Department for Communities –v- RM (UC) [2021] NICom 36

Decision No: C1/21-22(UC)

**SOCIAL SECURITY ADMINISTRATION (NORTHERN IRELAND) ACT 1992**

**SOCIAL SECURITY (NORTHERN IRELAND) ORDER 1998**

**UNIVERSAL CREDIT**

Application by the Department for leave to appeal

and appeal to a Social Security Commissioner

on a question of law from a Tribunal’s decision

dated 28 February 2020

DECISION OF THE SOCIAL SECURITY COMMISSIONER

1. This is an application by the Department for Communities for leave to appeal from the decision of a tribunal with reference CN/8288/19/05/O.

2. For the reasons I give below, I grant leave to appeal. However, I disallow the Department’s appeal.

**REASONS**

**Background**

3. The issue in this case is whether a tribunal erred in law by holding that information received from HMRC, regarding a payment received by a claimant in settlement of industrial tribunal proceedings, failed to reflect the definition of employed earnings in some material respect for the purposes of universal credit (UC).

4. The respondent and his wife had made a joint claim for UC to the Department for Communities (the Department) on 17 August 2018. On 17 December 2018 the Department decided that he was entitled to UC amounting to £0.00 as his earnings exceeded his entitlement to UC. This was on the basis that he had received earnings of £5,228.42 in the assessment period from 17 November 2018 to 16 December 2018.

5. The respondent requested a reconsideration, submitting that a compensation payment relating to a previous period of employment had been taken into account when calculating his income for UC purposes. On 3 October 2019 the decision was reconsidered by the Department but not revised. The respondent appealed. The appeal was considered by a tribunal consisting of a legally qualified member (LQM) sitting alone. The tribunal found that the compensation payment failed to reflect the definition of employed earnings in some material respect and allowed the respondent’s appeal.

6. The Department requested a statement of reasons for the tribunal’s decision and this was issued on 15 June 2020. On 2 July 2020 the Department applied to the tribunal to set aside its decision and, in the alternative, for leave to appeal to the Social Security Commissioner. The President of Appeal Tribunals refused the application to set aside the tribunal’s decision and refused leave to appeal by a decision issued on 1 October 2020. On 26 October 2020 the Department applied to a Social Security Commissioner for leave to appeal.

**Grounds**

7. The Department, represented by Mr Yeates of Decision Making Services, submits that the tribunal has erred in law on the basis that it found that the payment of £5,228.42 to the respondent was not a payment of earnings. He submitted that the tribunal had made an unreasonable finding in determining that the “true characteristic” of the payment was capital as opposed to income.

8. The respondent, was invited to make observations on the Department’s application. Observations were received from the respondent and subsequently from Mr Black of Law Centre (NI) on his behalf. He submitted that the tribunal had not erred in law and indicated that the respondent did not support the Department’s application.

**Relevant legislation**

9. The scheme of UC was established in Northern Ireland by the Great Britain Secretary of State for Work and Pensions under powers granted by section 1 of the Northern Ireland (Welfare Reform) Act 2015. It was introduced on a phased basis, commencing on 27 September 2017. By article 8(2) of the Welfare Reform (NI) Order 2015 (the Order):

1. Joint claimants are jointly entitled to universal credit if—
2. each of them meets the basic conditions, and
3. they meet the financial conditions for joint claimants.

10. By article 10 of the Order:

1. …, the financial conditions for joint claimants are that—
   * + 1. …
       2. their combined income is such that, if they were entitled to universal credit, the amount payable would not be less than any prescribed minimum.

11. By article 12 of the Order:

1. Universal credit is payable in respect of each complete assessment period within a period of entitlement.
2. In this Part an “assessment period” is a period of a prescribed duration.
3. Regulations may make provision—
   * + 1. about when an assessment period is to start;
       2. for universal credit to be payable in respect of a period shorter than an assessment period;
       3. about the amount payable in respect of a period shorter than an assessment period.
4. In paragraph (1) “period of entitlement” means a period during which entitlement to universal credit subsists.

12. By article 13 of the Order:

13.—(1) The amount of an award of universal credit is to be the balance of—

* + - * 1. the maximum amount (see paragraph (2)), less
        2. the amounts to be deducted (see paragraph (3)).

(2) The maximum amount is the total of-

* + - 1. any amount included under Article 14 (standard allowance),
      2. any amount included under Article 15 (responsibility for children and young persons),
      3. any amount included under Article 16 (housing costs), and
      4. any amount included under Article 17 (other particular needs or circumstances).

1. The amounts to be deducted are—
   * + 1. an amount in respect of earned income calculated in the prescribed manner (which may include multiplying some or all earned income by a prescribed percentage), and
       2. an amount in respect of unearned income calculated in the prescribed manner (which may include multiplying some or all unearned income by a prescribed percentage).
2. In paragraph (3)(a) and (b) the references to income are—
   * 1. in the case of a single claimant, to income of the claimant, and
     2. in the case of joint claimants, to combined income of the claimants.

13. The relevant regulations, made under article 12(3) by the Great Britain Secretary of State for Work and Pensions, are the Universal Credit Regulations (NI) 2016 (the UC Regulations). By regulation 22, these provide for an assessment period as follows:

22.—(1) An assessment period is a period of one month beginning with the first date of entitlement and each subsequent period of one month during which entitlement subsists.

14. The definition of “earned income”, which falls to be deducted from the maximum UC award as required by article 13(3), appears at regulation 51 of the UC Regulations. This provides:

51. “Earned income” means—

(a) the remuneration or profits derived from—

1. employment under a contract of service or in an office, including elective office,
2. a trade, profession or vocation, or
3. any other paid work; or

(b) any income treated as earned income in accordance with this Chapter.

15. The general principle for the calculation of “earned income” is provided for at regulation 53:

53.—(1) The calculation of a person’s earned income in respect of an assessment period is, unless otherwise provided in this Chapter, to be based on the actual amounts received in that period.

