

Employment Issues Update

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In compiling this seminar session the presenter is indebted to the work of Peter Kiely, a partner in the specialist employment law firm Kiely Thompson Caisley, and Adjunct Professor of Law at Victoria University.

Individual Employment Agreements

Restraints of Trade (*Auto-Movements (NZ) Ltd v Eveleigh, Fuel Espresso v Hsieh, Credit Consultants v Wilson*)

We are regularly asked by Accountants, as well as by others, to advise on the enforcement of Restraint of Trade provisions in employment agreements. The usual situation of course is that an employee whose contract contains such a restraint has resigned and has taken up employment with a competitor. In general Courts treat restraints of trade in employment agreements with some suspicion. They will not be enforced if they were not properly incorporated into the employment agreement, or if they are unreasonable in their extent.

This means that a restraint of trade must either be included in a written contract given to the employee before he or she commences work, or added later on payment of consideration for the restraint. An

employee cannot be restrained from earning a living once the employment is over, but the restraint must be limited to protecting the employer's proprietary interests in its clients.

In the *Auto-Movements* case, the employee had originally been employed on a fixed term agreement which contained a restraint of trade. The employment continued beyond the end of the fixed term without a new employment agreement being entered into. The employee accordingly became a permanent employee, the terms of whose employment were implied by the previous fixed term agreement. In this circumstance, the restraint of trade was no longer effective in the Court's view because of the presumption against implying restraints of trade into employment agreements without clear evidence of agreement to do so.

In the *Fuel Espresso* case, Mr Hsieh was employed as a barista at Fuel Espresso in Wellington. He was trained by Fuel Espresso. Mr Hsieh's employment contract contained a restraint preventing him from working for a competitor within a 100m radius of any Fuel Espresso shop, or setting up a competing business within a 5km radius of any Fuel Espresso operations for three months after his employment ended. Mr Hsieh resigned and started working for a competitor about 70m from where he had previously been employed.

The Employment Court held that the restraint was void as there had been no additional consideration for it at the time the contract was entered into. The Court of Appeal disagreed and said that **extra** consideration was not required except when there was variation to an existing contract. The restraint was plainly reasonable in the Appeal Court's view and agreements were made to be kept.

A closely related concept to restraints of trade is the prohibition on the misuse of confidential information. The difference is that it is an implied term in all employment contracts that information not generally available in the trade but learned only as a result of an employee's employment and which could reasonably be considered confidential, must not be used by the employee for his or her own purposes after employment ends.

In the *Credit Consultants'* case, a Mr Wilson was employed as a General Manager reporting direct to the Managing Director. He had significant access to confidential information including information about customers, and he had been heavily involved in the Company's business development plans. His employment agreement contained a restraint purporting to prevent him from soliciting the Company's clients, or setting up in opposition anywhere in New Zealand or soliciting employees for a period of six months after termination of his employment.

Mr Wilson was made redundant and went to work for a competitor taking a quantity of confidential information with him. He actively solicited his previous employer's clients. The Court held that the restraint was reasonable in that it was designed to protect only the employer's proprietary interests in its clients. Given the nature of Mr Wilson's work it was reasonable for the restraint to cover the whole of New Zealand, and the time period of six months was also reasonable in the circumstances. The Court noted that Mr Wilson had accepted a restraint period of 18 months with his new employer.

In addition, the Court had no difficulty in finding that Mr Wilson was in breach of the confidentiality provisions of his contract, and was also in breach of the non-solicitation provisions.

All reasonably standard stuff, but what is interesting is the way in which the Court dealt with Mr Wilson's new employer. The Employment Court accepted that it had no jurisdiction to hear a claim for damages against the new employer (in other words compensation for any financial loss) as it was not a party to the case. But as a penalty against third parties is provided for in the Employment Relations Act, the Court was able to award a penalty (totalling \$5,000 in this case) against the new employer for knowingly aiding and abetting Mr Wilson to breach his employment agreement. The Court also awarded a total of \$6,000 against Mr Wilson for his breaches of his employment agreement. Damages were not awarded against Mr Wilson mainly because it was difficult to quantify the actual amount. The Court used its power to have the penalties paid to the previous employer rather than to the Crown.

