

**IN THE EMPLOYMENT RELATIONS AUTHORITY  
AUCKLAND**

AA 461/10  
5149140

BETWEEN                      JOHN BECKETT  
  
AND                                HERBERT INSURANCE  
    GROUP LIMITED

Member of Authority:        Yvonne Oldfield

Representatives:             Richard Harrison for applicant  
   Sarah-Jane Neville for respondent

Investigation Meetings:     24 March, 7 September, 13 October 2009

Further Information and     5 November 2009, 11 February, 11 March and 14 April  
Submissions:                 2010 from Applicant

    20 January, 19 February, 22 March, 7 April and 30 April  
    2010 from Respondent

Determination:                27 October 2010

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**DETERMINATION OF THE AUTHORITY**

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**Employment Relationship Problem**

[1] Mr Beckett was employed by the respondent as CEO, Fire and General Division from November 2006 until early 2009. His employment relationship problem, which was lodged immediately upon the termination of his employment, included an allegation of unjustified dismissal and claims that the respondent had breached the employment agreement. Mediation resolved all but one issue: a dispute about Mr Beckett's incentive bonus for 2007.

[2] The only record of what the parties agreed about the bonus is contained in a series of emails which were exchanged between Mr Beckett and Mr Grant Herbert (managing director of the respondent) shortly before Mr Beckett was employed. The parties are in dispute about the meaning and effect of what is set out in those emails.

Based on his interpretation, Mr Beckett calculates that he was entitled to a bonus of \$123,261.00. He seeks to recover this sum, plus interest. The respondent says that no bonus is payable at all.

### Issues

[3] Mr Herbert's offer to employ Mr Beckett was made in an email dated 24 October 2006. It set out proposed terms including base salary and had the following to say in relation to the incentive component of the remuneration:

a. *“Suggested premium based incentive to be current premium income from existing Fire & General Book in New Zealand, plus 12.5% growth factor, on an annual basis, that figure then making up the new target. We will pay you an incentive equal to 20% of brokerage earned on the figure above that. So on an annual basis, say the book now is \$12.0 million premium excluding MII/Special Risks, then the annual target being current plus 12.5% will be \$13.5 million. Anything above that figure, you will take 20% of brokerage thereon. So say the book grows to \$16.0 million (which is more than achievable in my view) and average brokerage 14%, then brokerage on excess will be \$350,000.00. With a few things on the go at present, I will not at all be surprised if the book passes \$16.0 million, without very much effort next year. That would mean, as I am sure you can calculate, incentive payment of \$70,000 before tax. This could be paid quarterly on a provisional basis and adjusted after year end...*

...

b. *The incentive would exclude acquisitions. In the event of us making an acquisition, then I suggest the incentive be reviewed by mutual agreement...*”

[4] In a further email dated 6 November Mr Herbert clarified his offer as follows:

a. *“**Incentive** – We would need to agree that we could review the incentive should our turnover increase exponentially, due to acquisitions. I am sure you will agree the reason is obvious. My view is*

*that in the event of an acquisition, we would simply need to review the premium target to take into account the acquired business. We need to discuss the incentive as it applies to the Australian business. When offering the incentive, I had meant that to apply to the NZ account. Set-up costs are rather high as you can imagine...”*

[5] In an email of 7 November Mr Beckett accepted the offer, saying this in relation to the incentive:

*“Incentive of 20% as detailed in your email of 24 October 2006 and clarified in your email of 6 November 2006 in relation to premium from Australia and new acquisitions.”*

[6] There are now four issues for determination by the Authority. These are:

- i. What income was to be included in “premium income” or “brokerage”;
- ii. What business came into the category “Special risk”;
- iii. What deductions should be made as a result of acquisitions during 2007, and
- iv. Whether Gold Coast and Norfolk Island business shown in the New Zealand accounts should be excluded from the incentive calculation.

**(i) Premium income/brokerage**

[7] The respondent’s income had several different components but the two of relevance to this issue are commission and fees. ‘Commission’ is paid by an insurer to a broker at a percentage of the premium the insurer receives from the insured party. ‘Fees’ are not always charged but where they are, they are paid by the insured party to the broker in consideration of services provided to the insured party. They may bear no relation to the level of the premium.

[8] Some incentive schemes in this industry include both components for the purposes of bonus calculation, and some do not. The respondent says that Mr Beckett's incentive scheme was one of those which included income from commission only, and not fees. Mr Beckett disputes this.