(2) Where the Department—

(a) makes a determination as to whether the financial conditions in Article 10 of the Order are met before the expiry of the first assessment period in relation to a claim for universal credit, or

(b) makes a determination as to the amount of a person’s unearned income in relation to an assessment period where a person has failed to report information in relation to that earned income,

that determination may be based on an estimate of the amounts received or expected to be received in that assessment period.

16. The mechanism for calculating earned income is provided by regulation 55. This provides:

55.—(1) This regulation applies for the purposes of calculating earned income from employment under a contract of service or in an office including elective office (“employed earnings”).

(2) Employed earnings comprise any amounts that are general earnings as defined in section 7(3) of the ITEPA but excluding—

(a) amounts that are treated as earnings under Chapters 2 to 11 of Part 3 of that Act (employment income: earnings and benefit etc treated as income), and

(b) amounts that are exempt from income tax under Part 4 of that Act (employment income: exemptions).

(3)…(not relevant)

17. The reference to ITEPA is a reference to the Income Tax (Earnings and Pensions) Act 2003. By section 7(3) of that Act:

(3) “General earnings” means—

(a) earnings within Chapter 1 of Part 3, or

(b) any amount treated as earnings (see subsection (5)),

excluding in each case any exempt income.

18. Chapter 1 of Part 3 of the Act consists of section 62 of the ITEPA, which provides:

62(1) This section explains what is meant by “earnings” in the employment income Parts.

(2) In those Parts “earnings”, in relation to an employment, means—

(a) any salary, wages or fee,

(b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money’s worth, or

(c) anything else that constitutes an emolument of the employment.

(3) For the purposes of subsection (2) “money’s worth” means something that is—

(a) of direct monetary value to the employee, or

(b) capable of being converted into money or something of direct monetary value to the employee.

(4) Subsection (1) does not affect the operation of statutory provisions that provide for amounts to be treated as earnings (and see section 721(7)).

19. The particular provision which is central to the reasoning applied by the tribunal in this case is regulation 62 of the UC Regulations. This was amended from 16 November 2020 but at the material time read:

62.—(1) Unless paragraph (2) applies, a person shall provide such information for the purposes of calculating their earned income at such times as the Department may require.

(2) Where a person is, or has been, engaged in an employment in respect of which their employer is a Real Time Information employer—

(a) the amount of the person’s employed earnings from that employment in respect of each assessment period is to be based on the information reported to HMRC under the PAYE Regulations and received by the Department from HMRC in that assessment period; and

(b) in respect of an assessment period in which no information is received from HMRC, the amount of employed earnings in relation to that employment is to be taken to be nil.

1. The Department may determine that paragraph (2) does not apply in respect

of —

* 1. a particular employment, where it considers that the information from the employer is unlikely to be sufficiently accurate or timely, or
  2. a particular assessment period where—
     1. no information is received from HMRC and the Department considers that this is likely to be because of a failure to report information (which includes the failure of a computer system operated by HMRC, the employer or any other person), or
     2. where the Department considers that the information received from HMRC is incorrect or fails to reflect the definition of employed earnings in regulation 55, in some material respect.

1. Where the Department determines that paragraph (2) does not apply, it must make a decision as to the amount of the person’s employed earnings for the assessment period in accordance with regulation 55 (employed earnings) using such information or evidence as it thinks fit.
2. When the Department makes a decision in accordance with paragraph (4) it may—
   * 1. treat a payment of employed earnings received by the person in one assessment period as received in a later assessment period (for example where the Department has received information in that later period or would, if paragraph (2) applied, have expected to receive information about that payment from HMRC in that later period), or
     2. where a payment of employed earnings has been taken into account in that decision, disregard information about the same payment which is received from HMRC.

(6)…

**The tribunal’s decision**

20. The LQM has provided a statement of reasons for her decision. From this I can see that she had a number of documents before her, including the Department’s submission with a copy of the online UC claim form, the system decision, earnings details provided by HMRC, a “claim closure” notification and the reconsideration request and decision. She further had a handwritten letter from the respondent, a copy of his Industrial Tribunal conciliation settlement, a copy of a letter from his employer, a submission from the respondent’s representative, two letters detailing a breakdown of the payment and additional e-mail correspondence. The respondent attended and gave oral evidence, but was not represented. Mr McGrath represented the Department.

21. Mr McGrath outlined that the respondent had an ongoing award of UC, paid in arrears, and that two assessment periods were affected by the decision under appeal, being 17 November 2018 to 16 December 2018 and 17 December 2018 to 16 January 2019. He indicated that information was received from HMRC on 16 December 2018 as to the respondent’s earnings. The respondent had received a sum of money in settlement of a legal claim, which the Department treated as earned income. The Department confirmed that it had not considered that the discretion given in regulation 62(3) of the UC Regulations was applicable. The respondent submitted that he should not be penalised for his employer’s wrongful conduct in relation to non-payment of his wages in the past. He pointed out that the past earnings related to a period before UC existed and when he was not claiming UC. He submitted that the sums involved would not have led to an overpayment of Tax Credits, which he was receiving at the time, as they were still below the relevant threshold.

22. The LQM found that it was common case that the respondent received a payment of £5,757.41 during the assessment period from his employer relating to a period from 2005 to 2012. The respondent had initiated Industrial Tribunal proceedings which were settled in conciliation involving the Labour Relations Agency. The payment was described by the employer as a “gesture of goodwill” rather than a liability under a contractual obligation. The LQM was satisfied that the payment fell within the exception in regulation 62(3) where information from HMRC fails to reflect the definition of earnings in regulation 55 in some material respect. She found that the relevant sum was not earnings for the purposes of UC, allowing the respondent’s appeal.

**Hearing**

23. Due to ongoing Covid-19 restrictions, I held an oral hearing of the appeal by video link. Mr Yeates of Decision Making Services appeared for the Department and Mr Black of Law Centre (NI) for the respondent. The respondent also attended the hearing and addressed me at the conclusion. I am grateful to each of them for their submissions. I apologise for the subsequent delay in promulgating my decision.

