



LABOUR FLEXIBILITY AND THE LEGAL REQUIREMENTS FOR REDUNDANCY DISMISSALS

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Abstract

New-right economists and many employers argue that an efficient labour market requires that an employer should face few constraints on the right to dismiss workers as such constraints limit the employer's flexibility to adapt to changes in the marketplace and may inhibit the employer in hiring new labour. Others argue that an employee is entitled to be treated fairly whenever their security of employment is in jeopardy. The latter perspective is the one that has received legal endorsement by both the Employment Court and the Court of Appeal. This paper will examine the way in which the Courts have applied this principle in situations where a worker has been dismissed because of redundancy. It will discuss legal developments in the area and comment on the extent to which the legal requirements may inhibit an employer's decision making relating to reductions in its labour force.

The economic restructuring of the past decade has involved massive numbers of redundancies. In the main this disruption to people's lives has been regarded as a cost of gaining increased flexibility in the labour market with scant attention having been paid to the cost to the individuals affected. Indeed social welfare and labour law changes have worsened further the position of those affected. Any suggestion that such workers deserve some degree of protection has been met by hostility from employer spokespersons and new-right economists. Those who support this position have argued that employment protection laws are one of the remaining obstacles in the way of a fully flexible labour market (Brook, 1991).

It is not my intention in this paper to explore the nature of these arguments. Instead the paper is primarily concerned with the state of the current law relating to redundancies and some possibilities for reform. The basic argument of those opposed to any labour market intervention should, however, be briefly mentioned. It appears to hinge on the argument that the costs of redundancy compensation, and indeed any restrictions on dismissing workers at will, are such as to deter employers hiring new or replacement labour. Hence employment protection hinders the fully efficient use of labour. More fundamentally such theories effectively exclude an obligation for an employer to act fairly, assume that labour is purely a commodity to be disposed of at will and take little or no account of the impact of termination on employees.

The hostility of employer groups to any form of employment protection has been apparent since the passage of the Employment Contracts Act and it has been argued that the failure of the Act to severely restrict employment protec-

tion was a major defect. The most direct statement of the employer position is to be found in a joint paper by the New Zealand Business Roundtable and the Employers' Federation (NZ Business Roundtable, NZ Employers' Federation, 1992). In that paper it was proposed that, in the absence of a specific agreement to the contrary, all employment protection be abolished except for a requirement to give two weeks notice of the termination of employment.

This paper will discuss only redundancy terminations. In the case of other terminations Parliament has clearly decided that there should be protection against unjustified dismissal.¹ This paper will look at two aspects of the law on redundancy. The first are the situations in which the law potentially requires an employer to pay redundancy or other compensation to a dismissed employee. The second will consider the international labour standards on redundancy dismissals and some areas where reform of the law might be justified.

The obligation to pay redundancy compensation

An employer's current liability to compensate a worker for redundancy is largely dependent on the terms of the contract of employment. Most obviously if there is a specific term in the contract that term must be observed and can of course be enforced by legal action. According to the Department of Labour (1994) 45 percent of their surveyed contracts (covering 51 percent of workers) have either a substantive redundancy provision or refer to a separate agreement. A greater proportion, 71 percent, have a notice provision. It would seem reasonable to claim

that a substantial group of workers have no legal entitlement to redundancy compensation given that the department of Labour surveys only larger collective contracts. The only other legal liability relates to the period of notice of termination. The same Labour Department survey indicates that most workers have an average entitlement of about four weeks notice. The Department of Labour does not indicate how many, if any, contracts specifically exclude redundancy compensation, a point that, as is explained below, may be of some importance. It should also be noted that redundancy compensation is not protected by insolvency legislation in most cases (as opposed to wages owing) and so if the employer is insolvent any redundancy agreement may be practically useless in the face of the priority claims of the large financial institutions.

In the absence of a contractual entitlement to redundancy compensation a worker's only other options are to negotiate compensation when made redundant, not the most propitious time for such negotiations, or to rely on the personal grievance provisions of the Employment Contracts Act. It is this latter course that is discussed below. It is now clear that the Employment Tribunal and Court can now award such compensation in limited circumstances. This development, which has been apparent since 1991, has caused considerable controversy. The basis for the criticism of the courts has been the argument noted above that it is a barrier to labour flexibility. In addition it is argued that the courts are acting contrary to the philosophy of the Employment Contracts Act, that the courts are interfering in the contract between the parties and that the developments create business uncertainty. Regardless of this, it is now clear that the courts have the power to make such awards.

