

GOOD FAITH OBLIGATIONS IN PRACTICE: WHEN, WHAT, BY WHOM AND TO WHOM?

A Paper by Chief Judge Graeme Colgan of the Employment Court to the LexisNexis Employment Law in the Public Sector Conference Wellington 22 May 2008

Requiring people to do things "in good faith" is an inspired choice of legislative words. In the same way as we use such words and phrases as "fair", "reasonable", and "just", it would be churlish or worse to proclaim one's opposition to "good faith". "We are in favour of bad faith" and to "put an end to good faith in employment relations" are not going to be great vote winners. The phrase "good faith" is often linked to the word "bargaining" and indeed all employment bargaining must be conducted in good faith. But the requirement to act in good faith in employment relations is pervasive. It affects all employment relations interactions, or at least most that I can think of.

Like beauty and eyes, unadorned "good faith" is in the conscience of the beholder. So Parliament has gone some way to define what it means by good faith and even, in some instances, to deem certain sorts of conduct that some would not categorise as bad faith behaviour, as a breach of the obligation to act in good faith. So in some respects Parliament has given an old phrase new meanings and has added an element of objectivity to what would otherwise be an almost entirely subjective assessment of behaviour and whether it is "in good faith" or not.

The concept of good faith is important to those involved in advising and negotiating on behalf of those working in the public sector or those employing public sector employees. It is well known that collective bargaining can only occur under the Employment Relations Act 2000 and its amendments between employers and unions – the union itself being the party to the collective agreement. As far as trade unionism goes, the public sector still has by far the highest density in New Zealand. According to the most recent statistics from 2006, the public

sector's union density is roughly five times higher than the private sector's and roughly three times higher than the national average. The PSA is the biggest union in the country and, some would say, the preferred union of the current government. As a result of all this, good faith issues often arise in the public sector.

This address focuses on identifying the occasions on which practitioners should be aware that statutory good faith obligations will arise; the nature of those obligations; and will finally illustrate by reference to recently decided cases what the law expects of persons required to act in good faith. I conclude with a very recent decision that will be of particular interest to unions and public sector employers.

Good faith – What is it?

It is defined principally (but not exclusively) in s4 of the Employment Relations Act 2000 (*"Parties to employment relationship to deal with each other in good faith"*). As will be identified later in this paper, there are other references to and definitions of good faith including expansions of the s4 definition.

Section 4(1)(b) sets out a broad but not non-exhaustive definition of the requirement of dealing in good faith. Parties must not, whether directly or indirectly, do anything to mislead or deceive each other, or that is likely to mislead or deceive each other.

Section 4(1A), added in December 2004, elaborates on this definition:

- Good faith is *"wider in scope than the implied mutual obligations of trust and confidence"*.
- It requires parties to employment relationships to be active and constructive in establishing and maintaining productive employment relationships including being responsive and communicative.

- With some exceptions, it requires an employer proposing to make decisions that will or are likely to have an adverse effect on the continuation of employment of any employees to provide them with access to information relevant to the continuation of their employment about the decision and an opportunity to comment on that information before the decision is made.

When must good faith be practised?

Section 4(4) sets out eight non-exhaustive circumstances in which the duties of good faith must be carried out. These include:

- collective bargaining (including variations and initiation of bargaining);
- in any matter arising under or in relation to a collective or an individual employment agreement while the agreement is in force; (Two separate circumstances combined for the purpose of this paper.)
- bargaining for individual employment agreements or variations;
- consultations between employers and their employees and unions about collective employment interests including the effect on employees of changes to businesses;
- employer proposals that might impact on employees including in particular to contract out work of employees or sell or transfer all or part of a business;
- making employees redundant;
- access to workplaces by union representatives;
- communications or contacts between unions and employers relating to secret ballots held for collective bargaining.

The relationships where good faith is required

These are set out in s4(2) and include all possible permutations of relationships between employers, their employees, and unions representing those employees. The relationships are expanded to include other union-employer, union-union member, union-union, and certain employer-employer relationships. In practice there will be few employment relationships that are exempt from the Act's good faith requirements.

Occasions in practice in which employers must meet good faith obligations

The following is by no means exhaustive but includes circumstances that might not immediately cause an adviser to recommend the application of good faith to an employer dealing with employment relations day to day.

