a contract of employment, and

(b) in relation to a worker, means employment under his contract; and “employed” shall be construed accordingly.”

Employment Status – General

14. The s230 definition distinguishes between “employed” individuals on the one hand, and self-employed individuals, or independent contractors, on the other; that is between those working under a “contract of service” and those working under a “contract for services”. However, the statute does not set down the circumstances in which an individual may be said to work under a contract of employment.

15. In the absence of any comprehensive definition of a contract of employment, courts and tribunals have developed a number of tests over the years aimed at helping them

identify such a contract. It is now accepted that no single factor will be determinative of employee status and a number of factors must be looked at.

16. There are three essential elements which must be present in every contract of employment. They are frequently referred to as the 'irreducible core' without which a contract cannot be regarded as a contract of service, taken from MacKenna's judgment in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 1 All ER 433, QBD. They are:
- a. There must have been an obligation for the Claimant to have provided the work personally;
 - b. There must have been mutuality of obligation;
 - c. The Claimant must have been expressly or impliedly subjected to the control of the Respondent.

Personal service

17. With regards to the first element, even if the contract contained a limited power to delegate, there may still have been the obligation present for the employee to have provided work personally, but where there was a clear express contractual term which did not impose personal obligations, that would ordinarily militate against an employment relationship unless it was a sham or had been varied (*Staffordshire Sentinel-v-Potter* [2004] IRLR 752).

Mutuality of obligation

18. With regards to the second element, an employer and an employee must have been under legal obligations to one another during the entire contractual period under focus. Ordinarily, the obligations will have been upon the employee to undertake work when required/asked and upon the employer to have paid for it. Casual workers ordinarily fall outside of the ambit of this principle (*Carmichael-v-National Power* [2000] IRLR 43). Further, where the express terms of a contract made it clear that such obligations did not exist, there cannot have been an employment relationship. Gaps between assignments were just as relevant as the assignments themselves when considering all of the circumstances (*Sec of State for Justice-v-Windle* [2016] EWCA Civ 459).

Control

19. Finally, the employer must have had a sufficient degree of control, in terms of the general sense of authority exercised over an employee, for such a relationship to have existed. 'Control' in this sense was not to have been equated to the undertaking of work under close supervision.
20. If the three essential elements were present, the relationship can have been one of employment, but it was also necessary to consider all of the other surrounding

circumstances to finally determine its true nature. Those circumstances can include the degree of personal financial risk, the extent to which the individual provided his/her own equipment, whether the claimant was paid holiday and/or sick pay and whether he/she paid their own tax and national insurance or whether that was achieved through PAYE. There were many different factors that *could* have been relevant.

Sham arrangements

21. A number of cases are relevant to a consideration of situations in which a party alleges that the contractual documentation was a sham and did not reflect the reality of the parties' relationship in law; *Autoclenz Ltd v Belcher and Others* [2010] IRLR 70 CA and [2011] UKSC 41; *Consistent Group Ltd v Kalwak* [2008] IRLR 505 CA; *Firthglow Ltd (t/a Protectacoat) v Szilagyi* [2009] ICR 835 CA and *Snook v London and West Riding Investments Ltd* [1967] 2 QB 786].

22. For the reasons set out below I have not concluded in this case that the agreement was a sham, and it is not necessary to set the authorities out in detail.

Employment Status - Directors and Shareholders

23. The position of shareholders and/or directors has been considered in a number of cases. The former view 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 for Employment* [1997] IRLR 80 EAT in which the Claimant was the managing director and a 50% shareholder, but was not deemed to have been an employee).

24. However, in *Neufeld v Secretary of State for Business Enterprise and Regulatory Reform* [2009] IRLR 475, 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. 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 investigation into the circumstances 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)

25. In *Eaton v Robert Eaton Ltd v Secretary of State for Employment* [1988] IRLR 83, it was ruled that a director of a company is normally the holder of an office and not an employee. Therefore evidence is required to establish that the director was in fact employed.

26. In *Fleming v Secretary of State for Trade and Industry* [1997] IRLR 682, 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).

27. In *Rainford-v-Dorset Aquatics Ltd* EA-2020-000123-BA, UKEAT/0126/20/BA, 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."

28. 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.

29. In *Secretary of State for Trade and Industry-v-Bottrill* [1999] ICR 592, CA, (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?
30. In *Clark-v-Clark Construction Initiatives Ltd* [2008] ICR 635, EAT, the list was broadened to include some of the further following factors; Whether the individual was an entrepreneur and/or had built the company up and/or would profit from its success. It was also held that there were three sets of circumstances where it may be legitimate to not give effect to what is alleged to be a binding contract of employment: (1) where the company is a sham, (2) where the contract is entered into for some ulterior purpose, such as to secure some statutory payment from the secretary of state, and (3) the parties had not conducted their relationship in accordance with the contract.
31. In *Rajah v Secretary of State for Employment* EAT/125/95, 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.