It should be noted that while the Employment Court did not have jurisdiction to award damages against the new employer, the matter could have been pursued in the High Court where that jurisdictional issue would not apply.

Note that in earlier decisions a full bench of the Employment Court held that actions for breach of contract, and applications for injunctive relief (such as enforcement of a restraint of trade) must go first to the Employment Relations Authority. The Court does not have jurisdiction to hear such applications at first instance except in certain circumstances, the most notable being on "appeal" from the Authority.

The most effective action in dealing with an apparent breach of a restraint of trade remains a warning off of the employee and new employer, pointing out that the potential penalties are up to

\$5,000 for an individual and \$10,000 for an organisation.

Subsequently the High Court has considered similar issues (*Transnet NZ Limited v Dalahunty Power (NZ) Limited*) and confirmed the Employment Court's decision. The High Court added that where confidential information was obtained during employment **without** breach of contract, the High Court would have exclusive jurisdiction to deal with the matter after employment ended as the Employment Court's jurisdiction arose from a claim of breach of contract.

Accordingly the precise institution in which to file claims for damages for breach of a restraint of trade is a complex question, and depends on a range of subtle distinctions as to the legal basis for the claim.

Employment Agreements and Employer's Policies (*Cuttriss v Carter Holt Harvey Limited*)

The decision in this case makes it clear that for an employer's policies to be binding, they must be specifically incorporated into the employment relationship by the employment agreement. This could cause some problems in reaching a finding of serious misconduct by breaching a policy, when the policy has not been contractually incorporated. But in many, if not most cases, conduct justifying dismissal or a final warning will be self evidently misconduct with or without a written policy to that effect.

The disadvantage of including written policies into the contract is that where such policies are a contractual term of employment, they cannot be varied or removed without the agreement of the employees concerned.

The Test of Justification (Section 103A of the Employment Relations Act 2000)

In cases under the Employment Contracts Act the courts decided that the question of whether or not

an action by an employer was justified could be determined by reference by what a reasonable employer in the circumstances **would** have done. But by 2001 the generally accepted rule was that the appropriate test was whether or not the employer's action was something that a reasonable employer **could** have done, and this was confirmed at that time by the Court of Appeal in *W&H Newspapers Limited v Oram*.

In practice this test meant that the question became whether the employer's actions came within the range of responses open to a fair and reasonable employer. This was generally considered to give greater flexibility to employers because even if a decision was particularly harsh, as long as it was within the range of decisions **open** to a reasonable employer that was all that was needed.

As the law developed through the nineties there had been an increasing emphasis on procedure. In early decisions the question was whether the procedure followed by the employer was sufficiently flawed that the substantive decision was suspect, but by the time of *Oram*, there was a greater separation between procedure and substance. A dismissal for example could be substantively justified (that is the employee did it) but the procedure flawed. In that situation, the faulty procedure rendered the dismissal unjustified even though the employee was guilty of the alleged conduct.

This is not as unreasonable as it sounds, because at the same time the compensation payable to the employee was limited to the distress caused only by the faulty procedure not the dismissal. And as the employee would have been dismissed even if a fair procedure had been followed, there was no repayment of lost wages.

On 1 December 2004, a new section was inserted into the Act which returned the test to a consideration of what a fair and reasonable employer **would** have done in all the circumstances

at the time of the action complained of. This caused some consternation amongst employers who felt it would now be more difficult to justify a dismissal, warning, or other action.

The change to the legislation did not apply to employer's actions prior to 1 December 2004, and so it was some time before decisions on section 103A were considered by the Court. A number of recent decisions have shown that employers had no cause for alarm.

In essence following a number of cases in recent months, the current situation is this: any particular aspect of an employer's actions which affect employees adversely may be examined, and that examination will ask "is this what a fair and reasonable employer would have done". But the overriding consideration is whether the procedure as a whole passes that test, without unnecessary nit-picking about procedural flaws which had no real effect on the outcome. So again it becomes relevant to ask whether the faulty procedure actually resulted in an unsafe decision on the substantive allegation.