(a) Misconduct inquiries

It is well established and should be well known that an employer making inquiries into alleged misconduct by an employee must at least meet the statutory good faith obligations at all stages of that inquiry. Sometimes for valid reasons, an employer will not notify immediately an employee against whom misconduct may be alleged. The need to secure documentary (including electronic) evidence in circumstances where this may be at risk of disposal if the fact of the investigation is disclosed, is just one example of this area in which careful strategies need to be employed. Nevertheless, the statute requires an employer at all stages to neither mislead or deceive the employee, nor engage in conduct that might be likely to mislead or deceive. I am not aware of any cases in which these difficult balancing exercises have yet been considered and in the absence of such guidance, employers will probably be well advised to make the fact and nature of investigations into alleged misconduct known to affected employees as soon and as fully as reasonably practicable to meet the statutory good faith obligations.

(b) Employee performance concerns

Employer investigations into employee performance issues may encounter fewer of the sorts of practical problems just described for misconduct inquiries. It is difficult to imagine any circumstances in which an employee about whom an employer has performance concerns should not be told of these and of the steps proposed to be taken to address them from the outset.

(c) Business restructurings

Business restructuring and the need for employee knowledge and involvement has been a vexed question for many years. Employers develop and consider proposals for the more efficient operation of their businesses, sometimes constantly. Yet not all such proposals survive beyond the white board. It is only human nature, also, that many employees learning of a possible restructuring of their employer's business will become fearful, defensive, risk adverse, even antagonistic. Sometimes these negative consequences of advice of a possible restructuring (negative for the employees and, thereby, negative for the business) are wasted because the proposal of which advice has been given either goes no further or is so modified that it bears little resemblance to the original. Again the statutory good faith obligations appear to contemplate that information sharing will take place from the time of "proposing" to make such a decision under s4(1A)(c).

This issue was addressed by the Employment Court in an early case on the Act's requirements, *NZ Public Service Association Inc v Auckland City Council* [2003] 1 ERNZ 57. There the union found out that the employer had commissioned a review of its expenditure and had sought recommendations about this. The union feared that the recommendations, if adopted, might affect adversely the employment of its members. The employer declined to meet with the union to discuss these matters. The Court considered that the good faith obligation crystallised at the point that the employer adopted formally and publicly the consultant's recommendations; that is these then became the employer's proposals.

Although some of the Employment Court's findings were reversed on appeal, its conclusions about the point at which good faith obligations engage where there is a potential restructuring that may affect employees, was not altered. The case emphasises, however, that there can be no hard and fast rules because of the multiplicity of ways in which enterprises go about potential restructurings. Each case must be decided on its merits with such guidance as others previously decided may provide.

(d) Redundancies

However uncertain may be the time at which good faith obligations engage when restructuring is contemplated, where an employer has determined that redundancies are necessary, the Act very clearly requires the application of good faith behaviour. This includes giving affected employees access to information relevant to the continuation of their employment, about the decision proposed, and an opportunity to comment on that information before the decision is made.

(e) Individual bargaining

Finally, not only must collective bargaining engaged in by employers with unions be undertaken in good faith but so too must the more widespread and common bargaining for individual employment agreements including variations to them. Only about 20 percent of New Zealand employees are covered by collective agreements and, in the private sector, this proportion is even lower at about 9 percent. Individual employee bargaining is also more important for employers because each employee's agreement must be bargained for whereas, for collective bargaining, standard terms and conditions apply to all employees covered, at least as to core terms and conditions. Good faith individual bargaining will also include for such provisions as restraints on economic activity, for ownership of intellectual property, and similar "non-standard" terms and conditions.

Good faith obligations on employees

Although not yet well recognised, the Act's obligations apply, where appropriate, to employees as much as to employers.

(a) Misconduct investigations

When an employee is the subject of an inquiry into misconduct by the employer, it is unlikely that the employee will now be able to either remain silent or to contribute only minimally and strategically to the employer's inquiry. Although no case of which I am aware has yet raised the issue, the effect of the statutory good faith requirements on the so-called "right to silence" cases may be very significant. Where an employer is inquiring into misconduct that may also amount to a criminal offence (being investigated by the Police, the subject of a prosecution, or even the future possibilities of these), whether the employee should participate in the inquiry and, if so, to what extent, have been problematic questions in the past. Although, of course, no person can be compelled literally to self-incriminate, the new good faith requirements may strengthen the position of an employer whose employee refuses to participate in the investigation.

(b) Investigations into other employees' conduct

Not unconnected with this is the situation of an employee colleague who is a relevant witness in a misconduct inquiry. Not infrequently, such witnesses will feel divided loyalty and may be unwilling participants in the employer's inquiry. The good faith obligations may also strengthen the employer's hand in these circumstances: employees, by virtue of their employment relationship, may be required to assist their employers and thereby to disadvantage their colleagues.