24. Mr Yeats submitted that the tribunal had erred in law by finding that the payment of £5,228.42 made to the respondent by his employer in the assessment period from 17 November 2018 to 16 December 2018 was not a payment of earnings. Mr Yeates inferred that it was the tribunal’s view that the payment should be regarded as capital, although the tribunal had not stated this explicitly. On the basis that it was regarded as capital by the tribunal, he relied upon *Minter v Hull CC and Potter v SSWP* [2011] EWCA Civ 1155 submitting that it was the ‘true characteristics’ of a payment, rather than the label attached to it, which determine whether that payment is one of earnings or otherwise.

25. Mr Yeates noted that the respondent had brought Industrial Tribunal proceedings for non-payment of wages. As a result of conciliation action, a settlement was reached whereby the employer would make a payment to the respondent, which represented 1.5 hours of work per week for the period from 11 October 2005 to 9 September 2012 at the historical rates of pay. The payment was subsequently made via the employer’s payroll and was subject to deductions for income tax and national insurance. He submitted that the true characteristic was that it had been a payment for work carried out for a specified number of hours at a set rate of pay, and that regulation 62(2) of the UC Regulations required it to be attributed to the respondent’s UC award.

26. Mr Yeates observed that the tribunal indicated in its statement of reasons that consideration was given to the fact that tax and national insurance was deducted from the payment and that the Labour Relations Agency had described the payment as “salary.” He acknowledged that particular reference was made to a letter from the employer which described the settlement offer as a gesture of goodwill. He submitted that the tribunal’s conclusion was not consistent with the jurisprudence on this issue, as the true characteristics of the payment were not assessed by it. Rather, the tribunal examined the “circumstances surrounding the payment” and the various labels which were applied to it by the respective parties. He submitted that the true characteristic of the payment was that of earned income. As such, it had to be taken into account in assessing the respondent’s award of UC as prescribed by regulations.

27. For the respondent, Mr Black submitted that the tribunal correctly exercised the discretion permitted under regulation 62(3) of the UC Regulations to determine that regulation 62(2) did not apply in this case. He submitted that UC runs income assessment calculations based on earned income for monthly assessment periods. If the monies paid in compensation to the respondent were to be considered ‘earned income’, the employment these ‘earnings’ potentially relate to stretches back over 15 years. It could not therefore be reasonably considered an accurate reflection of earnings for that month and therefore there was an obligation on the Department, and the tribunal, to consider the application of regulation 62(3).

28. Mr Black submitted that settlement claims in employment disputes could not be seen as ‘earned income’ given the difficulties in assessing equivalent work, the problems with assessing the value of that work, the possibility of claims for injury to feelings and damages and the question of interest earned on the amount. He queried whether, in the relevant period, one could calculate an identifiable claim to a certain amount of income enforceable under a contract of employment. Furthermore, he submitted, general damages, awarded in for example a negligence claim, are not deemed to be ‘earnings’ for the purposes of benefit entitlement. He further submitted that it was therefore irrational to class an award that was not defined as ‘earnings’ by either the employer or employee, as such. He observed that the employer in the case was keen to point out there has been no admission of liability.

29. While submitting that *Minter* was wrongly decided, he also submitted that the case of the respondent could be distinguished from *Minter* in any event due to the difference in the relevant legislation applied. *Minter* was based upon an interpretation of the Housing Benefit regulations. The court held at para 27:

“27. Under the Housing Benefit Regulations, as the payment was a payment of what should have been paid as wages, it fell within Regulation 35. It was within the term “remuneration” in the opening words of paragraph (1) as it was derived from Miss Minter’s employment with the Council as it was solely referable to what she should have been paid during her employment. If not, it was “payment in lieu of remuneration” within (1)(b) as it was a payment for what she should properly have been paid.”

30. He further noted that the court held at para 29 that:

“It was common ground that “earnings” in Regulation 41 has the same meaning as in Regulation 35. Earnings thus encompass any remuneration or profit derived from employment including payment in lieu of remuneration. As a matter of ordinary language, then the payment was, for the reasons I have given, remuneration or profit derived from the employment or payment in lieu of such remuneration. We were referred by Mr Forsdick to Hochstauser v Mayes [1959] Ch D 22 *[my observation: the case reference should properly read Hochstrasser]* where this court decided by a majority that a scheme to assist employees of a company when moving by covering losses on property transactions was subject to tax as a profit of the employment; Jenkins LJ in giving one of the majority judgments considered that it would not be a profit of the employment if the payment was made for a consideration other than services (see page 47 of the report). In my view, on this test, the payment was for a consideration that derived from Miss Minter’s employment; it did not derive from her entering into a settlement agreement as distinct from her employment, as the settlement was a settlement of what should have been paid to her during her employment. It was therefore remuneration or a profit derived from her employment.”

31. Mr Black submitted that the term ‘payment in lieu of remuneration’ is present in the Housing Benefit Regulations 2006, by which *Minter* was decided, but not present in the UC Regulations. There was therefore no obligation to consider the payment from the respondent’s employers to be ‘payment in lieu of remuneration’ as was the case in *Minter*. Instead, the tribunal was empowered by the discretion afforded to them by regulation 62(3), if it considered that the information received failed to reflect the definition of employed earnings. The tribunal, having considered the evidence before them, had chosen to do so and was within their legal right to do so.

32. Mr Black further submitted that the tribunal’s decision was in keeping with established case law, which affords the right to courts or tribunals to determine whether awards received in employment disputes are to be considered as ‘earnings’. He opened some case law from the income tax jurisdiction, including *Oti-Obihara v HMRC (2011 TC 00819)*, where a First Tier Tax Tribunal found that section 401 of ITEPA does not apply to compensation for non-financial losses. He also relied on the decision of the Court of Appeal in England and Wales in *Moorthy v HMRC [2018] EWCA Civ 847*, as to how employment dispute awards are to be determined for income and tax purposes.

