SLAUGHTER AND MAY

Pensions and Employment: Employment/Employee Benefits Bulletin

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For more information, or if you have a query in relation to any of the above items, please contact the person with whom your normally deal at Slaughter and May or Clare Fletcher

New Law

Finance Bill (no.2) 2017: Employment aspects

The Finance (No 2) Bill 2017 was published on 8th September 2017, along with explanatory notes. The Bill includes the employment-related income tax provisions which were dropped from the first Finance Bill 2017. The effect of these clauses is as follows:

- Clause 5 introduces amendments to the income tax treatment of **termination payments**. The key points are:
    - all payments in lieu of notice (PILONs) will be taxable as earnings, not just contractual PILONs;
    - all employees will pay tax and Class 1 NICs on the amount of basic pay that they would have received if they had worked their notice in full, even if they are not paid a contractual PILON;
    - the existing £30,000 income tax exemption will be retained, and there will continue to be an unlimited employee NICs exemption for payments associated with the termination of employment;
    - however, employer NICs will be payable on any amount over the £30,000 exemption; and
    - the tax exemption for termination payments in respect of 'injury' will be amended to exclude 'injury to feelings' awards.

  These measures will apply from the tax year 2018-19.

- Clause 1 introduces a date for **'making good' on benefits in kind** which are not accounted for in real time through Pay As You Earn (PAYE). The date is 6th July following the end of the tax year in which the tax liability of the benefit in kind arises. The date will have effect for benefits in kind which give rise to a tax liability from the tax year 2017-18.

- Clause 2 amends the appropriate percentage for **ultra-low emission vehicles** (cars with CO2 emissions of 0-75 grams per kilometre) for the purpose of calculating the taxable benefit of a company car, and also makes related changes to the appropriate percentage for conventionally fuelled cars. The changes will have effect from the tax year 2020-21.

- Clause 3 introduces a new income tax exemption to cover the first £500 worth of **pensions advice** provided to an employee (including former and prospective employees) in a tax year. It will allow advice not only on pensions, but also on the general financial and tax issues relating to pensions. The exemption will apply from the tax year 2017-2018.

- Clause 4 extends existing reliefs for employees (or former employees) who may require **legal advice or indemnity insurance** which is funded by their employer, to apply in relation to proceedings where no allegation has been made or is expected to be made against the employee. Reliefs are also extended in relation to individuals on termination of employment. The extended relief will be available to legal expenses incurred from 6th April 2017.

Separately, the government has published new draft legislation to abolish foreign service tax relief on termination payments. It is intended that this will be included in a new Finance Bill 2018, which will be published after the Autumn Budget on 22nd November 2017.

The Finance (no.2) Bill had its second reading on 12th September. The Committee stages of the Bill are expected to start shortly after 9th October 2017, when the House of Commons returns from its conference recess.

Cases Round-up

ECtHR: Monitoring of employee's emails breached right to privacy

An employer's monitoring of an employee's work emails amounted to a violation of Article 8 (right to respect for private and family life, the home and correspondence) of the European Convention on Human Rights (ECHR), according to a recent judgment of the Grand Chamber of the European Court of Human Rights (ECtHR). It overturned a previous decision that the employer's actions did not violate Article 8 (as reported in our Bulletin dated 11th February 2016) (*Bărbulescu v Romania*).

Workplace communications: B was employed by a Romanian company (S) as an engineer in charge of sales. At S's request, B created a Yahoo Messenger account for the purpose of responding to clients' enquiries. On 3rd July 2007, S informed its employees that one employee had been dismissed after she had privately used the internet.

Monitoring: S decided to monitor B's Yahoo accounts between 5th and 12th July. It found that B had been using the Yahoo Messenger account for personal purposes, to send messages to his fiancée and his brother. B denied using the account for personal purposes and S therefore presented him with a 45 page transcript of his personal emails, which related to intimate subjects including B's health and sex life.

