

Do you have to pay bonuses or commission to departing employees?

Many of you reward your staff with a bonus or commission. These are useful tools to encourage staff motivation and loyalty. However, payment of bonuses or commission can become a sore point when an employee leaves you. Some years ago, it was sufficient to call a bonus or a commission discretionary to avoid paying it to a departing employee. Recently, courts have attempted to limit the originally unfettered discretionary nature of a bonus. Can you still avoid paying these to departing employees? You may be able to do so if you are extremely careful in what you put in writing.

Staying silent is not a solution. If you regularly pay bonuses or commission to your employees without any reference to this practice in your employment documents, a departing employee may be able to claim that the payment of bonuses or commission is an implied term of their contract of employment.

When interpreting a contract, one of the principles is that a written term normally supersedes an implied term. Implied terms can supplement a written term in the contract but cannot contradict it.

The courts have developed a body of case law regarding the interpretation of commission and bonus clauses. The use of the word “discretionary” is no longer sufficient to avoid payment. In *Clark v Nomura International plc* a banker, whose remuneration package consisted mostly of a sizeable discretionary annual bonus, was asked to stay on gardening leave during his notice after a dispute with his employer. During this period, the company refused to pay him a discretionary bonus that would normally have become due. Their reasoning was that the bonus was discretionary and he was leaving, so why should he be paid the bonus? The contract stated that bonuses are discretionary and based on the company and the employee’s performance. The employee obtained damages for breach of contract for non payment of the bonus because the court found an implied term not to exercise a discretion in a perverse manner. The court decided that no reasonable employer would have exercised their discretion in the way that Nomura did.

The courts confirmed the principle and went further in the case of *Horkulak v Cantor Fitzgerald*. An employee resigned as a result of bullying from his manager. The employee won a constructive dismissal claim. His three year fixed term contract contained an annual discretionary bonus. The courts decided that but for the action of the employer, this employee would have remained employed for the length of his contract. The court explained that even though the bonus was discretionary, the employer was in fact contractually obliged to exercise the discretion to pay the bonus, in a bona fide and rational manner. This meant that part of his damages for the breach of his

contract should include sums for the discretionary bonus in his first and second years of employment.

These two cases show that it is dangerous to rely on the word “discretionary”. Even when the contract is more detailed on the payment of the bonus, the courts will use a narrow interpretation of the contract. In *Brand v Compro Computer Services Ltd*, the contract stated that payment under the commission scheme ‘assumes that you [the employee] remain in full time employment with the Company at all time in order to qualify for the commission scheme’. The court interpreted this clause to mean that in order to qualify for a bonus the employee needed to be in full time employment as opposed to part time employment and awarded damages for non-payment of the bonus to the departing employee.

In *Chequepoint (UK) Ltd v Radwan*, whilst the contract of employment provided for a discretionary bonus, the employee had received a letter setting out the calculation of the bonus based on certain targets. This letter did not qualify the bonus as discretionary. The court concluded that once the company had notified the employee of the terms of the bonus, the employee became contractually entitled to it.

Most recently in the case is *Farrell Matthews and Weir v Hansen*. After communicating the rate of a bonus, the employer wrote to the employee adding a condition to the payment terms of the bonus. This new condition was that if notice was given by either party the bonus would cease to be payable. The employee complained about this condition and subsequently resigned and was successful in her claim of constructive unfair dismissal. The employee was awarded the bonus on the basis that once she had been told that she would be paid the bonus, it became a contractual entitlement and that adding a condition amounted to a fundamental breach of contract.

Despite these cases, there may still be scope for the non-payment of bonuses or commission to departing employees. Your contracts of employment will need to have precise wording dealing with the payment of commission and bonuses stating the circumstances in which they will not be payable. However, if you are intending to amend your current employees’ contracts to include new conditions on payment of commission or bonuses, you will need to go about this very carefully and we recommend that you talk to us first because of the risk of constructive dismissal complaints.

For more specific information or to discuss your requirements please call either Amanda Galashan or Julie Calleux at EmployEase on 0207 831 5052, or email us at info@employease.co.uk.

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