33. In the present case Mr Black submitted that the tribunal, having weighed up all the evidence available to it, was entitled to decide that the information received from HMRC in the assessment period was “incorrect, or fails to reflect the definition of employed earnings in regulation 55”.

**Assessment**

*Facts of the case*

34. The respondent brought proceedings in the Industrial Tribunal against his employer, claiming that the salary he received in eight tax years from 2005/06 to 2012/13 did not reflect the hours he had worked or - as I understand it - his *pro rata* holiday pay entitlement, in that period. I do not have details of the precise cause of action in the Industrial Tribunal proceedings, which seem likely to have been grounded on unlawful deduction from wages and/or breach of contract.

35. A compromise settlement of the proceedings was reached following conciliation by the Labour Relations Agency, under which the respondent would receive a payment from his employer. The basis of calculation was that the respondent would be awarded pay for an additional 1.5 hours per week at the relevant historical rate of pay for the period from 11 October 2005 to 9 September 2012. A settlement agreement in accordance with Article 21A of the Industrial Tribunals (NI) Order 1996 was prepared. This indicated acceptance by the respondent of the total gross sum of £5,757.41, subject to tax and national insurance deductions, which was to be paid alongside his November 2018 salary.

36. No contractual liability was admitted by the employer and the payment is referred to in correspondence as “a gesture of good will” in “exceptional circumstances”. From figures demonstrating the working out of the gross total sum of £5,757.41, however, it can be seen that the bulk of the payment was based upon hourly rates of pay and specified working hours and holiday entitlement, leading to objectively calculated amounts (ranging from around £350 to £950 annually). These were attributed to the respondent’s employment over each of the eight tax years from 2005/06 to 2012/13 inclusive. There was no element for injury to feelings or discrimination. The respondent submits that during that period he was in receipt of tax credits (TC), and that his entitlement to TC would not have been affected had his wages at the relevant time included the notional increases which comprised the settlement figure. I have no reason to doubt that.

37. With the deduction of tax and national insurance, and with the addition of wages for the particular assessment month, the respondent received a net payment from his employer of £5,221.25. Of that amount, only £330.45 was directly attributable to his normal monthly salary. As the respondent’s employer was a Real Time Information (RTI) employer, information reported to HMRC was that a payment amounting to £5,221.25 was made to him in the assessment period. That figure was duly passed to the Department for the purposes of UC assessment.

*Minter and Potter*

38. The cases of *Minter v Kingston Upon Hull City Council* and *Potter v Secretary of State for Pensions* were heard together by the Court of Appeal in England and Wales. Each was an appeal from the Upper Tribunal – the former from Judge Howell QC and the latter from Judge Jacobs. While addressed to different benefits – housing benefit (HB) and jobseeker’s allowance (JSA) respectively – the relevant legislation for each benefit had a similar structure.

39. The issues in *Minter and Potter* had arisen following employment law cases, such as *GMB v Allen* [2008] EWCA Civ 810, that identified a problem with the way in which equal pay legislation had been applied, principally affecting the wages of part-time workers. In order to avoid litigation, many local authorities adopted proactive approaches in cooperation with trades unions and the Advisory, Conciliation and Arbitration Service (ACAS) – the Great Britain equivalent of the Labour Relations Agency - and entered into settlements with individual employees. In *Minter*, the claimant had been employed part-time by Hull City Council and was claiming HB from the same council. Having attended a council “roadshow”, with support from Unison, she accepted a payment of £4,768.55 in settlement of any potential claim that could be brought under the Equal Pay Act 1970, the Sex Discrimination Act 1975 or for other related heads of claim.

40. She notified the council’s HB authority of the payment. It retrospectively calculated her past HB entitlement on the basis that the payment was properly classified as income or arrears of income. It decided that regulation 79(6) of the HB Regulations had the effect of attributing the income to a period in the past and that she had been overpaid HB as a result. It sought to recover £545.11 from her on the basis that the settlement payment represented income. The lawfulness of this recovery action was upheld by Upper Tribunal Judge Howell QC.

41. In *Potter*, the claimant was a part-time employee who was claiming JSA. In similar circumstances, a compensation figure was calculated by her employer in settlement of similar Equal Pay Act and sex discrimination claims in order to avoid litigation. The employer made advance payment to her of 10% of this figure – amounting to £721.74 – as a “goodwill gesture”. However, while accepting this sum, she rejected the offer of settlement and proceeded to pursue the claim before an Employment Tribunal. The SSWP assessed the sum of £721.74 as income under regulation 98 of the JSA Regulations and this analysis was upheld by Judge Jacobs.

42. Counsel for the appellants made the submission that neither the HB nor the JSA Regulations defined what payments were to be classified as “income” or “capital” and that the relevant regulations only applied once the payment had been classified as income or capital. As the substantial one-off payments did not have the characteristics of income, they were not therefore income.

43. The EWCA noted that by regulation 35(1) of the HB Regulations:

“… “earnings” means in the case of employment as an employed earner, any remuneration or profit derived from that employment and includes –

* 1. any bonus or commission;
  2. any payment in lieu of remuneration except any period sum paid to a claimant on account of the termination of his employment by reason of redundancy;
  3. any payment in lieu of notice of any lump sum payment intended as compensation for the loss of employment but only in so far as it represents loss of income”.

44. It further noted a “general sweep up provision” in regulation 41(3), which provided:

“Any earnings to the extent that they are not a payment of income shall be treated as income”.

45. The EWCA noted that the JSA Regulations were very similar to the HB Regulations, except to the extent that they did not have an equivalent to regulation 35(1)(b) (payment in lieu of remuneration). Regulation 98 provided:

“… “earnings” means in the case of employment as an employer earner, any remuneration or profit derived from that employment and includes:

…

* 1. any compensation payment;

…

(3) In this regulation “compensation payment” means any payment made in respect of the termination of employment other than ….

