



Ely Place Chambers

ANALYSIS ADVICE ADVOCACY

## ***Peninsula Business Services Ltd v Donaldson [2016] UKEAT 0249\_15\_0903***

### **Case Summary**

The EAT has ruled that there is no obligation upon an employer to provide childcare vouchers that are ordinarily provided under a 'salary sacrifice' scheme to a participating employee during a period of maternity leave. The EAT's decision is contrary to HMRC Guidance, which suggests that such vouchers are a 'non-cash benefit' that employers must continue to provide during maternity leave.

#### **The Facts**

Peninsula Business Services Ltd ('**Peninsula**'), in common with many employers, operated a salary sacrifice childcare voucher scheme (the '**Scheme**') by which employees agreed to forgo part of their salary in return for being provided with childcare vouchers to the value of the salary sacrificed. The cost of the childcare vouchers provided under the Scheme was met by the salary sacrificed by the employee; the Scheme did not require any contribution from Peninsula. The benefit to participating employees was that they made a saving on the income tax and National Insurance contributions they paid in respect of their salary.

Employees wishing to enter the Scheme were required to agree to a variation of their contract, Clause 3 of which stipulated that:

*"During periods of time spent on maternity leave; parental leave; additional paternity leave; parental leave; periods of sick leave during which the only payment payable to the employee is Statutory Sick Pay and any other unpaid leave, provision of Childcare Vouchers and Adjusted Monthly Salary will be suspended and salary payments will revert to normal i.e. the pre-variation position. During the voucher suspension period, the employee will remain in the scheme."*

Employees of the Peninsula received only Statutory Maternity Pay ('**SMP**') while on maternity leave, from which by law no deductions may be made. Accordingly, an employee of Peninsula who was on maternity leave had no salary that could be sacrificed in exchange for childcare vouchers. If Peninsula were to provide childcare vouchers under the Scheme to employees on maternity leave, it would be obliged to pay the cost of the vouchers.

Ms Donaldson applied to join the Scheme and was refused entry because she would not agree to the suspension of childcare vouchers while on maternity leave. She brought a claim to the Employment Tribunal ('**ET**'), complaining *inter alia* that the terms of the Scheme and Peninsula's refusal to allow her to join the Scheme unless she agreed to those terms amounted to:

- Unfavourable treatment on grounds of pregnancy and maternity contrary to s.18 Equality Act 2010 ('Equality Act');
- A detriment on grounds of pregnancy and maternity contrary to s.47C Employment Rights Act 1996 ('ERA'); and
- Indirect discrimination on grounds of sex contrary to s.19 Equality Act.

### The Judgment of the ET

The ET upheld Ms Donaldson's claims of unfavourable treatment contrary to s.18 Equality Act and detriment contrary to s.47C ERA on the basis that "*Women on maternity leave are entitled to non-pay benefits during ordinary and additional maternity leave, whether or not the benefits are contractual, in accordance with the Maternity and Parental Leave Regulations 1999*".

In reaching this conclusion, the ET placed weight on 2014 Guidance published by HMRC, which stated that during any period of ordinary maternity leave contractual non-cash benefits provided under a salary sacrifice scheme in lieu of sacrificed salary, including childcare vouchers, "*must continue to be provided*".

The ET upheld Ms Donaldson's claim for indirect sex discrimination contrary to s.19 Equality Act on the basis that Clause 3 of the Varied Contract put women at a particular disadvantage when compared to men, since women were more likely to be absent for a period during which they were entitled only to received statutory pay. The ET found that the reasons put forward by Peninsula for the inclusion of Clause 3 were financial and cost alone could not provide objective justification (applying *Cross v British Airways plc* [2005] IRLR 423).

### The EAT's Decision

#### The Maternity and Pregnancy Discrimination Claim: s.18 Equality Act/s.47C ERA '96

The central issue in the appeal was whether the ET was correct to interpret the Maternity and Parental Leave Regulations 1999 ('**The Maternity Regs**') as requiring Peninsula to continue to provide salary sacrifice childcare vouchers during a period of maternity leave.