Redundancies and personal grievances: the *Bilderbeck* case

Since the decision of the Court of Appeal in *Brighouse Ltd v Bilderbeck*² the law on dismissals has been considerably clarified. The first point, that should be made, and which has been clear since the *Hale*³ case, is that a genuine commercial decision to make an employee redundant cannot be attacked through the personal grievance procedure. In that case the Court of Appeal made it clear that the nature or wisdom of a commercial decision to make employees redundant was not a matter for the courts. Cooke, P said:

this Court must now make it clear that an employer is entitled to make his business more efficient, as for example by automation, abandonment of unprofitable activities, re-organisation or other cost-saving steps, no matter whether or not the business would otherwise go to the wall. A worker does not have the right to continued employment if the business could be run more efficiently without him. The personal grievance provisions ... should not be treated as derogating from the rights of employers to make management decisions genuinely on such grounds. Nor could it be right for the

Labour Court to substitute its own opinion as to the wisdom or the expediency of the employer's decision. When a dismissal is based on redundancy, it is the good faith of that basis and the fairness of the procedure followed that may fall to be examined on a complaint of unjustified dismissal...the Court and the grievance committee cannot properly be concerned with an examination of the employer's accounts except so far as it bears on the true reason for dismissal (*Hale* : 155).

This decision meant that the courts could only be concerned with two issues; was the decision in fact a genuine commercial decision, and was it implemented in a manner that was procedurally fair. The former issue is not usually one that arises where a number of redundancies are contemplated. The latter requirement arises, of course, from the principle that a dismissal that is procedurally unfair will constitute an unjustified dismissal regardless of the substantive nature of the decision.

What then is the impact of the law of personal grievances on a decision to make a worker redundant? The *Bilderbeck* decision has now clarified the law and has essentially supported the approach adopted by the Employment Court since the *Hale* decision. The case did, however, reveal a clear division in the Court as to the extent procedural fairness is relevant in a redundancy dismissal. The first point that should be made, is that the Court as a whole agreed that a dismissal for redundancy must be carried out in a procedurally fair way. The dispute was not over this point but over whether compensation awarded for the failure to do so could extend to compensation for the redundancy itself, or, to put the matter another way, could procedural fairness include an obligation to pay redundancy compensation. It was accepted by all the judges that a failure to give proper contractual notice or pay in lieu, conveying the decision in a way that is likely to cause additional distress and humiliation or that does not take into account the legitimate concerns of the employee are all possible grounds or compensation. For example, Gault J in his dissenting judgment, mentioned failure to provide assistance with alternative employment if that was appropriate or failure to give notice so as to maximise the opportunity to find other work. Richardson J, also dissenting, said that procedural fairness may require "counselling and job assistance and retraining and that the employer also provide a cushion either by allowing additional time beyond the contractual period of notice or by payment in lieu."

The more controversial aspect of the case, and the previous decisions, is whether compensation can be awarded for the loss of the job as such. Following *Bilderbeck* the law now seems to recognise three possible situations. It must be stressed, as Cooke P made clear that there is no general right to compensation for redundancy as is the case in some countries but instead rights must be negotiated as part of the contract of employment. The three situations that are now recognised are:

(i) If the contract has a clear provision providing for compensation for redundancy then this provision will be definitive of the matter. Having agreed to a fixed sum of compensation or a formula for its assessment one party cannot claim that it is procedurally unfair when it is applied.

(ii) The contract specifically provides that there is to be no compensation for redundancy. Again the contract will be definitive unless there are exceptional circumstances. While such a contract may be unfair, the worker will have specifically agreed to the position when employed.

Of these two situations Cooke P said "If the contract contains an express provision and formula for redundancy compensation or (less likely) an express provision that there shall be no such compensation, no doubt it will govern, save possibly in very exceptional circumstances." but went on "Where no express provision applies, the ordinary personal grievance procedure will be available..."

One or other of the above options is likely to be favoured by employers following *Bilderbeck* as they give certainty to the employer's position at least in respect of the redundancy compensation aspect of the termination. Which option is achieved will of course depend on the relative bargaining position of the parties.

(iii) The third situation is where the contract is silent on the matter. This was the situation in *Bilderbeck*. Sir Gordon Bisson made the point that if the contract was silent on redundancy it did not mean that no compensation was payable on redundancy. It merely meant that "The contract is simply silent on the issue leaving it open to be considered in the circumstances of each dismissal." It is in this situation that the courts may decide that compensation is payable. This decision is not inevitable and will be based on principles that have developed since the *Hale* decision.