(c) Long term sickness or injury

The extent to which a sick or injured employee must disclose information to his or her employer about the sickness or injury and prognosis for return to work, has long been a

difficult area. Again, the new obligations of good faith may place greater obligations on employees to make relevant disclosures to their employers.

(d) Employee conflicts of interest

Finally, employees with actual or potential conflicts of interest may now be required to disclose these both sooner and with greater frankness than may have been the case before. The entry into a personal relationship that may cause a conflict of interest may be one example of the impact on employees of the new good faith obligations. So, too, may be an intention by an employee to compete with his or her employer after the end of employment that may be some time away while the employee develops a new business enterprise.

To my knowledge the Act's good faith obligations have not until now been considered in cases where it is alleged employees have breached their employment contracts by competing with their employers. As in many of the instances outlined, lateral thinking and inventive pleading invoking the statutory good faith obligations may change the balance of power in employment relationships that come into conflict.

Good faith obligations on unions

As in the case of employees, some unions are slow to recognise or at least comply with the statutory good faith obligations in their dealings with employers. Where there is already conflict or the prospect of it (strikes or lockouts), it might be counter-intuitive to consider carefully good faith obligations towards an employer to that conflict. But the Act makes no exemptions. Where, for example, a union may reasonably anticipate receipt of formal advice of lockout action, it is unlikely to be good faith behaviour to avoid service of such notices by premature office closure, disconnection of fax machines, and the like.

(a) Representation of employees

When unions represent employees in disputes with employers, they will not only have, as agents, the good faith obligations imposed by the law upon those employees but also, independently, their own good faith obligations as unions. So, for example, unions may need to consider the consequences of any particular strategy not only for the member being represented but also for the union as a separate entity in its own relationship with the employer.

(b) News media comments during disputes

Public comment, written or oral, about employment relations with employers during disputes is also an area in which, in my observation, some unions have failed or refused to consider sufficiently their good faith obligations. Egregious denigration of a particular employer in the course of a difficult dispute may run the risk of undermining the bargaining or the employer. As will follow later in this paper, in the public health sector at least, there are now particularly stringent good faith obligations including requirements to behave with courtesy and respect that may require age-old attitudes to change. I have to say of course that the obligations are mutual and I have seen instances of some employers going too far in recent times.

(c) Conflicting interests of union members

Potential difficulties for unions in complying with good faith obligations may also arise where they represent one member whose interests conflict with those of another. One example is of an employer's inquiry into an allegation of sexual harassment of one union member employee by another union member employee. Although such situations have always required unions to act deliberately and delicately, meeting their good faith obligations to each of their members and to the employer will probably make more complex and difficult an already delicate situation.

(d) Collective bargaining

Finally, of course, unions are bound by the new good faith obligations when bargaining for employment agreements and the statutory requirements are now complex and arguably contrary to old style dispute tactics.

Key words and phrases of good faith

The following list of words and phrases taken from the Act illustrate well the very different environment created by Parliament since 2000 and, in particular, since the 2004 legislative amendments.

- *"mislead"* (or likely to)
- *"deceive"* (or be likely to)
- *"active and constructive"*
- *"responsive and communicative"*
- *"best endeavours"* (s32(1)(a))
- *"consider and respond"* (s32(1)(c))
- *"recognise role and authority"* (s32(1)(d)(i))
- *"not undermine"* (s32(1)(d)(iii))
- *"facilitate rather than obstruct"* (s181(1)(a))
- *"[act] in a manner designed to resolve issues"* (s181(2))
- *engage constructively and participate fully and effectively"* (Schedule 1B clause 2(b)(iii) and (4))
- *"behave openly and with courtesy and respect"* (Schedule 1B clause 4(2)(a))
- *"create and maintain open, effective and clear lines of communication"* (Schedule 1B clause 4(2)(b))
- *"search for solutions that will result in productive employment relationships and enhanced service delivery"* (Schedule 1B clause 4(2)(d)(ii))
- *"to encourage, enable and facilitate employee and union involvement"* (Schedule 1B clause 3)
- *"support collective bargaining and [mecas]"* (Schedule 1B clause 6(1))

Practitioners advising parties would do well to consider all of these words and phrases and advise upon strategies that are consistent with them, even if particular words or combinations or them do not apply expressly to a particular situation. That is because in several material respects, the specifics addressed in s4 in particular are said not to be exhaustive but only exemplary.