(a)-(d)”

46. It noted that regulation 104(4) was identical to regulation 41(3) of the HB Regulations.

47. The EWCA observed that in the case of *R v National Insurance Commissioner ex parte Stratton* [1979] ICR 209, where the Court had to consider whether a redundancy payment was income or capital for the purposes of unemployment benefit, Lord Denning had found that the correct approach was to examine the “true characteristic” of the payment. In that case, the Court found that a redundancy payment was made to compensate for loss of a job and was not payment for loss of future income.

48. In *R(SB)21/86* Commissioner Rice had applied *Stratton* and found that a compensation payment for unfair dismissal fell within the term “any payment in lieu of notice or remuneration” within the definition of earnings in the supplementary benefit regulations, as its true characteristic was compensation for future income or remuneration that would otherwise have been payable had the employment not been terminated.

49. The EWCA held that if a sum was paid in settlement of claims, it did not matter in determining its true characteristic whether it was a lump sum or a series of periodic payments. It was only necessary to examine why the compensation was being paid. It found, in the case of *Minter*, that the payment was compensation for the lower wages the claimant had been paid in breach of the Equal Pay Act, and that its true characteristic was clearly compensation for past lost income. It fell within the term “remuneration” in regulation 35(1) as it was solely referable to what should have been paid during her employment. If not it was “payment in lieu or remuneration” within 35(1)(b). If it was not a payment of income under regulation 35, then it must have been earnings under regulation 41(3). It found in the case of *Potter* that the true characteristic was that it was an on account payment for what was due to be paid to the claimant by way of lost wages and that it was compensation for past income. It was earnings within regulation 98 and, if it was not, it was earnings within regulation 104(4).

The relevance of *Minter and Potter* to UC

50. Mr Yeates submitted that the tribunal had erred by finding that the payment to the respondent failed to reflect the definition of employed earnings in regulation 55 and – he submitted – had therefore found that the payment was a payment of capital. In this context, he submitted that the tribunal had erred by failing to place reliance on *Minter and Potter* in terms of identifying the true characteristic of the payment and holding it to be income as opposed to capital.

51. However, I find this submission problematic. The “true characteristic test” was created to deal with a specific problem in earlier social security legislation. In CH/1561/2005, which concerned the impact of a payment of arrears of working families’ tax credit on entitlement to housing benefit, Mr Commissioner Jacobs (as he then was) explained the problem (at paragraph 19):

“The Regulations deal with both income and capital. They provide for the calculation of both, for disregarding both, for treating income as capital and capital as income, for student income and for benefit income. What they do not do is to provide a definition of income or capital”.

52. The *Stratton* case involved unemployment benefit, while *Minter* and *Potter* involved HB and JSA respectively. As Mr Black has pointed out, the legislation applying in those cases was different and, in particular, included provisions that required any earnings, to the extent that they were not a payment of income, to be treated as income. In addition, they did not relate to a present assessment period, but were attributed, in *Minter*’s case, as payment of earnings for a specific past period in which HB was received and, in *Potter*’s case, as income for a prospective future period.

53. The logic of Mr Yeates’ submission based on *Minter* is that the compensation payment received by the appellant in the present case would be attributable to a past period for HB purposes – if he had been claiming HB in the period 2005-2012 - while also attributable to a present period for UC purposes. I would find such an outcome to be anomalous. However, that is not decisive.

54. It seems to me that a more significant difference arises between UC and what are now termed “legacy” social security benefits. Whereas UC retains the general outline of capital and income which is familiar from many past benefits, it appears to me that a distinguishing feature is the definition of “earned income” within UC. Unlike the position with HB or JSA legislation, relevant terms within the UC legislation are now defined with direct reference to the provisions of income tax legislation. The consequence of this, it seems to me, is that the question of whether a payment amounts to earned income is not to be addressed on the basis of its “true characteristics”, but rather whether it falls within the definition provided in the legislation.

55. Mr Yeates placed his focus on regulation 51 of the UC Regulations which defines “earned income”. His submission, based on regulation 51, is that the compensation sum received by the respondent would constitute “remuneration … derived from … employment under a contract of service … or any income treated as earned income in accordance with this Chapter”. He made no direct reference to further UC provisions in his submissions.

56. Nevertheless, regulation 55 is of direct relevance. Paragraphs 55(1)-(3) and (5) make provision relevant to “employment under a contract of service”. In particular, by regulation 55(2), “employed earnings” comprise any amounts that are general earnings as defined in section 7(3) of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA). This definition in turn leads to section 62 of the ITEPA, and excludes various amounts under Chapters 2 to 11 of Part 3 of the ITEPA and Part 4 of the ITEPA. In other words, regulation 55(2) serves as a gateway between social security law and income tax law, defining concepts within the former in terms of the latter.

57. The direct link between the definition of employed earnings in the UC Regulations and the income tax legislation, it appears to me, distinguishes UC employed earnings cases from HB and JSA cases, such *Minter and Potter*. The task for the UC decision maker is not to decide whether a payment falls into one or other of the undefined binary categories of income and capital. In order to decide whether a payment constitutes “employed earnings”, rather than focus on whether a payment has the true characteristics of income, it appears to me that the sole question instead is simply whether it falls within the definition of general earnings under section 7(3) of the ITEPA. However, that question is complicated to some extent by the question of whether the income tax law to be applied in the adjudication of UC is precisely the same as applied by HMRC in charging income tax, or whether it is modified to some extent in the UC context.

58. The Department primarily submits that the tribunal erred in law on the basis that it did not address *Minter and Potter*. Mr Yeates infers from its decision that it treated the compensation payment received by the respondent as capital, as it had not treated it as income. However, I see no basis for such an inference to be drawn from the tribunal’s statement of reasons. Nor do I consider that the tribunal has erred in law by failing to apply the “true characteristics” test. It appears to me that such a test is not appropriate for determining whether a payment amounts to earned income in the context of UC. I therefore reject Mr Yeates’ submissions to this effect.

