MONSTROUS EX GRATIA

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The Statement of Practice

Statement of Practice 13 of 1991 was released on 31st October[2] and deals with the subject of ex gratia awards made on the termination of an office or employment by retirement or death. Ex gratia payments made on the termination of an office or employment due to genuine redundancy or because of death or disability due to an accident are not affected by the Statement[3]. Among the potential effects is the nullification of the statutory concession given to the taxpayer which allows the first £30,000 of any ex gratia payment to be received free of tax[4].

S.148(1) ICTA 1988 provides that:

> "Subject to the provisions of this section and section 188, tax shall be charged under Schedule E in respect of any payment to which this section applies which is made to the holder or past holder of any office or employment, or to his executors or administrators, whether made by the person under whom he holds or held the office or employment or by any other person."

All seems simple enough. The two sections, s.148 and s.188, are to govern the taxation of retirement or termination payments, which are the avowed object of SP 13/91's ire. The only acknowledgment of the existence of the harsh and uncertain world beyond these two sections peeps over the wall in s.148(2):

> "This section applies to any payment (*not otherwise chargeable to tax*) which is made...in connection with the employment..."[my italics].

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2 [1991] STI 925.

3 paragraphs 1 and 10 SP 13/91.

4 s.188(4) ICTA 1988

The hunt is therefore on for the Revenue to find a circumstance in which a termination payment is "otherwise chargeable to tax". The thorn in the side of a charging provision is s.188. Of particular concern is subsection (4):

> "Tax shall not be charged by virtue of section 148 in respect of a payment of an amount not exceeding £30,000 ..."

In the Statement of Practice, paragraph 2 declares that:

> "An ex gratia payment is made under a retirement benefits scheme if the decision to make the payment involves an arrangement. Self evidently, there will be an "arrangement" if the payment flows from any prior formal or informal understanding with the employee. But the term arrangement goes wider [we are told] and includes any system, plan, pattern or policy connected with the payment of a gratuity. Some examples are-
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> (i) a decision at a meeting to make an ex gratia payment on an employee's retirement; or
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> (ii) where, say, a personnel manager makes an ex gratia payment under a delegated authority or on the basis of some outline structure or policy; or
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> (iii) where it is common practice for an employer to make an ex gratia payment to a particular class of employee."

The statutory basis for this statement is s.611(2) ICTA which provides:

> "References in this chapter to a scheme include references to *a deed, agreement, series of agreements, or other arrangements* providing for relevant benefits..." (my italics)

The Statement Analysed

The chargeable event envisaged in the Statement of Practice focuses on the word "arrangement" in s.611(2). The Revenue's argument in a nutshell is that, in circumstances analogous to the three enumerated in the Statement of Practice, even the first £30,000 of an ex gratia payment will form part of a "retirement benefits scheme" as an arrangement.

This argument is unattractive on a number of footings.

The first is that it is difficult to see, logically, how a unilateral decision by an employer to make a payment to an employee (whether removed from her/his position or deceased) can be said to be an arrangement. To my simple mind an arrangement requires some element of reciprocation. A "unilateral arrangement" would seem to be a decision to act or a process of mental compartmentalising. It does not, however, involve a co-ordination of actions between parties.

In the three examples, it is difficult to locate any sense of arrangement that falls within the spirit of the section. A decision at a meeting is clearly a unilateral act and cannot be said to be an arrangement made with any person not present at the meeting. The question might arise as to whether the arrangement between those present would satisfy the section but I shall return to this later. The anomaly which strikes one at

this point can be explained as follows. Suppose it could be said that a decision or arrangement taken at a meeting *can* constitute an "arrangement" in the circumstance where the employee has no input in the decision, nor is s/he even made aware that such a payment is either likely or possible. Transfer those same facts to the position of an employee of a sole trader, where that sole trader makes all management decisions unilaterally. It cannot be said that such a decision constitutes an "arrangement" because it is an ex gratia payment made by one individual to another. It must therefore follow that, if the Revenue's view is correct, employees of companies will be taxed differently from the employees of sole traders.

A payment by a personnel officer does not even possess the ambiguity of being the product of a meeting. It is clearly a unilateral choice to benefit an ex-employee and is therefore within the s.148 regime and not the "retirement benefits scheme" provisions. Where it is common practice for an employer to make ex gratia payments, that cannot be more than an arrangement internal to the employer's management competence and not, of necessity, an arrangement between employer and employed.

The question of who must be party to this arrangement remains to be answered. I have said that a unilateral decision is not enough but must the employee or any other party be involved? The Revenue's approach would seem to suggest that they need not be. Section 612(2) specifically envisages the involvement of third parties and the employee in contractual negotiations. However, it appears to me that anything which is decided by the employer, in whatever collective form management may act *qua* employer, must be a unilateral act and not an arrangement.

Alternatively, it must be said that an ex gratia payment by definition is something that must be performed unilaterally. Much can be gained from a comparison of "arrangement" with, on an *eiusdem generis* basis, the other three scenarios envisaged by s.611(2). "Agreement, or series of agreements" suggests some form of quasi-contract which is the very antithesis of an ex gratia payment. Similarly, it is difficult to imagine a deed without `parties to a deed'. The seeming intention of the section is to limit "schemes" to those circumstances where there are relations nearly amounting to contract (as Lord Devlin put it in another context in *Hedley Byrne v Heller*[5]. While the concept causes the mind to swim the more one considers it, the intention is apparent enough.)

Conclusion

The most attractive part of the Statement of Practice is contained in Paragraph 3, which provides quite simply:

> "The position in individual cases can be decided only on their facts."

In conclusion, I think it is well to reconsider the mischief of ss.148 and 188. It is clear that in s.188, Parliament has decided that where an ex gratia payment is made to an employee on terminating her employment, or upon death, any sum up to the value of £30,000 is to be received free of tax. One wonders, then, as to the propriety of the Revenue seeking to introduce taxation by the back door in this way. Much is said by that school of political theorists known disparagingly as "conspiracy-theorists" of the spectre of "civil service legislation". On occasion one is minded to lend them a moment's credence.

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5 [1963] 2AllER 595.