So, for example, although the phrases "*best endeavours*", "*consider and respond*", "*recognise the role and authority*" and "*not undermine*" all appear in s32 that relates to collective bargaining, those words and phrases will probably colour the tests that the Employment Relations Authority and the Employment Court will apply to allegations of bad faith elsewhere in the legislation. Also, for example, the requirement not to undermine may well influence the Court's consideration of conduct by an employee towards an employer and, thereby, the justification for what the employer might do in response. Similarly, the requirement in s32 to use "*best endeavours*" may assist the Court to determine whether an employer has acted in good faith and therefore justifiably when addressing an employee's substandard performance.

"Good faith" obligations pre 2000

Good faith did not emerge like a bolt from the blue or, depending on your point of view, the first ray of sunshine, when the Employment Relations Act 2000 came into force in October that year. The Employment Court had been developing concepts and tests that, although not always termed "good faith", nevertheless reflected the sorts of conducts that are now required expressly in statute.

One example was the development of the rules of fair process in decision making by employers that might lead to dismissal or disadvantage. Indeed, the provenance of those

rules goes back as far as the *Auckland City Council v Hennessey* [1982] ACJ 699; (1982) ERNZ Sel Case 4 in the Court of Appeal in 1982.

One landmark judgment of the Employment Court was *NZ Food Processing etc IUOW v Unilever NZ Ltd* ERNZ Sel Cas 582. At 595 the Court set out the minimum requirements of procedural fairness that can be summarised as:

- notice to the employee of the specific allegation of misconduct and of the likely consequences of the allegation is established;
- an opportunity (real as opposed to nominal) for the employee to attempt to refute the allegation or to explain it or to mitigate conduct;
- an unbiased consideration of the explanation;

Those general requirements might be said to have been ones of fair dealing in good faith with employees and have been developed over numerous cases.

In the area of redundancy, what we now call good faith requirements were set by the Court of Appeal in *Aoraki Corporation Ltd v McGavin* [1998] 1 ERNZ 601, 618; [1998] 3 NZLR 276 as follows:

- It was not mandatory for employers to consult with all potentially affected employees in making any redundancy decision.
- However, in some circumstances an absence of consultation where it could reasonably have been expected may cast doubt on the genuineness of the redundancy or its timing.
- So too may a failure to consider any redeployment possibilities.

- A just employer, subject to the mutual obligations of confidence, trust and fair dealing, will implement redundancy decisions in a fair and sensible way.

Good faith obligations post 2004

Although, arguably, the most significant change to the legislation made by Parliament in December 2004 was the addition of the new test of justification in personal grievances under s103A, of importance also was the addition of new subsections (1A), (1B) and (1C) to s4. Subsection (1A) is the most significant for the purpose of this paper. Although it took a couple of years for cases to emerge under these new provisions, at least to Employment Court level, there are now a number that give guidance to practitioners.

In *Air NZ Ltd v Hudson* [2006] 1 ERNZ 415; (2006) 3 NZELR 155 the Employment Court considered the effect of the new good faith obligations as part of determining justification for a dismissal that was itself determined by application of new s103A. At paragraph [124] of *Hudson* Judge Shaw noted, in relation to the objectives of new s103A:

... common law concepts such as trust and confidence ... have been supplemented by Parliament ... with a central statutory requirement of good faith which, as described in s 4(1A), is wider in scope than the implied mutual obligations of trust and confidence. Section 4(1A) was introduced into the principal Act as an amendment at the same time as the enactment of the new test for justification. This is an indication that Parliament was mindful of common law principles applicable to employment law to date but intended to add to or modify those principles. For example, whereas the Oram decision relied on a breach of trust and confidence to justify a dismissal, this expansion of that test to include good faith means this concept must now be part of an inquiry into dismissals or other actions by employers.

In *Simpson Farms Ltd v Aberhart* [2006] 1 ERNZ 825 the Employment Court dealt not only with the application of the new s103A test to redundancy dismissals but also the application of the new good faith principles. Contributing to a finding of unjustified disadvantage in employment, the Court concluded that the breach by the employer of its consultation and other good faith obligations under s4 was significant. It had rejected a reasonable proposal for a trial in a new position to gauge suitability and failed to respond to a reasonable request for information about proposed reorganisation and a new position to be created.

In *Nee Nee v TLNZ Auckland Ltd* [2006] ERNZ 95 the Employment Court again dealt with redundancies. Among other grounds, the dismissals were found to have been in breach of s4 good faith obligations as amended in 2004. The employer was found to have contradicted unilaterally an operative collective agreement scheme for preferring permanent employees over casuals. The Court found that irrespective of the employer's intention at the time it entered the collective agreement, its subsequent conduct was not in good faith.