59. “Earned income” for UC purposes cannot simply be categorised as a payment which is not capital. The proper focus of enquiry in such cases lies within the ITEPA. The submissions provided by the Department to the tribunal did not address the ITEPA in any comprehensive way. However, in cases where the definition of income is in dispute, it seems to me, an onus falls on the Department to provide reasoned submissions addressing the provisions of the ITEPA and any relevant case law. This is a very substantial piece of legislation and is likely to have generated a substantial body of jurisprudence. The Department cannot assume that this will be familiar to tribunal members who have had to be knowledgeable about social security law but not, hitherto, income tax law.

60. That leads to the more general issue of whether the payment of £5,228.42 to the respondent fell within the definition of “earned income” in regulation 51 and whether the tribunal has erred in law by applying regulation 62(3) to it.

*The tribunal’s treatment of the relevant UC provisions*

61. The default position under regulation 62(2) of the UC Regulations is that the amount of the claimant’s employed earnings for each assessment period is to be based on the information which is reported to HMRC under the PAYE Regulations, and is received by the Department from HMRC in that assessment period. Nevertheless, a discretion to depart from that general position is given to the Departmental decision maker or - on appeal - to the tribunal. Where the tribunal considers that the information received from HMRC is incorrect or that it fails to reflect the definition of employed earnings in regulation 55 in some material respect, it may assess the employed earnings differently. In the instant case, it decided that the settlement payment in respect of a claim for the period 2005-12 should not be taken into account in the November-December 2018 assessment period.

62. I understand the word “incorrect” as it appears in regulation 62(3)(b)(ii) to mean simply that the data or information regarding the amount of payment was factually wrong. On this approach, it is not arguable that the information received from HMRC was incorrect. The respondent’s employer was an RTI employer and had provided accurate details of the payment it had made to the respondent in the particular assessment period. The respondent does not dispute the fact of the payment being made, the date of payment or the amount of that payment.

63. It seems to me that the only debatable issue is whether the tribunal was entitled to find that the payment failed to reflect the definition of employed earnings in some respect, also within regulation 62(3)(b)(ii). As observed above, employed earnings in regulation 55 comprises:

“any amounts that are general earnings as defined in section 7(3) of the ITEPA but excluding—

* 1. amounts that are treated as earnings under Chapters 2 to 11 of Part 3 of that Act (employment income: earnings and benefit etc treated as income), and
  2. amounts that are exempt from income tax under Part 4 of that Act (employment income: exemptions)”.

64. As noted above, section 7(3) of the ITEPA leads to section 62(2), which provides that “earnings”, in relation to an employment, means—

(a) any salary, wages or fee,

(b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money’s worth, or

(c) anything else that constitutes an emolument of the employment.

65. Before addressing this further, I consider that it might be useful to consider other recent case law on the issue of calculating earnings received during the UC assessment period.

*Case law on earnings and assessment periods*

66. Recent decisions of the courts in relation to UC have considered aspects of the way in which earnings have been treated within fixed UC assessment periods. For example, in *R(Johnson) v Secretary of State for Work and Pensions* [2020] EWCA Civ 778 the Court of Appeal in England and Wales (EWCA) addressed a situation where claimants who were paid monthly were treated as receiving double pay in one assessment period, due to payday falling on a weekend or bank holiday, and then none in the next assessment period. This arbitrary situation had disruptive effects to the ongoing UC award, resulting in the effective loss of the work allowance in the assessment periods without normal pay and wide monthly variations in UC awards with resulting budgeting problems.

67. The Divisional Court below in *R(Johnson) v Secretary of State for Work and Pensions* [2019] EWHC 23 had been prepared to find that the equivalent provision in the Great Britain Regulations to regulation 53, which had said that “earned income in respect of an assessment period is … to be based on the actual amounts received …” gave flexibility to the decision maker. It held that the words “based on” implied that it did not have to calculate UC entitlement from actual amounts received. It further relied on regulation 22 which referred to income “in respect of” the assessment period as supporting the position that pay in respect of periods outside the assessment period could be treated differently.

68. While rejecting the approach of the Divisional Court, to the extent that it had based its decision on an interpretation of the UC Regulations that permitted flexibility in regard to the assessment period, the EWCA nevertheless held that the rule that required both payments to be taken into account in the one assessment period was so irrational as to be unlawful. The EWCA held that it would not be inconsistent with the overall UC scheme to devise an exception to solve the problem and observed that a properly drafted narrow exception would have avoided such significant, predictable but arbitrary effects as had arisen. While confirming that the threshold for establishing irrationality is very high, the particular case was one of the rare instances where the refusal to put in place a solution for a specific problem was so irrational that the threshold was met.

69. Subsequently, in *R(Pantellerisco) v Secretary of State for Work and Pensions* [2020] EWHC 1944, the High Court in England and Wales addressed the position of a claimant who was paid four-weekly. The situation resulting was that, as the year has thirteen 4-week periods in it, but twelve monthly assessment periods, the claimant’s entitlement was assessed on the basis of eleven UC assessment periods in which she received one thirteenth of her annual salary and one UC assessment period in which she received two thirteenths of her salary. This in turn affected how she was affected by the “benefit cap”.

70. The benefit cap is a limit on the total amount of benefit payable. It does not apply in cases where the income from working a 16-hour-week in an assessment period exceeds certain thresholds. However, in the case of the particular claimant, the effect of taking only her 4-weekly payment into account was that the benefit cap applied, as she fell below the relevant income threshold, when it would not had her income been calculated on a monthly basis. Similarly to the approach of the Court of Appeal in *Johnson*, Garnham J held that the failure to provide the claimant with an exception to the benefit cap in her situation was irrational and unlawful.