Respondent's Submissions

32. The respondent submits that there are a number of features of the evidence which are contra-indications of employment status. It accepts that none are individually determinative or conclusive but submits that when taken together they do not reveal a genuine employment relationship:
- i) Payment of salary below national minimum wage rate. This is compatible and consistent with remuneration as an office holder, but not genuine employment status.
 - ii) The claimant received no pay for at least some of the six months from April – October 2021, and the claimant's acceptance of a zero pay arrangement is inconsistent with employment status (As set out above it was accepted in evidence the precise amounts received are not entirely clear or consistent).
 - iii) The claimant was not in reality subject to any control as the sole shareholder, director and employee.
 - iv) That as at the date of insolvency, and for some time prior to insolvency, the Director's Service Agreement did not genuinely reflect the position of the parties.

Claimant's Submissions

33. The claimant submits that :

- i) The contract of employment was entirely genuine;
- ii) The division between salary and dividend has been accepted by HMRC and he has been assessed for tax and national insurance by HMRC on the basis that he was an employee in relation to part of the income derived from the company.
- iii) He received holiday pay and sick pay in accordance with the contract of employment, which is not consistent with the contention that his relationship with AEL was solely in his capacity as director/shareholder. .

Conclusions

34. I accept the claimant's evidence as to how and why he entered into a contract of employment and I am satisfied that it was not a sham.

35. However, that does not in and of itself resolve the question of whether it was genuinely a contract of employment (see Bottrill - para 29 above).

36. As is set out above the irreducible minimum of a contract of service/employment contract are personal service, mutuality of obligation, and control.

37. In my judgment it is clear that:

- i) The contract required personal service in that the claimant was the sole employee and it was his consultancy expertise that the company was supplying;
- ii) There was mutuality of obligation in that the claimant was obliged to supply his services and the respondent was required, insofar as it was able to, to provide him with work.

38. Before dealing with the element of control the claimant's submission, as set out above, is essentially that the contract was entirely genuine, and that he had acted in accordance with it and with his accountant's advice. Whilst the element of control is necessarily artificial where he is the sole shareholder, director and employee; that does not in and of itself prevent it from being a contract of employment and will always be true of one man companies, particularly, as in this case, a service company whose only purpose is the provision of the services of the individual.

39. However, in my judgment the third element, control, is much more difficult for the claimant. As is set out above the claimant was the sole shareholder, sole director and sole employee. There was literally no one other than himself to exercise any control and it must follow, in my view and in reality that here was no control over him. However, I accept that this necessarily always true of one man companies, and that

there is no principle of law or fact that that employees of one man companies cannot be genuinely employed. In the particular circumstances of this case this factor is not in and of itself determinative.

40. It follows that it is necessary to look at other factors to determine whether as it was operated in practice it was genuinely a contract of employment, and in particular whether that was true as at the date of insolvency. This raises two questions. The first is whether as it was operated prior to the last few months prior to the insolvency the contractual relationship was genuinely an employment relationship; and the second is whether that relationship changed.
41. In relation to the first in my judgement the question is whether the combination of the lack of control and the fact that AEL failed to pay the minimum wage are, taken together, sufficient to indicate that this was not a genuine employment relationship. In my judgment the fact neither AEL nor the claimant at any point considered whether the claimant as an employee was entitled the national minimum wage and if so whether he was receiving it, indicates that neither, which in practice means the claimant himself, considered this a standard employment relationship with one of the most basic features of an employment contract. In my judgment the combination of this and the lack of control is sufficient to conclude that this was not a genuine employment relationship.
42. In case I am wrong in that conclusion, and if in reality the relationship was originally a genuine employment relationship, I have gone on to consider the second question.
43. In my view there are two factors which militate against the conclusion that by the date of the insolvency that there was a genuine employment relationship and/or that the relationship created by the Director's Service Agreement still represented the genuine relationship. Firstly, for some six months prior to the insolvency the claimant chose not to pay himself a salary, and in his capacity as an employee to accept non-payment. Secondly he took alternative employment in July 2021 which necessarily prevented him from carrying out his duties for AEL, at least within his contractual hours, but with no consequence. Put simply for the last three months prior to the insolvency he provided no services to AEL and received no salary from AEL for at least some of those months; and was employed full time by another company. In those circumstances it is in my judgement impossible to conclude that at the point of the insolvency that the relationship between him and AEL was genuinely governed by or reflected in the Director's Service Agreement.
44. For the reasons set out above I am not satisfied that the contract was a genuine contract of employment within the meaning of s230 ERA 1996.
45. It follows that the claimant has not established in principle that the SOS is liable to make the payments sought and his claims must be dismissed.

Employment Judge Cadney
Dated: 15th March 2024

Judgment sent to the parties on 08 April 2024

For the Tribunal Office