Dismissal and claim: On 1st August S terminated B's employment contract for breach of S's internal regulations that prohibited the use of company resources for personal purposes. B unsuccessfully challenged his dismissal before the Romanian courts, which found that S had complied with the relevant dismissal proceedings, had been entitled to set rules for the use of the internet, and had informed B of those rules.

Privacy complaint: B appealed to the ECtHR, arguing that S's decision to terminate his contract after monitoring his electronic communications and accessing their contents was in breach of his privacy, and that the Romanian courts had failed to protect his right to respect for his private life and correspondence under Article 8 EHRC. In its initial judgment, the ECtHR held that there had been no violation of Article 8 ECHR, and that the domestic courts had struck a fair balance between B's Article 8 rights and S's interests (see our Bulletin dated 11th February 2016 for further details).

Privacy at work: The Grand Chamber of the ECtHR allowed B's appeal. It confirmed that, although it was questionable to what extent B could have had a reasonable expectation of privacy, in view of S's restrictive regulations on internet use (of which he had been informed), "*an employer's instructions could not reduce private social life in the workplace to zero. The right to respect for private life and for the privacy of correspondence continued to exist, even if these might be restricted in so far as necessary.*"

Balance not struck: The ECtHR found that the Romanian courts had not struck the right balance between B's right to respect for his private life, and S's right to take measures in order to ensure the smooth running of the company. It noted in particular the following points:

- B had not been informed in advance of the extent and nature of the monitoring, or the possibility that S might have access to the actual contents of his messages. The ECtHR confirmed that, in order to qualify as prior notice, the warning from an employer had to be given before the monitoring was initiated, especially where it entailed accessing the contents of employees' communications. In this case, employees were simply told, shortly before B's disciplinary sanction, that one of their colleagues had been dismissed for using the internet for personal purposes.

- In addition, the degree of intrusion into B's privacy was significant, since S had recorded all of B's communications during the monitoring period in real time and had printed out their contents.

- The Romanian court had failed to determine whether there had been any legitimate reasons justifying the monitoring. It had referred to the need to avoid S's IT systems being damaged, or liability being incurred by S in the event of illegal activities online. However, these examples could only be seen as theoretical, since there was no suggestion that B had actually exposed S to any of those risks.

- The Romanian court had also not sufficiently examined whether the aim pursued by S could have been achieved by less intrusive methods than accessing the contents of B's communications. It had also not considered the seriousness of the consequences of the monitoring and the subsequent disciplinary proceedings, namely the fact that S had received the most severe disciplinary sanction.

Implications for UK employers: This judgment should not require a step change in how UK employers approach monitoring of employee communications. Many of the points made by the ECtHR in terms of advance notification of monitoring and the limitations on monitoring already apply in the UK, whether under the Data Protection Act 1998, the Regulation of Investigatory Powers Act 2000 or the Information Commissioner's Employment Practices Code. These principles are maintained under the General Data Protection Regulation (GDPR), which imposes strict notification requirements which employers must comply with before processing employee data. For further details, see our briefing: What do employers in the UK need to know about the new General Data Protection Regulation (GDPR) from an employment perspective?

In practice, this means that:

- Employers cannot entirely deny any right to privacy for employees using work computer systems, no matter how clear and well-communicated the policy is.
- Employers must therefore ensure that they approach any monitoring of employee's communications with care, having a clear business rationale for doing so, and carrying it out in a reasonable manner.
- Any monitoring should be limited (in time and scope) to what is strictly necessary, and carried out in accordance with the employer's policy.
- The policy must be notified to employees in advance of the monitoring taking place.
- The policy should make it clear when or if personal use of the employer's communication systems may be permitted. It should also (if appropriate) make it clear that the contents of communications may be viewed.

TUPE: offshoring and redundancy

When an employer moves part of its UK business offshore, TUPE may apply to that transfer. However, it does not necessarily follow that UK employees have the right to transfer overseas on their UK terms and conditions, according to a recent judgment of the EAT (*Xerox Business Services Philippines Inc Ltd v Zeb*).