71. Another case was *R(Caine) v Department for Work and Pensions* [2020] EWHC 2482. In that case the claimant had a weekly liability to pay housing costs. She challenged the formula for converting weekly costs in monthly costs, based on a 52 week assessment, as each year consists of 52 weeks and one day or 52 weeks and 2 days, meaning that she lost one of two days entitlement to housing costs annually. Knowles J held that the regulations could not be said to have produced such stark and arbitrary effects as they did in the two earlier cases. He declined to accept that they were irrational, saying:

“216. The question is *not* whether there was a better solution than that chosen by the Government and approved by Parliament … During the hearing I raised with counsel the mathematical concept of ‘best fit’, whereby the mathematical modeller attempts to devise an equation or a graph which most closely, but perhaps not perfectly, replicates a data set, usually gathered by empirical observation. Whilst the analogy is not perfect, in a sense, that is what the Government was trying to do when it devised this aspect of the UC Regulations. It was attempting to construct a mathematically based system in the Regulations (the equation) which would achieve, perhaps imperfectly, its policy goals in relation to housing costs (the data set). The question for me is whether, in light of that data set, the equation it chose is irrational. In my judgment, given the diverse range of views on what is obviously a difficult problem, it is impossible to characterise the choice which the Secretary of State … as irrational …The way in which monthly equivalent housing costs can be calculated is an issue on which reasonable minds can, and plainly do, differ and there is more than one permissible approach.”

72. In the Upper Tribunal in *LG v Secretary of State for Work and Pensions* [2021] UKUT 121, Judge May QC decided an appeal which involved the same 4-weekly pattern of payment addressed in *R(Pantellerisco) v Secretary of State for Work and Pensions*. In disallowing the appeal, he distinguished *Pantellerisco* on the facts, since the level of the claimant’s income in *LG v SSWP* meant that the benefit cap was not engaged. He briefly addressed regulation 63(2)(b)(ii) in the course of the decision but found that it did not apply on the facts of the case.

73. Also in the Upper Tribunal, in *NM v Secretary of State for Work and Pensions* [2021] UKUT 46, Judge Jacobs considered a case where the claimant received payments from his former employer, which led to nil assessments. Those payments were made late and represented unpaid wages, holiday pay and the return of a deposit that the claimant had paid on his uniform at the start of his employment. He applied regulation 63(2)(b)(ii) to the return of the deposit on the uniform. He then addressed whether late payments of wages that had to be enforced were similarly covered, as follows:

“13. The claimant’s representative has argued that regulation 61(3)(a) applies, because the payments made by the employer were not timely. I accept that the payments were made later than they should properly have been paid and that the timing suggests that they were made reluctantly. But that is not relevant. It is not the payment that has to be timely. It is the information from the employer that must be ‘unlikely to be … timely’. The information is the amount of the employed earnings for each assessment period. That does not mean that the earnings had to be earned in the period. As the claimant’s representative accepted, earnings almost always relate to past periods. The fact that the payments were only made as a result of negotiation and conciliation does not alter their character as earnings. The employer correctly reported the amount that was paid. The information reported to HMRC and passed to the Secretary of State was correct. This was done timeously. Regulation 61(3)(a)) does not apply.

14. The argument that regulation 61(3)(b)(ii) applies fails for the same reasons. The information was correct. It may be that ‘incorrect’ can be interpreted broadly, as the claimant’s representative has submitted, but it cannot make something incorrect that was correct. Again, the important word is information. The information is the amount that the claimant was paid and it was correctly reported. Matters relating to the timing of the payment, and the willingness or lack of it with which it was paid, are irrelevant to this provision.”

74. It is plain from the case law addressing the irrationality of the application of UC rules that the courts have been ready to examine and resolve aspects of the UC regime that have been found to be irrational, to the extent that the legislation gives rise to highly unfair, but easily remediable results. In the present case it was not submitted that the treatment of the compensation payment as income within a single assessment period, despite being payable in respect of a lengthy past period, was irrational to the extent that it was unlawful. Nevertheless, I consider that some support for the tribunal’s decision can be found in the approach to the interpretation of the UC Regulations taken by the Divisional Court in *Johnson*, and in particular at paragraphs 50-56. This interpretation would enable a flexible approach to be adopted by decision makers in approaching the issue of whether a payment is properly attributable to a particular assessment period. At paragraph 56 Singh LJ had said:

“For all those reasons, on a proper interpretation of regulation 54, read in context, the earned income of a claimant is the earned income he or she receives in respect of the assessment period, that is in respect of periods of time comprising the assessment period. The calculation will be based upon the actual amounts received. That will be the starting point and in many, perhaps in the vast majority of cases, may well be the finishing point of the enquiry that the legislation requires. However, there may need to be an adjustment where it is clear that the actual amounts received in an assessment period do not, in fact, reflect the earned income payable in respect of that period”.

75. The regulation 54 in the Great Britain regulations referred to in the judgement is the equivalent of regulation 53 in the Northern Ireland regulations. Although addressing the question of whether a payment of income is properly considered within a particular assessment period, as opposed to the amount that is attributable, the Divisional Court in *Johnson* plainly advocates a flexibility of approach that would be consistent with the decision reached by the tribunal in the present case. Such an approach would permit tribunals to mitigate any injustice or harsh effects that might arise from inflexible application of the regulations. It appears to me that such an approach would be generally consistent with the role of tribunals in administering justice.

76. However, as I have indicated above, the EWCA in *Johnson* expressly rejected the reasoning of the Divisional Court at paragraphs 34-45 of its decision. I find myself in disagreement with the EWCA on this issue. Technically, I am not bound by the EWCA. Nevertheless, while not, strictly speaking, binding on me as a Northern Ireland Social Security Commissioner, I consider that long-established principles of comity, applying when identical provisions may come to be interpreted differently in Great Britain and Northern Ireland, require me to follow the judgement of Rose LJ (as she then was) in the EWCA in *Johnson* in preference to that of Singh LJ in the Divisional Court (see *EC v Secretary of State for Work and Pensions* [2015] UKUT 618 at paragraphs 26-35). This has the coincidental effect of achieving consistency with the decision of Upper Tribunal Judge Jacobs in *NM v SSWP*.