These principles were summarised by Chief Judge Goddard in the Employment Court's decision in *Bilderbeck* as:

1. Not every redundant employee is entitled to compensation.
2. In considering the overall duty of fair treatment incumbent on every employer, the Court may inquire whether the case calls for compensation for redundancy.
3. In the absence of a prior agreement to pay compensation for redundancy the answer to the question whether the duty of fairness calls for payment will depend on circumstances such as -
 - the reason for the redundancy;
 - the length of service of the employee;
 - the period of notice of dismissal;
 - the means of the employer to pay.
4. Circumstances calling for a compensatory payment

as part of the overall duty of fairness may arise in the absence of a prior agreement where, for example, an employer has voluntarily decided on redundancy as a cost-saving measure and can reasonably afford to pay compensation.

5. The fact that some compensation has been offered [or, I would add, paid] is a relevant factor in determining whether, as a whole, the employer's conduct has been fair and reasonable."

These various factors must be balanced in each case and the Court has taken particular account of the employer's ability to pay especially where the redundancies are part of a restructuring or cost saving measure rather than for survival or solvency reasons.

The *Bilderbeck* case did reveal a strong division of opinion between the majority and minority opinions. Richardson J in particular argued strongly that the personal grievance provisions was not appropriately used to pay redundancy compensation. His views appear to have been strongly influenced by three factors. The first was a need for certainty in the law, secondly a view that if the contract was silent the parties had decided not to allow for redundancy pay and that this agreement should not be overridden by the courts. Finally he was of the view that the question of redundancy pay was one for Parliament and not the courts.

Richardson J can be criticised on several points. One particular point, and indeed the one central to the majority decision as well, is whether silence in the contract means that the issue of redundancy pay was fully considered by the parties. Richardson J appears to take the view that the negotiation of a contract of employment is a rational considered exercise involving various concessions as well as gains and seems to imply that the result will be an agreement addressing all relevant employment issues. His quote from the old Arbitration Court in *NZ Related trades IUW v NZMC Ltd* [1983] ACJ 233, which makes this point, in fact refers to a formal industrial negotiation. Since 1991 this scenario has concerned a substantially reduced number of people, a situation which is especially likely to be so in smaller enterprises and with middle level employees. It is this type of employee that has featured in many of the redundancy cases. In such situations issues such as the term of employment may not have been fully considered and, equally significantly given the ongoing relational nature of the employment contract, the nature of the original position may have changed substantially since initial employment. It is such situations that the flexible attitude adopted by the Employment Court is most appropriate. What may be fair after six months employment may not be so after a considerable period of employment and loyal service.

The judgments in the Court of Appeal also reveal a strong division within the Court on the nature of the contractual relationship and on the possible role of the Court in relation to wider questions of social policy. The minority opinions,

and especially that of Richardson J, have clearly been attracted by elements of the law and economics rhetoric and a classical notion of contract. They reject the idea of the courts having a strong policy role. Richardson J states "it is not open to the courts to construct an extra-statutory concept of social justice applicable in redundancy situations" and later that "The social and economic policy implications of possible redundancy regimes call for careful analysis" and that they are "surely for the legislature and not the courts."

The majority on the other hand appears to be more cognisant of the need to deal with the realities of the employment relationship and to take account of inequalities of bargaining power. Casey J in particular accepted this point. He explicitly stated that he could understand the desire of the Court and Tribunal to secure fair treatment where employees, especially in smaller firms, have little ability to achieve satisfactory redundancy deals in their contracts and in a climate "engendered by restructuring and extensive dismissals, where redundancy payments have become commonplace in the major undertakings affected." Cooke P noted that the personal grievance provisions had not been curtailed in respect of redundancy by the Employment Contracts Act in 1991 and commented that "The emphasis on efficiency and market forces is thus accompanied and in a sense balanced by a reaffirmation and broadening of the scope of personal grievance remedies." He contrasted the lack of changes to the personal grievance provisions in the Employment Contracts Act with the changes to the dispute of rights procedure where restrictions had been imposed on the Court's power to determine redundancy compensation in rights disputes.

A standard for reform: the ILO convention and recommendation

The *Bilderbeck* decision will allow compensation for redundancy in some limited situations. The standard on which compensation will be based appears, to be that of the fair and solvent employer. The case will not apply where there is a clear contractual term on redundancy compensation. The case thus does little to provide an equitable and rational system designed to provide a degree of protection and stability for employees where there is a redundancy. The basic philosophy of the present situation is that redundancy is a matter for negotiation, ignoring of course respective industrial strength. Sensible labour market planning would suggest a more rationale approach to the problems caused by economic induced dismissals, at least to the extent of some minimum standards. The remainder of the paper raises some of the issues that reform should address.