UK workplace: Z was employed by Xerox UK (XUK) as a Commercial Executive in a Finance Accounting Team in Wakefield. His contract provided for his work location to be "Leeds or Wakefield" with the proviso that XUK could require him to work at any other location within a reasonable commuting distance from his home.

Offshoring: In 2014, XUK's holding company decided to move the Finance Accounting Team function from XUK in Wakefield to another group company (XBSP) at Manila in the Philippines. It accepted that the offshoring would amount to a TUPE transfer. Affected employees were offered a choice: they could either object to the transfer and be made redundant by XUK on enhanced terms, or they could transfer to XBSP but would still be made redundant, and only with the statutory minimum redundancy pay (SRP). This was on the basis that XBSP would have no requirement to carry out the transferring work in the UK after the transfer. A Q&A issued to affected employees made it clear that XBSP would only consider employing transferring employees in Manila on local terms and conditions.

Transfer and dismissal: Z chose not to object to the transfer and claimed to be entitled to transfer to XBSP and work in Manila on his UK salary (which, at £26,000, was nearly ten times the local salary in Manila). XBSP refused to allow him to relocate on that basis, since it maintained it would defeat the point of the transfer (which was to make cost savings). Z was therefore dismissed nine days after the transfer, and was paid only SRP.

Unfair dismissal? The Tribunal upheld Z's unfair dismissal claim against XBSP. It found that XBSP had not established that redundancy was the true

reason for dismissal, since Z was willing to transfer to Manila. It also found that there had been an agreed variation of Z's contract as regards a change of workplace from Wakefield to Manila (as permitted by regulation 4(5) of TUPE), and that Z was entitled under TUPE to protection of his terms and conditions, including his salary.

No contract variation: The EAT allowed XBSP's appeal, finding that there was in fact no variation of Z's contract. At all material times, the term as to location was Wakefield. Z had no unilateral right to change that term to Manila. Z made it plain that he was seeking a change of location only if he retained his UK terms and conditions, but XBSP at no time accepted those terms. Therefore, there was never any valid variation of the contract.

No right to transfer on UK terms: The EAT clarified that under TUPE, XBSP was required, after the transfer, to employ Z at Wakefield and to pay his salary. It was not required to employ him in Manila at the same salary in the absence of a variation of the contract.

Redundancy? The EAT considered that XBSP had a strong case for saying that the dismissal was for an economic or organisational reason entailing changes in the workforce (for TUPE purposes) and that it amounted to redundancy (for unfair dismissal purposes). However, it decided that that conclusion involved some degree of factual assessment, which the Tribunal had failed to undertake. The case was therefore remitted to a different tribunal to determine what the reason for dismissal was and whether dismissal was fair.

Check the contract: This case is good news for employers, since it confirms that where a business is being transferred overseas, affected employees will only be able to transfer on their existing terms if the new location is within those existing terms, or if the new employer agrees to a variation of those terms. This emphasises the importance of assessing the contractual place of work, since this will be relevant both as regards whether the employees can be regarded as redundant, and whether they can insist on relocating on their existing salaries.

Dismissal which deprived employee of long-term disability benefits was unfair and discriminatory

Where an employee is in receipt of long-term disability benefits (LTDB) under his employment contract, he has an implied right not to be dismissed, save for good cause, in circumstances in which he would lose his entitlement to those LTDB. Dismissal in those circumstances may amount to both unfair dismissal and discrimination arising from disability under section 15 of the Equality Act 2010, as demonstrated by a recent EAT decision (*ICTS (UK) Limited v Visram*).

LTDB benefits: V was employed as a security agent at Heathrow Airport. V's contract of employment included entitlement to a LTDB plan, which was funded by an insurance policy. In October 2012, V went off on sick leave with work-related stress and depression. There was a dispute about V's LTDB and the insurance cover for them, but the benefits were ultimately provided to V.