77. The tribunal in the present case accepted that the information received from HMRC regarding the payment to the respondent failed to reflect the definition of employed earnings in regulation 55 in some material respect. Once the question of whether the payment can or should be attributed to a period other than the relevant assessment period falls away, as it must on the basis of the reasoning of the EWCA, the sole focus falls on the question of whether the payment fails to meet the definition of employed earnings in some material respect.

*Whether the payment to the respondent failed to meet the definition of employed earnings*

78. As observed above, “employed earnings” are defined in regulation 55(2). This links in turn to the definition of “general earnings” given in section 7(3) of the ITEPA, subject to the exclusions in sub-paragraphs 55(2)(a) and (b). The exclusions in sub-paragraph 2(a) relate to matters falling within Chapters 2-11 of Part 3 of the ITEPA (sections 63-220) and it does not appear to me that any of them apply. The exclusions in sub-paragraph 2(b) relate to matters exempt from income tax under Part 4 of the ITEPA (sections 227-326B) and again it does not appear to me that any of them apply.

79. The application of the definition in section 7(2) of the ITEPA is further qualified by regulation 55(3) which provides for disregards set out in Chapter 2 of Part 5 of the ITEPA (sections 333-360A) and for certain expenses given to services users in certain circumstances defined under regulation 52(2). Again it does not appear to me that any of them apply. No other provisions in regulation 55 appear to affect the position.

80. By section 7(3), “general earnings” means earnings within Chapter 1 of Part 3 of the ITEPA, or any amount treated as earnings by sub-section 7(5), excluding in each case any exempt income. None of the sub-section 7(5) categories appear relevant. Chapter 1 of Part 3 of the ITEPA consists solely of section 62. By 62(2) “earnings”, in relation to an employment, means (a) any salary, wages or fee, (b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money’s worth, or (c) anything else that constitutes an emolument of the employment.

81. It appears to me that the compensation payment was not a gratuity or other profit or incidental benefit of any kind obtained by the respondent. Therefore the category of 62(2)(b) does not apply.

82. The questions remaining, it seems to me, are whether the compensation payment was “salary, wages or a fee” or was otherwise covered by the term “anything else that constitutes an emolument of the employment”. I can find no definition of “emolument” in the ITEPA. However, it is generally understood as meaning compensation for employment or for holding an office.

83. Although the payment made to the respondent relates to a claim in the Industrial Tribunal for underpaid past wages or salary, the liability to pay wages for the past period was disputed by the employer. As observed by the tribunal, the settlement payment was referred to as a goodwill gesture. It was made in consideration for the withdrawal of legal proceedings, as opposed to being made directly in consideration for employment services. The employer had denied any contractual liability to the respondent under any contract of employment or contract of service. Equally the payment was not an emolument as not directly constituting compensation for employment or holding an office.

84. The correct position under income tax law appears to me to be set out by Jenkins LJ in *Hochstrasser v Mayes*, which I have referred to above. That case concerned the tax position of a payment made by an employer under a housing scheme to compensate for a loss in property value resulting from an employee’s transfer to a new work location. He said:

“The decisive question in each of these two cases therefore is, as I see it, simply whether the payment made by I.C.I. to the employee pursuant to the guarantee is a payment made to the employee in that capacity and for no consideration other than services, in which case it is taxable as a profit of his employment; or was such payment made for a consideration other than services, in which case it is not so taxable. I think it may truly be said that the housing agreement in each case was entered into by I.C.I. with the employee in his capacity as employee, in the sense that it was by virtue of his being an employee of I.C.I. that he was given the opportunity of participating in the housing scheme and for that purpose of entering into the housing agreement with I.C.I. But it does not necessarily follow that the employee, having entered into the housing agreement and thereafter receiving a payment from I.C.I. under the guarantee, must be taken to have received that sum in his capacity as employee and for no consideration other than services”.

85. This case of *Hochstrasser* was relied upon in *Minter and Potter* to support the finding that the compensation for arrears of wages amounted to consideration for services. However, in those cases, the settlement was proactively and voluntarily entered into by the employers to compensate for discriminatory underpayment of wages. In *Hochstrasser* itself, the housing scheme was an initiative of the employer to incentivise relocation that formed part of the contract of employment. This was not the case here. The employer settled the proceedings with no admission of liability. Its position was that it had met its contractual liability to pay wages and had no further liability. But for the legal proceedings, it would not have voluntarily made any payment to the respondent. The settlement payment was in consideration for the proceedings being withdrawn, not in consideration for employment services provided by the respondent between 2005 and 2012.

86. Mr Black had referred me to certain case law under Chapter 3 of Part 6 of the ITEPA, which deals with compensation for termination of employment. This was not the applicable law here, and I did not find the case law he referred me to as particularly helpful. The Department did not refer the tribunal or myself to any case law that would clarify the approach of HMRC to taxation of compensation settlement payments and to establish that a similar approach must be adopted under regulation 55 and section 7(3) of the ITEPA as modified to apply in the field of UC. While I, and the tribunal before me, have an inquisitorial jurisdiction within the specialist field of social security law, there are limits to the extent to which we can explore income tax law in the absence of structured submissions. I consider that the onus remained firmly on the Department to establish its case to the tribunal and to me.

87. However, I cannot be satisfied from the submissions made that the payment received by the respondent in settlement of industrial tribunal proceedings was a payment of wages or salary, or an emolument of employment under the ITEPA and the related UC Regulations. It appears to me that the tribunal was similarly entitled to exercise its discretion under regulation 62(3)(b)(ii) and to hold that the payment made to the respondent in consideration of withdrawing his Industrial Tribunal proceedings failed to reflect the definition of employed earnings in some material respect for the purposes of universal credit (UC).

88. Therefore, I must disallow the Department’s appeal.

(signed): O Stockman

Commissioner

25 August 2021