One indicator of the minimum level of reform that might be sought can be found in ILO Convention 158 'Concerning Termination of Employment at the Initiative of the Employer' and the associated recommendation No 166. Convention 158 provides for:

- (a) consultation with the worker's representatives. Such consultation should involve the provision of information on the reasons for the redundancy and its extent and is designed to allow discussions on the possibilities of reducing the terminations and minimising their effect.
- (b) notification to the 'competent authority.'

The Recommendation goes further in elaborating on the measures that should be taken to deal with and minimise the effects of redundancy terminations. The Recommendation specifically refers to the need to balance the recommended measures with the efficiency of the enterprise. The recommended measures include early consultation on technological change, the provision of relevant information to facilitate consultation, and measures to avert the need for terminations. It is recommended that these include reductions in hiring, natural reduction, retraining, restrictions on overtime and the like. The recommendation also stresses the need for selection to be made according to criteria established in advance and which balance the interests of both the enterprise and the workers.

The ILO standards recognise the need for redundancies but provide for measures to help alleviate and minimise such terminations. They do not impose undue obligations on employers but they do attempt to ensure that workers interests are considered. To a large extent it is these principles that are at the heart of the *Bilderbeck* case. Nevertheless there is no general legislation in New Zealand to ensure that such considerations are taken into account, let alone that more concrete protection such as minimum notice periods or some degree of compensation are provided. While there are those who support the expansion of the minimum code to include statutory provisions for redundancy (Brosnan and Rea, 1991; Wallis, PL, 1992 and the Labour Party, 1993) and even those who have suggested that a compulsory compensation scheme be developed to help those who lose jobs due to redundancy (New Zealand Planning Council, 1980) their voices are largely ignored by those who worship the chimerical god of freedom of contract. Apart from basic standards, problems can also arise because of business rearrangements which have the effect of creating redundancies. The remainder of the paper addresses the lack of a mandatory period of notice; and the lack of rules relating to the transfer of business undertakings. Both are deficiencies which should be eliminated by statutory provisions. While they do not cover the whole of the problems posed they do provide examples of two weaknesses in the current law.

Mandatory notice periods

In most respects New Zealand law accords with the international standards in Parts I and II of ILO Convention 158 relating to termination of employment, although not Part III on redundancy. The exception, which relates to all terminations including redundancy, is that in New Zealand there is no *entitlement* to either reasonable notice or redundancy compensation.⁴ This fails to accord with

Article 11 of the Convention which provides that a worker shall be "...entitled to a reasonable period of notice or compensation in lieu thereof", nor Article 12 which relates to severance allowances.

At present, workers potentially face a double-edged sword. When an employer is in severe financial difficulty, employees may know nothing of this situation until faced with little or no notice of redundancy. In the worst case the employer may immediately go into liquidation. In such cases, if no redundancy pay offer is made, an action for unjustifiable dismissal is pointless as the Court, looking at the employer's situation, will not make an award of compensation. Thus employees suffer detriment from both the suddenness of their redundancy and the lack of redundancy compensation. Some of this detriment would be alleviated if there was a mandatory period of notice. If this period was reasonably substantial, say four to eight weeks, it would allow employees greater time to adjust to the dismissal in both financial and psychological terms. It would also provide time to look for alternative employment. There appears to be support for the proposition that reasonable advance notice (two months) is effective in reducing re-employment earnings losses and the probability of post-dismissal unemployment (Nord, and Yuan Ting, 1991). If, as seems likely, employers cut back on redundancy compensation the unwillingness of some, and the inability of others, to compensate means that the detriment suffered by redundant workers should be alleviated by other means. A mandatory notice period would provide at least a minimal degree of protection.

Transfers of undertakings

Employers in New Zealand recently lost an effective tool for reducing conditions and wages when the partial lock-out was outlawed.⁵ It is possible, therefore, that they will attempt to use other means to achieve the same ends. One such possibility is to take advantage of company law to organise corporate structures with many small associated companies and then liquidate them should changes to the workforce or employment conditions be desired. The absence of redundancy law regulating transfers of undertakings allows the exploitation of such methods. Another development likely to exacerbate this deficiency is the increased freedom in relation to company restructuring⁶ and the influx recently of multi-national companies. These two factors are likely to increase in the number of mergers and takeovers, the very thing which precipitated the European Union and United Kingdom moves to protect employee's interests in this context (Bourn, 1983).