Dismissal: In July 2014 V attended a medical capability hearing. He accepted that he could not foresee any circumstances where he would be able to return to his employment. As a result, V was dismissed on grounds of medical incapability in August 2014. V objected that his dismissal was in breach of the implied term not to deprive him of LTDB benefits. The Tribunal upheld his claim, and ICTS appealed.

Unfairness: The EAT dismissed the appeal. It confirmed that dismissal in breach of the implied term was outside the range of reasonable responses and therefore unfair. The EAT rejected an argument that V's long-term sickness could amount to "good cause" so as to avoid the implied term biting. It observed that if this were the case, it would render the implied term useless, since entitlement to LTDB are bound to be predicated upon a long-term absence from work. The EAT also found that ICTS had also conducted an inadequate investigation into whether V had the benefit of LTDB; it had assumed that benefits were only payable to V if they were covered by the insurance policy, but this was not the position under V's contract.

Discrimination: The EAT also held that ICTS could not justify its actions for the purposes of V's discrimination claim. It found that there was no legitimate aim for dismissing V, since there was no evidence that there was a real need to remove V from the payroll. There was no operational difficulty caused by his continued employment; his removal from the payroll was simply a tidying up exercise without real need. On the other hand, the discriminatory effect on V was

substantial. At a time when he was unfit to work, the dismissal denied him the benefit of the LTDB entitlements which amounted to a significant income.

Handle with care: This case is a reminder that dismissing an employee who is entitled to LTDB is a difficult process. Employers will need to make sure they have a clear justification for the dismissal, unrelated to the employee's ill-health, and that there is a clear reason why the employee cannot simply remain on the payroll.

The case also provides a salutary reminder that entitlement to LTDB under the employment contract should always be conditional on the provision of cover under the underlying insurance policy. Otherwise, as here, the employer will be obliged to provide the benefits itself. It is not clear why this was not weighed in the balance in ICTS' favour when the EAT considered the burden which it would face of keeping V on the payroll.

Points in practice

Corporate governance reforms: BEIS response to green paper

BEIS has published the response to its green paper on corporate governance reform. The key points to note are:

- **Pay ratios**: Listed companies will be required to report annually the ratio of CEO pay to the average pay of their UK workforce. Companies will also be required to publish a narrative explaining changes to that ratio from year to year, and setting the ratio in the context of pay and conditions across the wider workforce.

  The reporting requirement will (the response suggests) only cover UK employees, although multinational companies would be free to also publish a broader ratio covering all employees in their group.

  The government will give further consideration to the methodology for calculating the ratio, as well as including the option of reporting ratios by pay quartile. At this stage, the government proposes that the ratio should be calculated based on the CEO's total annual remuneration (as set out in the existing single figure in the Directors' Remuneration Report) relative to the average total remuneration of the company's UK workforce.

- **No additional binding votes**: The government has decided not to implement the green paper proposal for more binding votes by shareholders on companies' remuneration policies (which might have been triggered by a 20 per cent vote against the policy at an annual meeting).

- **Naming and shaming**: The government does however intend to introduce a public register of listed companies encountering shareholder opposition to executive pay and other resolutions of 20% or more, along with a record of what these companies say they are doing to address shareholder concerns.

- **Employee engagement**: The government has set out three proposals for reform to strengthen the voice of employees (as well as customers and wider stakeholders) in boardroom decision-making. It will:

  (i) require all companies of significant size (private as well as public) to explain how their directors comply with the requirements of section 172 of the Companies Act 2006 to have regard to employee and other interests;

  (ii) invite the Financial Reporting Council (FRC) to consult on the development of a new provision of the UK Corporate Governance Code (the Code) requiring premium listed companies to adopt one of three employee engagement mechanisms: a designated non-executive director; a formal employee advisory council; or a director from the workforce; and

  (iii) encourage industry-led solutions by asking ICSA and the Investment Association (IA) to complete their joint guidance on practical ways in which companies can engage with their employees and other stakeholders. The Government will also invite the GC100 group to complete and publish new advice and guidance on the practical interpretation of the directors' duties in section 172 CA 2006.