[9] Mr Beckett says that since he was employed as CEO to grow the business it would have made no sense for him to be incentivised on commission income only and not fees. This assertion is not accepted. There are many possible reasons why fees might not be included in an incentive scheme. By way of example only, I note that there is less scope to "grow" fees income in the way that commission paid by the insurer can be grown (because they are not always charged) and in many cases, fees do no more than cover overheads. In any event, the question for the Authority is not what would have made most sense, but what the parties actually agreed to.

[10] In his email of 24 October Mr Herbert uses "premium income" when referring to the setting of the target, and "brokerage" when talking about what is to be compared to the target, but the terms must obviously bear the same meaning in this context. The respondent argues that the term 'brokerage' means 'commission' as set out in the Vero Insurance Terms Glossary and in the Australian Tax Office ruling, which is as follows:

*"It (commission) is also known as brokerage when paid (by the insurance company) to a broker. Commission does not include fees or charges payable directly by an insured to a broker for the broker's services."*

[11] Mr Beckett argued that the term 'brokerage' is often used to mean income derived from both commission and fees and provided examples of this usage drawn from the respondent's own sale and purchase agreements and from its audited accounts.

[12] All that can be concluded from these conflicting examples is that, within the industry, the term "brokerage" is sometimes used to mean commission only and sometimes used to mean income in a wider sense. Either meaning could be applied in the context of an incentive scheme.

[13] I do not accept however that the term “premium income” is equally capable of carrying two meanings. On a common sense interpretation, premium income can only mean income bearing some relation to premium. Commission is a percentage of a premium payment and therefore can be described as premium income. Fees, on the other hand, are stand alone charges which need not be related to the premium paid.

[14] In the context of Mr Beckett’s incentive scheme brokerage must mean premium income, which in turn can only mean commission. On this analysis, it follows that premium income and brokerage (as used in the email) would not include fees.

[15] **I conclude that income from fees is to be excluded from the incentive calculation.**

(ii) **Special risks**

[16] The parties agree that Mortgage Indemnity Insurance and Mortgage Impairment Insurance (MII) must be excluded from the incentive calculations. They disagree about what else falls within the category “special risks” – specifically, whether it includes Investment Managers Insurance (IMI) - a specialist product for the finance industry and fund managers’ business. Mr Herbert says he always regarded IMI as a special risk product and never intended it to be counted for the purposes of Mr Beckett’s incentive calculations.

[17] In an email dated 12 September (during negotiations which preceded the offer) Mr Beckett expressed his understanding of what the new job would entail as follows:

*“As I understand it, the position is running the New Zealand fire and general, wholesaling and marine businesses – everything other than the mortgage indemnity business...”*

[18] When the offer came on 24 October however the words “special risks” were added in. Clearly something more than just MII was to be excluded. Mr Beckett says that he understood from Mr Herbert that:

“[special risks] *included special products or projects* [Mr Herbert] *was developing – for example... specialty bonds and so on. There was never any suggestion or explanation that special risks was to include IMI insurance – and not only IMI but all other Financial Lines business where there was some, no matter how tenuous, connection with a mortgage indemnity client...*”

[19] Mr Beckett’s view is that apart from what he has identified here, the respondent did not have any special risk business. Mr Beckett argued that within the industry generally, products of the same type as IMI are often part of a Fire and General book of business. He also provided evidence (which is accepted) to demonstrate that most of the major insurers in New Zealand are able to write this type of insurance (although not all necessarily do so.) For this reason he does not accept that there is anything special about IMI, certainly nothing to make it a “special risk” product.

[20] Very little direct evidence was provided to assist the Authority in resolving the question whether IMI should be called a “special risk” product. Mr Herbert maintained that he used the term “special risk” to mean all products outside the respondent’s Fire and General book of business, which was recorded in a Fire and General database. Other business (including IMI and MII) was recorded in a separate Financial Risks database. There was no category entitled “special risk” in the respondent’s databases. Effectively the respondent’s position is that “financial risk” equated to “special risk.”

[21] Mr Beckett pointed out that he did not know how the respondent labelled its databases, or classified products, until after he was employed, and reminded the Authority that the Fire and General Book of business need not equate to a database of the same name. He also argued that the Respondent could not make a special case for IMI because it had “*not separated out other clients within the financial risk database as it was not only IMI clients within this database.*”

[22] This submission was not supported by evidence. It was not established that there was significant business within the financial risk database except for IMI, MII and other projects which the parties agreed were “special risk” such as the specialty bonds.