We do not of course recommend that employers make procedural errors. This is relatively easy to do with the Act's requirements of good faith and various judicial pronouncements on what does or doesn't constitute fair procedure. But employers can take some comfort from the fact that if they treat an employee fairly and reasonably, and any procedural slips are relatively minor having little or no effect on the final outcome, they are likely to have done what a fair and reasonable employer would have done in all the circumstances.

But the law should still be considered as developing in this area.

Employees and Contractors

There have been a number of cases recently about whether or not a worker is an employee or a

contractor. The complexity of this issue is demonstrated by the case of *Bryson v Three Foot Six*, which involved a model maker on Lord of the Rings. The Employment Relations Authority determined that Mr Bryson was an independent contractor, the Employment Court held that he was an employee, the Court of Appeal decided that he was an independent contractor, and the Supreme Court decided he was an employee.

The Act requires the Court to determine the real nature of the relationship, and in doing so to take into account all relevant matters. This includes the employment agreement itself, and the existing common law tests. The determination is a balancing exercise with the Court putting the indicators of an employment relationship on one side of the scale, and the indicators of an independent contractor relationship on the other. How the parties themselves describe the relationship is only one factor.

The common law tests involve consideration of the level of control exercised over the worker by the "employer", whether or not the worker is an integral part of the employer's business or just providing ancillary services, and whether or not the worker could reasonably be described as being in business on his or her own account.

In the half dozen cases decided since *Bryson*, most have held the worker to be an independent contractor. But all employment lawyers are frequently faced with providing contracts for relationships which purport to be principal and contractor, but are clearly employment relationships. The key factors which should raise alarms for accountants are situations where the "employer" has a high level of control over the day to day activities of the worker, and where the worker is an integral part of the business. A person delivering pamphlets for a pamphlet delivery business is more likely to be an employee. A person delivering pamphlets for a plumber is more likely to be a contractor.

Whether or not the person is in business for themselves is sometimes self evident, sometimes not. The method of taxation is an important consideration but not determinative. In many ways the taxation arrangements do no more than repeat the parties view as to the nature of their relationship, which is one factor only.

A recent High Court case (*Sensation Yachts Ltd v The World of Interiors Ltd*) sounds a word of caution for those employees who see tax advantages in being contractors. A common situation is for the "employee" to set up a company and for the employer to then contract with that company for the provision of the employee's services. This is sometimes done in the mistaken belief that the company tax rate will apply, rather than the personal rate. Of course the attribution rules in a situation like this would usually remove that tax advantage, but the introduction of a company between "employer" and worker is a helpful factor to go on the independent contractor side of the scales.

The cautionary note relates to what happens when there is a subsequent breach by the employer, most usually repudiation of the contract (in employment terms a "dismissal"). The worker's company would normally be able to claim loss of profits for the breach, although lost profit is notoriously difficult to calculate. But when all the company's income was to be used to pay the worker it would have made no profit. This means it has lost nothing and so has no claim for damages against the "employer". (In theory the worker could apply to the Court for relief under the Contractual Remedies Act as a claimant through a party to the contract (section 9(7)). This would have to be done through the Court's of general jurisdiction (District and High Courts), and would be opening up new areas of law).

There can be advantages to employers in those working for them being classed as independent contractors, and advantages to those doing the work in being classified as employees. A well

advised employee will not lightly give up those advantages.

Off the Record Discussions (*Bayliss v McDonald*)

Letters exchanged in attempts to resolve employment relationship problems are often headed "without prejudice". Without prejudice correspondence cannot be used as evidence in later judicial proceedings, the reasoning being that the public interest in resolving disputes without court action outweighs the private interest in the outcome of the dispute in question.

What is not generally understood is that the heading "Without Prejudice" does not in itself provide that protection. Before an evidential privilege arises there must be an actual dispute between the parties, and the correspondence must contain a proposal to resolve that dispute. If both conditions are not satisfied the correspondence is admissible evidence in later proceedings regardless of whether or not it was stated to be without prejudice. The same considerations apply to verbal statements.