In *X (now White) v Auckland District Health Board* [2007] 1 ERNZ 66 the Court had recourse to the s4 good faith obligations in determining that a dismissal for alleged serious misconduct was unjustified both procedurally and substantively. Breaches of s4 including misleading advice about the identities of managerial representatives at a significant first investigative meeting ("*someone from HR*" became the employer's solicitor) and a failure or refusal to exchange all relevant documentary records under s4(1A)(c).

In *CEO Unitec Institute of Technology v Henderson* (2007) 4 NZELR 418 the Court considered a case of dismissal for serious misconduct being alleged harassment of other employees. Again in this case the Court invoked the statutory good faith obligations in assessing whether the employer's process that led to the dismissal was how a fair and reasonable employer would have gone about its investigation of alleged serious misconduct. The Court noted the statutory requirement for the employer to be responsive and communicative as part of being active and constructive in maintaining a productive employment relationship. In particular the Court relied on the obligation under s4(1A)(c) that when proposing to make a decision

that would, or would be likely to, have an adverse effect on the continued employment of the grievant, to provide her with access to information relevant about its decision and an opportunity to comment on the information before the decision was made.

In the very recent Full Court decision of *Waikato District Health Board & Ors v New Zealand Public Service Association* (Colgan CJ, Travis & Shaw JJ 20 March, 2008 AC 6/08) the Employment Court considered requirements for ratification of collective agreements in light of the Employment Relations Act 2000 and its amendments.

The Court had to address the effect of a signed, but arguably unratified, collective agreement and whether employer parties could seek remedies for non-ratification. The PSA argued that ratification is an issue between the union and its members and is not the business of the employer. At para [24], the Court noted that

...while the 'how' of ratification is...not a matter for decision by the employer party or parties to bargaining, the 'what' and 'when' of ratification are matters governed by the statute and therefore on which the employer(s) may have justiciable rights. Ratification is one of several union member interactions that Parliament has specified that employers are entitled to be told of and know about. It is noteworthy that, at the commencement of collective bargaining, the statute requires a union to advise the employer of the ratification procedure that will be used. Likewise, the statute requires a union initiating bargaining for either a mult-employer collective agreement or a single employer collective agreement to advise the employer of the result of the statutory secret ballot that must be conducted by the union...

The Court continued at paras [25] – [27] that

All these requirements that might arguably be thought to be matters between the union and its members, and not the concern of the employer, illustrate the statute's pervasive requirements of information transparency and exchange, important elements of the overarching obligation of good faith between such parties.

It is not only union members who may hold unions to account in their exclusive bargaining role in collective negotiations. Statutory requirements referred to tend to confirm also that Parliament intended to allow employers to hold unions to account for statutory compliance in the bargaining process, just as, of course, unions are entitled to do so in respect of the participation of employers.

While some remedies may be open to union members but not to employers if a breach of the statutory ratification procedure is established, these reflect the different

interests that union members may have. However, the entitlement in law to challenge compliance with the legislation is not with union members alone.

The Court held that a concluded signed collective agreement that adheres to the form and content of such agreements as prescribed by the Act, but that has not been ratified, is of no effect in law. Nothing precludes the Employment Relations Authority from declaring under s163 that an unratified collective agreement is of no effect.

The consequences of non-compliance with good faith obligations

These may include:

- a compliance order to require good faith conduct;

- if the failure is
 - deliberate
 - serious
 - and sustainedor
 - was intended to undermine bargaining (individual or collective) or an employment agreement (individual or collective) or the employment relationshipor
 - a breach of s59B or s59C (passing on)liability to a penalty of \$5,000 (individual), \$10,000 (corporation);

- an unjustifiable disadvantage or dismissal (personal grievance); see *Aberhart* (above)

- refusal of discretionary relief; eg *Service & Food Workers' Union Nga Ringa Tota Inc v Spotless Services (NZ) Ltd* unreported, 13 July 2007, AC43A/07 at para [27];

- reductions of remedies in personal grievances under s124 (including disqualification from reinstatement).

So it may be seen that the Employment Court, even if not the Employment Relations Authority in many cases, applies expressly the statutory good faith tests in appropriate personal grievance and other cases. Those advising their organisations or clients, whether employers, unions or employees, will do well to consider these requirements and, in appropriate cases, to rely upon them, whether in challenging the justification for a dismissal or disadvantage, in establishing justification, or in any other employment relationship interaction.