[23] Mr Herbert says that he employed Mr Beckett to grow the Fire and General book of business. At the time of Mr Beckett's employment Mr Herbert was in discussions with another person whom he intended to employ to manage all the Financial Lines business (including IMI.) There is no dispute that Mr Beckett knew about that at the time. As he stated in his witness statement:

*“At the time of my employment, Grant Herbert was in discussions with a chap regarding the role of Herbert's Liability (Financial Lines) Manager. He refers to this liability manager in his offer email to me of 24 October 2006. However, the liability manager's role was never filled....”*

[24] Instead, Mr Beckett took on responsibility for IMI and other Financial Risks business and (with his staff) ended up doing a considerable amount of work in those areas. In such circumstances it is understandable that he feels he should be rewarded for growth in that part of the business. However, the Authority's task is to decide what the contractual terms were at the time the agreement was entered into. It is not relevant to consider what terms might have been reasonable, or might have been agreed, had it been known at the time the contract was entered into that there would be no Financial Lines manager.

[25] The fact that both parties understood at the time of Mr Beckett's employment that the proposed Financial Lines manager (who was to report to Mr Herbert) would be responsible for IMI supports a conclusion that IMI was not intended (at the time) to be captured by the incentive scheme. The fact that Mr Beckett subsequently took on some responsibility for IMI does not change that.

[26] **I conclude that income from IMI is to be excluded from the incentive calculations.**

(iii) **Acquisitions**

[27] Both parties agree that the respondent generated \$4,245.00 of additional sales as a result of the purchase of books of business during 2007. There is no dispute that this figure should be deducted from income for the purposes of the bonus calculation. The parties disagree about whether there should also be a deduction for the business a

new employee attracted after she joined the company that year. Mr Herbert told me that this employee was to be paid above market salary in consideration of the fact that she brought clients with her.

[28] Mr Herbert did not provide evidence to back up his assertion that he provided additional consideration for the new business this person brought with her, but more importantly, she was not the owner of a book of business that she could sell to anyone. She had previously been working for a competitor of the respondent and the clients in question were not “her” clients in the first place. By no stretch can the employment of a new staff member in such circumstances be considered an acquisition.

[29] **I accept as Mr Beckett has argued that no deductions are to be made for income associated with the new employee. The only deduction for acquisitions is the figure of \$4,245.00 already agreed.**

**(iv) Gold Coast and Norfolk Island business**

[30] Early in the Authority’s investigation of this matter the parties advised that they had agreed to base the bonus calculations on figures from the respondent’s management accounts for the 2007 calendar year.

[31] For a period in 2007, before systems had been set up for the new Gold Coast business, transactions for that business were invoiced through the head office in New Zealand. The respondent’s position is that, as agreed in respect of Australian business, deductions in respect of the Gold Coast had to be made from the total income shown in the 2007 management accounts.

[32] Mr Beckett says that this issue had already been addressed late in 2007 when an accounting adjustment was made for the Gold Coast income though a bulk credit to the Australian section of the accounts. He says therefore that no further deduction needs to be made for the purposes of calculating his incentive.

[33] The respondent’s Chief Financial Officer, Ian Jagger, gave the following evidence in response:

*“I believe the confusion on this issue with Mr Beckett has occurred since the income reversed in the head office systems in March 2008 was added into the Gold Coast systems, and therefore also the Gold Coast portion of the management accounts in October 2007. There was indeed a delay in booking the reversal into the head office portion of the management accounts but this is the reason this must be adjusted for the bonus calculation...”*

...

*Mr Beckett accepts... that approximately \$79,000 of Gold Coast income was included within the New Zealand head office figures during the 2007 calendar year. It appears that the only point of contention is the date of the reversal of this income from the New Zealand head office figures. This did not occur until March 2008.”*

[34] On the question of the date of reversal of the Gold Coast income I accept Mr Jagger’s evidence. He is in the best position to know this information being the person best acquainted with the detail of the accounting records. To suggest that his evidence is not reliable amounts to an assertion that he has attempted deliberately to mislead the Authority and the evidence falls short of establishing that. I accept that the 2007 management accounts include Gold Coast business that was not originally agreed to be included as income for the purposes of the bonus calculation.