In the *Bayliss* case, the employer held a disciplinary meeting with the employee, both employer and employee being represented. During the meeting, the employer's representative suggested an "off the record" discussion with his counterpart. During that discussion, the employer's representative suggested a payment in return for the employee's resignation. This was agreed, but unfortunately there had been a misunderstanding between the representatives as to the precise terms under which the employee would resign. The employer then required the employee to return to work. She refused claiming to have been constructively dismissed by the employer seeking her resignation at the meeting.

The Court held that there was no dispute between the parties at the time of the meeting, a dispute being defined as a significant difference between the expressed views of the parties about a matter

concerning them both. As there was no existing dispute the "off the record" discussions between representatives was admissible in evidence, and the employer's offer of payment if the employee resigned was a key ingredient in her claim to have been unjustifiably constructively dismissed. The same reasoning would have applied to a "without prejudice letter.

There are earlier decisions of the Court to the effect that the statutory confidentiality attaching to formal mediation applies only to statements made by the parties in mediation which were intended to assist in resolving the employment relationship problem which was the subject of mediation. Any statements not aimed at resolving the employment relationship problem are accordingly admissible in evidence, including any offers of payment in return for the employee's resignation.

Putting the two principles together, it is clear that considerable care must be exercised by an employer who wishes to suggest an exit package in return for a resignation. Achieving confidentiality for such an offer whether inside or outside of mediation is particularly difficult and should not be attempted without assistance.

Remedies (*Simpson Farms Limited v Aberhart, EPMU v Terry Young Limited*)

Last year the Court of Appeal commented that awards of compensation for hurt and humiliation should be relatively modest and in line with earlier decisions. As a result the view was widely expressed that the Court had effectively put a notional ceiling on such compensation of \$27,000.

In *Aberhart* the Chief Judge of the Employment Court took the view that the Court of Appeal could not have intended to set a ceiling, as there was no ceiling on awards in the Act. There had also been a number of earlier decisions in which the Court of Appeal had sanctioned higher awards.

The Employment Court also noted that the great majority of employment cases are settled in mediation, some for amounts well in excess of those awarded by the courts. This is presumably because it is in the party's interests to settle justifiable claims for high levels of compensation. In the instant case, the Court upheld an Authority award of \$15,000 compensation.

In the *EPMU* case a penalty for breach of good faith was awarded against the employer. The Union claimed that the employer had attempted to persuade staff not to join the Union and not to negotiate a collective agreement. The employer also spoke to some employees individually arguing that by being in the Union the employee gave up their right to negotiate their own employment, and that the Union did not care about the employee but was only after their money.

The employer claimed that the purpose of these meetings and conversations was to ensure the employees knew that the decision whether or not to join the Union was a matter for them alone. But the fact was that in the following months several employees resigned from the Union. The employer then proposed a credit union scheme in which employees and the employer would both contribute to an investment fund for the employee's benefit. This was only proposed to non-Union members, and did not proceed.

As the employer deducted Union fees on behalf of the Union, the Union wrote advising the employer of a fee increase. The employer put a notice on staff notice boards incorrectly stating that the Union's fee increase was 18%.

In all these circumstances the Authority had little trouble in determining that the employer's actions were intended to undermine Union membership and influence employees not to be involved in collective bargaining. The employer had also misled employees about the Union fees. A penalty of

\$6,000 (the maximum being \$10,000) was imposed against the employer.

Public Holidays (*NZ Fire Commission v Firefighters Union, Air New Zealand v New Zealand Airline Pilots Association*)

There have been some helpful cases on Public Holidays over the past two years; two involving the Fire Service and one involving Air New Zealand.

Pay

In the most recent Fire Service case, the Service paid its fire fighters a regular amount each pay day to cover work done, or to be done, on public holidays throughout the year. The Court held that while this arrangement was consistent with the requirements of the Holiday's Act for calculating the amount of payments for public holidays, it was inconsistent with the Act in respect of the timing of that payment. The Act requires payment for a public holiday to be made in the pay period on which the public holiday falls. It follows that regular payment throughout the year for public holidays worked is a breach of that requirement.