- **Greater transparency on outcomes from share incentive schemes**: Listed companies will also be required to provide a clearer explanation in remuneration policies of a range of potential outcomes from share-based incentive schemes.

- **No abolition of LTIPs**: The government "is not convinced" that the abolition of LTIPs is justified (as was proposed by the BEIS committee report in April 2017). The response notes that, provided they are "properly designed and set out", LTIPs can be a powerful tool in promoting long-term executive decision making.

- **Share buybacks**: The government will take forward its manifesto commitment to commission an examination of the use of share buybacks, to ensure that they cannot be used artificially to hit performance targets and inflate executive pay. The review will also consider concerns that share buybacks may be crowding out the allocation of surplus capital to productive investment.

- **Corporate governance of large privately-held businesses**: The government will introduce secondary legislation to require companies of a significant size to disclose their corporate governance arrangements in their directors' report and on their website, including whether they follow any formal code. This requirement will apply to all companies of a significant size unless they are subject to an existing corporate governance reporting requirement.

Next steps: The FRC will consult on the proposed amendments to the Code in "late Autumn" 2017. The government plans to lay draft statutory instruments before Parliament by March 2018, and consult on them "where necessary". The proposals are intended to be brought into force by June 2018, to apply to company reporting periods commencing on or after that date.

GDPR update: Consent and legitimate interests

The Information Commissioner's Office (ICO) has confirmed that it will publish its final form guidance on consent under the General Data Protection Regulation (GDPR) in December, to coincide with the issue of the EU Article 29 Working Party's consent guidance. The ICO has indicated that its final form is unlikely to change "significantly" from the draft issued in March (see our Bulletin dated 10th March 2017 for further details).

The ICO has also made it clear that consent is not the 'silver bullet' for GDPR compliance. The GDPR clarifies that pre-ticked opt-in boxes are not indications of valid consent, and specifies organisations must make it easy for people to exercise their right to withdraw consent. The requirement for clear, plain language when explaining consent is now strongly emphasised, and organisations must ensure the consent they already have meets GDPR standards. This is likely to be problematic in an employment context.

The ICO highlights that there are five other ways to lawfully process personal data, including the legitimate interests condition. It emphasises that organisations will need to document their decisions to be able to demonstrate to the ICO which lawful basis justifies the data processing. The ICO points to its existing guidance on legitimate interests (see ICO: Data Protection Guide: The conditions for processing) and states that there is no need to await further GDPR guidance, although this is expected from the Article 29 Working Party in 2018.

If you would like to discuss the impact of the GDPR on your employment practices, please speak to your usual Slaughter and May contact, or see our briefing: What do employers in the UK need to know about the new General Data Protection Regulation (GDPR) from an employment perspective?

New Vento injury to feelings bands

The Presidents of the Employment Tribunals for England and Wales and Scotland have published their joint response to the judicial consultation on awards for injury to feelings in discrimination claims. The revised *Vento* bands have been uprated to take into account both inflation and the 10% uplift required by *Simmons v Castle*. The revised figures, which are to be applied to claims lodged on or after 11th September 2017, are as follows:

- a **lower band of £800 to £8,400** (for less serious cases)

- a **middle band of £8,400 to £25,200** (for cases that do not merit an award in the upper band), and

- an **upper band of £25,200 to £42,000** (for the most serious cases), with the most exceptional cases capable of exceeding £42,000.

The Presidents will review and, if necessary, amend the Vento bands in March 2018 and annually thereafter. Any new rates will come into effect in respect of claims presented on or after 6th April in each year.

If you would like further information on these issues or to discuss their impact on your business, please speak to your usual Slaughter and May contact.

If you would like to find out more about our Pensions and Employment Group or require advice on a pensions, employment or employee benefits matters, please contact Jonathan Fenn or your usual Slaughter and May adviser.

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