[35] It is also argued for Mr Beckett that:

*“When the parties agreed to use the 2007 calendar year management accounts as the basis for calculating Mr Beckett’s incentive payment, no mention was made of the inaccuracy or that these accounts had been adjusted in March 2008 and were no longer accurate. This should have been disclosed at the time it was agreed to use these accounts. The Respondent cannot now alter these accounts and is estopped from doing so.”*

[36] Mr Beckett suggests that if he had known that Gold Coast income had not been deducted from the management accounts, he might have wished to consider

whether the audited accounts or the financial year accounts “*would have more accurately captured the income for the period in question.*”

[37] I am not persuaded by the estoppel argument. There is no dispute that the parties agreed to use the 2007 management accounts for the purposes of calculating the incentive, but that agreement was made in the context of existing disagreement about the four issues for determination in this case. The issue of the Gold Coast income is not fundamentally different from the other three issues. The 2007 management accounts were proposed to be used whether or not deductions were to be made for income from fees, from IMI, from clients who had followed the new employee to the respondent, and from the Gold Coast and Norfolk Island.

[38] Mr Beckett also challenges some of the business attributed to the Gold Coast on the basis that he or his staff worked on the accounts concerned. However, as set out already in respect of the other issues, I am not satisfied that incentive is payable in respect of work done unless there was agreement to that effect.

[39] I accept therefore that the Gold Coast income must be excluded from the incentive calculations as the respondent has indicated.

[40] As for the Norfolk Island business Mr Beckett argued that there was no basis at all for excluding this from the incentive calculation. Unlike the Australian business (once the Australian office was established) Norfolk Island business was always managed and booked through the New Zealand office. The New Zealand column in the management accounts included Norfolk Island income distinct from the “Oz” columns (which recorded Gold Coast income) and this Norfolk Island income was never reversed out of the accounts.

[41] The emails about the incentive were silent on Norfolk Island, in marked contrast to Australia. They confirm that the incentive applies to the New Zealand account and relates to the Fire and General book “*in New Zealand.*” I am satisfied that the Norfolk Island business fell within the New Zealand account and within the New Zealand Fire and General book. On that basis I accept that Norfolk Island business should be included in the calculations.

**(v) Quantum**

[42] Mr Beckett's bonus can now be calculated as follows, using data from the 2007 calendar year management accounts:

2006 income (excluding fees) <sup>1</sup>	\$2,721,969.00
Less MII & Special Risks including IMI	-\$1,663,412.00
Less Gold Coast	Nil
Less acquisitions	Nil
Sub total	\$1,058,557.00
Plus 12.5%	\$132,319.60
<b>2007 Target:</b>	<b>\$1,190,876.60</b>

2007 income (excluding fees)	\$3,231,769.00
Less MII & Special Risks including IMI	-\$1,908,604.00
Less Gold Coast	-\$79,909.00
Less acquisitions (undisputed)	-\$4,245.00
<b>2007 result:</b>	<b>\$1,239,011.00</b>

2007 Result	\$1,239,011.00
Less 2007 Target:	- \$1,190,876.60
Subtotal	\$48,134.40
<b>Bonus at 20%</b>	<b>\$9,626.88</b>

**(vi) Interest**

[43] Mr Beckett also claims interest on his bonus. Clause 11 of the Second Schedule to the Employment Relations Act provides that in any matter involving the recovery of money:

*“the Authority may, if it thinks fit, order the inclusion, in the sum for which judgment is given, of interest, at such rate not exceeding the 90-day bill rate (as at the date of the order), plus 2% as the Authority thinks fit, on the whole or part of the money for*

<sup>1</sup> I use the term 'income' with its ordinary meaning. The income figures here are net of other exclusions about which there was no dispute.

*the whole or part of the period between the date when the cause of action arose and the date of payment in accordance with the determination of the Authority.”*

[44] Mr Beckett’s incentive was to be “*paid quarterly on a provisional basis and adjusted after year end...*” On that basis I accept that Mr Beckett is entitled to interest on the arrears at the rate of 5.2% per annum from the end of the 2007 calendar year until the date of payment.

**(vii) Costs**

[45] The parties have advised that they have agreed that costs will lie where they fall. I therefore make no order for costs.

**(viii) Orders**

[46] **The respondent is ordered to pay to Mr Beckett the sum of \$9,626.88 plus interest at the rate of 5.2% per annum from 31 December 2007 until the date of payment.**

Yvonne Oldfield

Member of the Employment Relations Authority