Alternative days

In the earlier Fire Service case, the Court of Appeal held that having a roster cycle which provided for regular additional days off satisfied the Holidays Act requirement that an alternative paid day off must be provided when a public holiday is worked on a day that is a normal working day for the employee.

The requirement is that the alternative day off must also be on a day which would otherwise have been a working day for the employee, and the roster satisfied that requirement.

Transferring public holidays

The Court also confirmed that another method of dealing with work done on a public holiday is to agree with the employee in question that the public holiday will be transferred to a different day. This is a different situation from an alternative day off. If a

public holiday is transferred, the employee is paid the ordinary rate of pay for working on the day of the original public holiday as for that employee the day is no longer a public holiday.

When you see the number of cafés which have a surcharge for public holidays, it is clear that these employers at least are unaware that all the staff working on that day could be paid at ordinary time, if they had agreed to observe that public holiday on a different day. There is no way the employer can avoid providing 11 paid days off to full time workers for public holidays, but the payment of time and a half can be avoided by a prior agreement to transfer the holiday.

But how specific must that transfer be? In the *Air New Zealand* case the Court of Appeal made it clear that the "exchange day" to which the public holiday is transferred must be identified and agreed before the original "public holiday" on which the employee has agreed to work. That means that the actual day to which each holiday is transferred must be identified, an agreement to agree the actual day later is not enough. And it is not open to employers or employees to decide after the event that a particular public holiday on which the employee worked will be treated as having been transferred to a different day.

In summary if an employer wishes an employee to work on a public holiday and take another day as an alternative, one option open to the employer is to seek the employee's agreement before the public holiday in question that the employee will take that public holiday on a particular alternative day.

Annual Leave Entitlements (*NZ Tramways Union v Transportation Auckland*)

The question in this case was whether those employees who were receiving four weeks annual leave instead of the statutory three would be entitled to five weeks when the statutory entitlement increased on 1 April 2007.

The Court's decision was that such an increase was not automatic but depended on the wording of the contract. In this particular case, the contract provided that in addition to the three week's holidays provided by the Holidays Act 1981, the employees would be entitled to a further holiday of one week each year in recognition of the nature of their work, making a total of four weeks a year.

The Court held that the extra week of annual holiday was merely an enhancement to the minimum entitlement under the Act of three weeks. The Court took note of the fact that the contract referred to the 1981 Act (which provided for only three weeks) and not to the 2003 Act with its 4 weeks annual leave after 1 April 2007. If the contract had been intended to enhance the four weeks under the 2003 Act (which had been passed at the time), the contractual reference would have been to that Act and not to the earlier statute.

In other words the Court reached the unsurprising conclusion that whether or not an additional week's leave provided in a contract is to be added to the four weeks now required under the Act is a matter of interpretation of the particular contract. In some contracts it is clear that employees will be entitled to four weeks after a qualifying period (such as six years service). A simple clause of that nature would not require the employer to provide five weeks under the new statute. Other contracts provide the "annual leave provided by statute" with an **additional** week's leave after a qualifying period. Such a clause would clearly require five weeks leave for employees who qualify. Of course there are numerous contracts which are not so clearly worded and it is these which cause the problem.

Collective Employment Agreements

Employer Communications With Employees During Bargaining (*Christchurch City Council v Southern Local Government Officers Union*)

In this case, the Court of Appeal overturned the Employment Court's ban on employers communicating directly with Union Members during the bargaining process. The Court of Appeal took a much narrower view than the Employment Court on what constituted bargaining. The net result is that employers are able to communicate with employees about the bargaining **process**, so long as their communications do not undermine the bargaining and do not amount to negotiation of terms and conditions of employment. This prohibition applies only from the time at which bargaining for a collective agreement is initiated, until the time when it is finished.

Of course the employer and union can agree on wider communications, or more restricted communications if they choose.

Passing on of Collective Terms (*National Distribution Union v General Distributors Limited*)

In December 2004, one of the swerves to the left was that the Act was amended to prohibit automatically passing on the terms and conditions negotiated by unions on behalf of their members to non-union employees, and to provide a regime for the payment of bargaining fees by non-members who wished to have the terms and conditions of union members.