Reg. 9 of the Maternity Regs, enacted pursuant to s.71(6) ERA, provides:

- "(1) An employee who takes ordinary maternity leave or additional maternity leave*  
*(a) is entitled, during the period of leave, to the benefit of all of the terms and conditions of employment which would have applied if she had not been absent, and*  
*...*  
*(2) In paragraph (1)(a), "terms and conditions" has the meaning given by sections 71(5) and 73(5) of the 1996 Act, and accordingly does not include terms and conditions about remuneration.*  
*(3) For the purposes of sections 71 and 73 of the 1996 Act, only sums payable to an employee by way of wages or salary are to be treated as remuneration."*

Reading regs. 9(2) and 9(3) Maternity Regs together, an employee is entitled while on maternity leave to the “benefits” of the terms and conditions which would have applied had she not been absent. Excluded from this entitlement are “terms and conditions about sums payable by way of wages or salary”. Peninsula contended that reg. 9 Maternity Regs did not require it to continue to provide employees who were part of the Scheme with childcare vouchers during maternity leave, since, *inter alia*:

- The “benefit” of the Scheme to the employee was the savings the employee made in tax and National Insurance contributions and not the vouchers themselves; and
- Childcare vouchers provided as part of a salary sacrifice scheme were in any event to be properly considered as “sums payable by way of wages or salary” and accordingly were exempt from the obligation on an employer under reg. 9 Maternity Regs.

Having given consideration to the underlying taxation legislation that enables childcare voucher salary sacrifice schemes, the EAT (Langstaff J, Jenkins and Worthington) accepted both of Peninsula’s submissions. Crucially, the EAT found that childcare vouchers provided under a salary sacrifice scheme are properly to be considered as remuneration for the purposes of reg. 9 Maternity Regs. In reaching this conclusion, the EAT found persuasive Peninsula’s submissions that, properly regarded, the Scheme was not one of ‘salary sacrifice’ but rather ‘salary diversion’; by entering into the Scheme an employee was not truly sacrificing their salary but was rather directing the employer to divert a proportion of their salary to pay for childcare vouchers. The EAT held that:

*“Though the phrase [salary sacrifice] is in common use, and is referred to by that colloquial description in the legislation, as we have set out at the start of this judgment it is something of a misnomer. It is in reality not a sacrifice but a diversion of salary, which the employee has earned but which is redirected prior to it being placed within the employee’s pay packet, in order to purchase vouchers to the value of the salary utilised.” (§36, EAT Judgment)*

The EAT did not explicitly acknowledge that this conclusion was contrary to HMRC Guidance, though it referred to Peninsula’s submission that the Guidance was in error. However, an oblique explanation as to its departure from HMRC’s position is to be found in the EAT’s observation that the fact that childcare vouchers are treated as a “non-cash benefit” for the purposes of personal taxation did not deprive the vouchers of the character of remuneration for the purpose of the equality legislation: “The question is factual, and not to be determined by labels adopted for other purposes.” (§37, EAT Judgment)

The EAT considered that to find that childcare vouchers provided under a salary sacrifice scheme were not remuneration for the purposes of reg. 9 Maternity Regs would produce a windfall to affected employees that could not have been contemplated by the legislature. Parliament had legislated for employers to pay employees on maternity leave SMP only and it was not discrimination, nor contrary to the Maternity Regs, to do so:

*“The employee receiving a salary without entering a sacrifice scheme is not entitled by law to receive any more than legislation requires as a minimum. If that employee previously paid for childcare out of that salary, she would have no more money than if she did not. Where, instead,*

*the same money (overall) is used by arrangement with the employee to pay for childcare without the cost of it forming part of her pay packet, it is difficult to see why in principle she should be entitled not only to the minimum for which statute provides but also for the amount spent on childcare in addition. The tax benefit disappears: but this is a benefit which only applies as a consequence of being in receipt of the higher salary to which the Claimant is no longer entitled.” (§38, EAT Judgment)*

The lay members of the EAT in particular were also concerned as to the potential chilling effect that a requirement that employers continue to pay for childcare vouchers from their own resources during an employee’s maternity leave may have on the continued operation of childcare voucher salary sacrifice schemes:

*“The policy behind the provision of childcare vouchers through a salary sacrifice recognised in the taxing statutes as entitling the maker of it to favourable tax treatment is to enable more women with young children to remain in or return to the workplace ... It incentivises women to remain at work; and therefore is overall of economic benefit to the country. But the scheme is entirely voluntary on the employer’s part. If entering such a scheme had the consequence that once employees became pregnant the employer would face a cost beyond that it would already face by provision of statutory maternity pay, it would have the effect of discouraging employers from offering such a scheme. This is particularly acute where small and medium enterprises are concerned. Both Lay Members, from their different perspectives, regard such a consequence as very damaging to a valuable policy. We do not think that Parliament can have intended this consequence.” (§39, EAT Judgment)*

Having found that childcare vouchers provided under a salary sacrifice scheme were properly characterised as ‘remuneration’ for the purposes of reg. 9 Maternity Regs, it followed there was no obligation on Peninsula to continue to provide them to employees while on maternity leave. Accordingly, making the offer to Ms Donaldson to enter into the Scheme on the terms proposed did not amount to unfavourable treatment contrary to s.18 Equality Act or a detriment contrary to s.47C ERA. On the basis of its findings, the EAT reversed the decision of the ET and substituted a decision that Ms Donaldson’s claims must be dismissed.

It should be noted that, on the facts of the case, the EAT additionally questioned whether Peninsula’s refusal to allow Ms Donaldson to join the Scheme unless she agreed to its terms could in any event amount to a breach of reg. 9 Maternity Regs, since Ms Donaldson had not entered into the Scheme and had accordingly not been deprived of the terms and conditions of her pre-maternity employment while on maternity leave.

#### The Indirect Sex Discrimination Claim: s.19 Equality Act

The EAT also upheld Peninsula’s appeal in relation to Ms Donaldson’s claim for indirect sex discrimination. The combined effect of ss.39(2), 66, 70 and 76 Equality Act is to exclude from the Tribunal’s jurisdiction claims for direct sex and/or pregnancy and maternity discrimination contrary to s.13 Equality Act or indirect sex discrimination contrary to s.19 Equality Act, where the claim (as did Ms Donaldson’s) relates to an employee’s terms and conditions of employment. The EAT also

expressed some doubt as to whether, on the same analysis, the ET had any jurisdiction to consider claims for maternity and pregnancy discrimination under s.18 Equality Act.

### **Commentary**

The decision of the EAT in this case is significant for employers who offer childcare voucher salary sacrifice schemes, but do not offer enhanced contractual maternity pay and who have previously considered themselves bound by HMRC Guidance to continue to offer childcare vouchers from their own resources to employees during periods of maternity leave. Similarly, it will be reassuring to employers that offer a childcare voucher salary sacrifice scheme on similar terms to that of Peninsula's Scheme.

The Judgment in *Peninsula v Donaldson* also has potentially broader application. Although the EAT's decision related specifically to childcare vouchers, it is possible that the same analysis could be applied to other benefits provided under comparable 'salary sacrifice' schemes for the purpose of income tax and National Insurance relief for employees. Similarly, there is potential scope for the EAT's reasoning in *Peninsula v Donaldson* to be extended to the provision of childcare vouchers or alternative salary sacrifice benefits during other periods of absence, such as sickness absence, during which an employee is similarly entitled only to statutory pay.

The effects of the EAT's decision in *Peninsula v Donaldson* may, however, be curbed by changes to the taxation of childcare expenses that are due to be introduced in early 2017. Although employer salary sacrifice schemes will continue to operate for those who have already subscribed, the Government is planning to introduce a new Tax-Free Childcare Scheme, which is said to offer another option for tax savings on childcare direct through the Government. The decision in *Peninsula v Donaldson* will, however, continue to apply to existing employer childcare voucher salary sacrifice schemes.

**Anna Lintner**

**Ely Place Chambers**

**17 March 2016**

*Anna Lintner appeared as Junior Counsel for the Respondent in the EAT proceedings in Peninsula Business Services Ltd v Donaldson, led by John Samson of Ely Place Chambers.*