
The Personal Tax Planning Review

THE RIGHT TO PAY IN LIEU OF NOTICE

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In *Abrahams v Performing Rights Society Ltd* (*The Times* 5th June 1995), the Court of Appeal recently considered a term of a contract of employment which permitted an employer to pay a sum of money "in lieu of notice". It was held that this was not a payment of damages for breach of contract but a payment provided for under the contract. As a result, there was no question of the employee being under a duty to mitigate his loss.

The Revenue currently argue that where the employee's contract of employment allows the employer to make a payment "in lieu of", in other words as an alternative to, giving notice to the employee, then any payment made under that provision is an emolument from the employee's employment. As a consequence, the payment is fully taxable and does not qualify for the £30,000 exemption which applies to payments which are only taxable under TA 1988 s.148.

The Revenue's argument is that this is a payment which is provided for in the employee's contract of employment and so it is an emolument on the principle set out in *Dale v De Soissons* (1950) 32 TC 118. In the normal case, the employer breaches the contract of employment by refusing to give the required notice. The payment which he makes (sometimes described as "in lieu of notice"), is really a payment of damages for breach of contract. Such a payment is not an emolument from the employment as it is paid because the employment has been brought to an end: see *Henley v Murray* (1951) 31 TC 351.

The Revenue's argument can only succeed if the term which allows the employer unilaterally to make a payment in lieu of notice is valid. However, it seems to the author that such a term may conflict with certain employment law provisions. Section 49(1) of the Employment Protection (Consolidation) Act 1978 provides:

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- "(1) The notice required to be given by an employer to terminate the contract of employment of a person who has been continuously employed for one month or more -
- (a) shall be not less than one week's notice if his period of continuous employment is less than two years;
 - (b) shall be not less than one week's notice for each year of continuous employment if his period of continuous employment is two years or more but less than twelve years;
 - (c) shall be not less than twelve week's notice if his period of continuous employment is twelve years or more."

This means that, after one month, all employees have a minimum period of notice inserted in their contracts of employment by statute. Section 49(3) goes on to say:

- "(3) but this section shall not be taken to prevent either party from waiving his right to notice on any occasion ..."

This would not allow a general waiver

" ... or from accepting a payment in lieu of notice."

In other words, this section does not prevent an employee accepting an offer of compensation for breach of his contractual right to notice. It does not, of course, mean that a term which allows the employer to force an employee to accept a payment in lieu is valid.

EPCA 1978 s.50 and Schedule 3 give the employee further rights in respect of his period of notice. This deals primarily with the pay to which the employee is entitled during his period of notice. Section 51 provides that the rights conferred by Schedule 3 are to be taken into account in computing the employer's liability for breach of contract if he fails to give the required notice.

Sections 49 and 50, therefore, give the employee certain statutory rights in relation to notice periods. These rights are further protected by s.140 which provides:

"... any provision in any agreement (whether a contract of employment or not) shall be void in so far as it purports -

- (a) to exclude or limit the operation of any provision of this Act."

It seems to the author that a term in a contract of employment which entitled an employer to pay a sum of money rather than giving notice would purport to exclude the operation of ss.49 and 50 and so would be void by virtue of s.140.

It may, however, be argued that such a provision is valid insofar as it affects periods of notice beyond the minimum period given by statute.

Even if the provisions for payment in lieu of notice are valid, the Revenue's argument appears misconceived. A payment is not an emolument simply because it is paid under a term of the contract of employment. It must still be a payment for being an employee and not for something else: see *Shilton v Wilmshurst* [1991] STC 88. In *Hochstrasser v Mayes* (1959) 38 TC 673, the taxpayer was paid, under a contractual scheme, for a loss which he suffered in moving home at the company's behest. The House of Lords decided that the payment derived from his personal situation as a homeowner and not from his employment. In *Mairs v Haughey* [1993] STC 569, the House of Lords held that a payment under a contractual redundancy scheme was not an emolument from the recipient's employment. It was rather a payment to relieve distress as a consequence of becoming unemployed.

A payment "in lieu of notice" is made because the contract of employment has been brought to an end. Therefore, it does not come from the employment, but rather from the termination of the employment: see *Henley v Murray* (supra). For this reason, the payment is not taxable as an emolument from the ex-employee's employment any more than a payment of damages for breach of contract where the employer dismisses the employee without notice and without the right to make a payment "in lieu of notice". This is supported by Lord Browne-Wilkinson in *Delaney v Staples* [1992] 1 AC 687 at 692 where he deals with payments which the employer is contractually entitled to make "in lieu of notice" and comments:

"In such a case if the employer summarily dismisses the employee he is not in breach of contract provided that he makes the payment in lieu. But the payment in lieu is not a payment of wages in the ordinary sense since it is not a payment for work to be done under the contract of employment."

Further, it is not a case like *Dale v De Soissons* (supra) where the employee had a contractual right to a fixed sum under his contract of employment. The employee has no right to the payment in lieu of notice. It would be open to the employer to give notice rather than making the payment. If the employer chooses to make a payment in lieu of notice, it cannot truly be said that this payment derives from the employment.