The consequences of restructuring can have quite different impacts depending on the means adopted. Whenever an employer disposes of the business undertaking to a third party, employee's positions effectively become redundant as contracts of employment are legally non-transferable, whether or not a new owner is prepared to hire the employees on the same terms and conditions. This does not, however, apply in the situation of a simple transfer of

company shares as the same legal identity of the employer is retained. In practice, however, the transfer of company shares may in practice result in a very different type of employer. A transferee company may bring in a totally new management team, amend the constitution, and change the whole nature of the business. The non-contractual work situation (voluntary overtime, fringe benefits and promotion) may be unilaterally changed. In the absence of statutory protection to the contrary, employees will be powerless to legally stop this and will have little or no input into their destiny. Problems may also arise should a transferor fail to make an offer of compensation to employees (assuming there is no contractual obligation) in situations where complex arrangements involving exchanges of shares for assets or liquidation of the parent company is involved. The transferor company may become an empty shell devoid of assets, yet remain the nominal employer and thus have no funds with which to pay compensation.

The Transfer Of Undertakings (Protection of Employment) Regulations 1981 which operate in the United Kingdom may give some guide to possible reform. These essentially comply with EU Council Directive 77/187, and contain a duty for employers to inform and consult with employees about impending transfer of undertakings. Furthermore, in relation to transfers of subsidiary companies by receivers and liquidators in "hiving down" situations, employees still remaining in the employment of the parent company are automatically transferred to the subsidiary upon its sale. Hence they are acquired as employees by the third party purchaser. In this way the employees are protected from technical redundancy.

United Kingdom style regulation of 'hive downs' would go a long way towards protecting against artificial redundancies. The regulations provide that the dismissal "...of any employee of the transferor...either before or after a relevant transfer is an 'unfair dismissal' if the...principal reason for the dismissal is the transfer or a reason connected with the transfer..." But it will not be 'unfair' if the dismissal was for a substantial (economic or organisational) reason. It is arguable that a similar provision would give protection against some types of the employer tactics mentioned above.

Conclusion

The above discussion of current redundancy law identifies deficiencies amenable to statutory reform. While the current legal situation gives a degree of protection to some, and in practice a very small minority, of workers most workers are left to cope as they can. At a time when Australia has seen fit to legislate towards meeting its international obligations⁷ criticism of the New Zealand Government for not taking its international obligations and reputation seriously is particularly pertinent. The theory that the market will provide the best solutions is not one that is universally observed. The past year has been marked by much legislative activity directed towards new statutory protection: for consumers under the Consumer

Guarantees Act and for financial information users as a result of the Financial Reporting Act. Notably absent however, has been any attempt to afford extra employment protection, or information, for workers. In his dissenting judgment in *Bilderbeck Richardson J* suggested "previous long service, loss of future benefits for which the worker has not yet qualified and the limited financial resources of the employee during any ensuring unemployment as well as the intangible impact of loss of job security are considerations which a just employer should have in mind in implementing the redundancy decision in a fair and sensitive way." It is apparent employer's will not always do so. Statutory reform would ensure they did.

Future research

Redundancy is of course only one aspect that requires consideration as part of an active labour market policy. Nevertheless it is one that is central to labour market flexibility if workers who become redundant in one area are to be employed in another. The appropriate degree of legal intervention depends on the identification of factors that will smooth this process. A degree of equity and income smoothing are likely to be among these. At the same time the degree to which redundancy costs inhibit employers should be identified. Facts rather than rhetoric might be useful here. It is also important to mesh labour law with company law so as to minimise technical and artificial redundancies or the use of company law to avoid existing (or reformed) legal obligations. A sensible approach to redundancy law reform requires information and input from all disciplines represented at this conference.

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Notes

- ¹ Hence the retention and expansion of those provisions in the Employment Contracts Act.
- ² 10 October 1994 Court of Appeal (CA 143/93) Cooke, P, Richardson, Casey, Gault JJ and Sir Gordon Bisson (63 pages).
- ³ *GN Hale & Son Ltd v Wellington Caretakers Union* [1991] 1 NZLR 151 (CA)
- ⁴ Reasonable notice and compensation are merely considerations taken into account when determining whether or not a dismissal was unjustifiable.
- ⁵ *Witehira v Presbyterian Support Services (Nthn)* (Unreported, 17 June 1994, Employment Court, AEC 31/94, Goddard CJ, Castle and Travis JJ).
- ⁶ For example, the share buy back provisions in the Companies Act 1993.
- ⁷ The *Industrial relations Reform Act 1993* (Cwlth) which is in part are intended to fulfil Australia's obligations under ILO Convention 158

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