Individual employees can opt out of the bargaining fee arrangement (that is it cannot be compulsory). The more contentious issue is identifying when terms negotiated with the union have been automatically passed on to non-union members. The obvious example would be a 5% wage increase negotiated into a collective agreement. If the employer then automatically applies that 5% increase to all employees it runs the risk of breaching the relevant provisions.

The Court decision makes it clear that it will be very difficult for a Union to prove passing on. The term or condition passed on must be "the same or

substantially the same" as the term in the collective agreement. Substantial similarity is not sufficient. Also the employer's intention in passing on the term and condition must be to undermine the collective agreement; intention is notoriously difficult to prove. And the collective agreement must **actually** be undermined. Unlike the restrictions on communications during bargaining, it is not enough just to undermine the union or the bargaining process; it is the agreement itself which must be undermined. As yet there are no examples of how a collective agreement can be undermined, if it is possible at all.

Adding New Employers to Collective Agreements (*Epic Packaging Limited v EPMU*)

As you are probably aware, bargaining for a new Collective Agreement can commence (by notice from the Union) 60 days before expiry of the Collective, or (by notice from the Employer) 40 days before the date of expiry. Once bargaining has been initiated and the existing Collective Agreement has expired, employees are free to strike in support of their claims, and employers are free to lock out employees in support of their claims.

There is also provision in the Act for additional employers to be added to an existing Collective, which if the employer agrees will then become a multi-employer collective agreement (MECA). The effect of the *Epic Packaging* case is that strikes and lockouts can be used as a tactic to persuade a new employer to join an existing CEA only after bargaining has been initiated with (or by) the existing employer party in accordance with the Act.

Performing Striking Employees' Duties (*National Distribution Union v General Distributors Limited, EPMU v Air Nelson, Service and Food Workers Union v Spotless Services*)

The Act prohibits an employer from employing or engaging another person to do the work of striking or locked out employees. But other employees can

agree to do the work of colleagues who are on strike or locked out provided they have not been employed specifically for that purpose.

In the *NDU* case employees at a grocery distribution centre went on strike, and arrangements were made for another company to carry out their work. The evidence was not clear as to whether it was the employer or the suppliers of the goods who had made these arrangements. The use of the other company was held not to be a breach of the Act as the arrangements for their employees to do the work of those on strike may well have been made by the supplier and not by the employer of the striking workers.

In the *Air Nelson* case freight handlers went on strike, and managerial employees of Air New Zealand (Air Nelson's parent company) loaded freight onto aircraft. The Authority's determination that this was not a breach of the Act was overturned by the Court. The Court held that this was different from the *NDU* case in that the employer (Air Nelson) had arranged for Air New Zealand and/or its employees to undertake the work.

In the *Spotless Services* case, Spotless was responsible amongst other things for cleaning various District Health Board sites. The employees had notified the commencement of rolling strike action. The company then locked employees out in order to obtain their agreement to a minimum number of employees remaining available to reduce any risk to patient health. The Court held that the lockout was unlawful as the right to strike could be curtailed only by the existing statutory constraints. When the statutory constraints did not apply as in this case, the employer had no right to restrict in any way the employee's right to strike, and so had no right to use a lock out to obtain their agreement to such a restriction.

In summary then, if an employer cannot provide a particular service to a client because of strike action, there is nothing to prevent that client from

making alternative arrangements to do the work of the striking employees. But it is not open to the employer of the striking workers to make those arrangements, nor is the employer entitled to use a lock out to force striking employees to agree to restrict their strike action. It is always open to an employer of course to ask the Union to make suitable arrangements, but it cannot require the Union's agreement.

After Words

Some rules are absolutes, such as when payment for public holidays must be made, but others are more subjective. Far fewer employers would get into trouble if they consulted meaningfully with employees before they make decisions affecting the employee, and if they asked "how would I like to be treated in this situation". Fewer still would have problems if they also took professional advice before acting rather than after the employee has complained.

There will always be lunatic claims from employees. But better to be defending a lunatic claim than one where the employee has a reasonable chance of success.



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