

**IN THE EMPLOYMENT RELATIONS AUTHORITY
AUCKLAND**

**[2014] NZERA AUCKLAND 530
5446354**

BETWEEN

DAVID GEORGETTI
Applicant

AND

COMPASS COMMUNICATIONS
LIMITED
Respondent

Member of Authority: Eleanor Robinson

Representatives: Applicant in person
Dean Organ, Advocate for Respondent

Investigation Meeting: On the papers

Submissions received: 25 November 2014 from Applicant
02 December 2014 from Respondent

Determination: 22 December 2014

DETERMINATION OF THE AUTHORITY

Employment Relationship Problem

[1] The Applicant, Mr David Georgetti, claims that he is owed monies in respect of unpaid bonuses earned during the period March 2012 to August 2013 by the Respondent, Compass Communications Limited (Compass).

[2] Compass denies that Mr Georgetti is owed any monies in respect of unpaid bonuses and claims that he was paid at all times in accordance with the terms of the individual employment agreement between the parties (the Employment Agreement).

[3] The parties agreed to the Authority determining this issue based on the Statements of Problem and in Reply, witness statements, and on submissions from the parties.

Issues

[4] The issue for determination is whether or not Mr Georgetti is owed monies in respect of unpaid bonuses by Compass.

Background Facts

[5] Compass is a New Zealand owned independent internet and telecommunications service provider, offering a diverse range of technology solutions from fully outsourced virtual desktops to onsite management of IT infrastructure.

[6] Mr Georgetti commenced employment with Compass on 21 November 2006 in the position of General Manager Compass Residential Solutions. He was provided with the Employment Agreement which he signed on 13 November 2006.

[7] Clause 6.1 of the Employment Agreement stated: "*The terms relating to the Employee's remuneration are detailed in Schedule 5*". Schedule 5 of the Employment Agreement stated in relation to the bonus payable:

6. Remuneration

...

Bonus

Employee is entitled to get a bonus of \$60,000. Bonus will be calculated on achievement of Margin and Revenue targets.

[8] Clause 25.0 of the Employment Agreement provided:

25.0 Variation

25.1 The Employee expressly acknowledges that the company has the sole discretion to alter the contents of Schedules as attached.

25.2 No term or provision of this Agreement (exclusive of Schedules) may be amended or varied unless such amendment or variation is reduced to writing and signed by the parties.

[9] In accordance with Schedule 5 of the Employment Agreement the bonus payment was to be calculated on the basis of the achievement of margin and revenue targets.

[10] The targets are not defined in the Employment Agreement, and these were later agreed to by the parties. Other than for the targets, the terms and conditions applicable to the payment of bonuses are not specific and not clearly defined, and I note that there is no

reference to the fact that a bonus payment will not be made in any period in which Compass does not make a profit.

Period prior to 2010

[11] Mr Karim Hussona, Group Chief Executive Officer, stated in his witness statement that the bonus prior to 2010 was based on achievement of revenue and margin targets as stated in Schedule 5 of the Employment Agreement, and as Compass did not at that time have departmental P&L accounts, it had been agreed to pay bonus based on achievement of the formula:

- Quarterly profit target of \$50k profit growth (GP) per quarter
- Assuming 30% GP, this was amended to \$166,667.00 per quarter revenue growth

[12] Mr Georgetti in accordance with the common practice at that time, would record results and calculate the bonus to be paid, which Mr Hussona would approve.

[13] Mr Georgetti stated in his witness statement that he would transfer the figure from the line in the departmental P&L as prepared by the financial controller into the spreadsheet he and Mr Hussona used to calculate his bonuses.

[14] The initial targets and/or the bonus payments made prior to 2010 are not in dispute. The maximum bonus payable was \$60,000.00 per annum.

Events in 2010

[15] In early 2010 there was discussion between Mr Georgetti and Mr Hussona about changing the bonus criteria to use the accounting practice measure EBITDA (Earnings Before Tax, Depreciation and Amortisation) which is calculated using information obtained from financial statements, starting with operating profit or loss, and subsequently adding back depreciation and amortisation. In an email to Mr Hussona dated 22 April 2010 Mr Georgetti wrote:

Hi Karim,

...

We spoke of changing my bonus criteria to use EBITDA instead of revenue, and I was supposed to come up with a forecast

...

I wanted to suggest that we convert today's revenue growth targets into operating profit targets based on their ratios over the last 12 months as follows

...

I'm all for changing the basis to EBITDA. Both operations are running VERY lean on costs, so I have no fat to trim to boost EBITDA. It has to come from Revenue growth and/or better margin products. ...

[16] Mr Hussona responded by indicating he was happy with the approach suggested, and asking Mr Georgetti to advise on the effect on bonus.

[17] Mr Georgetti responded by email dated 21 July 2010:

We've experienced some revenue growth from Jan-Mar qtr to Apr-Jun qtr. At the moment I would receive about 44% of the \$6k for this. Not major but better than previous quarters.

...

Can you confirm you are happy with this, as I feel too often I take the hit personally (through loss of bonuses) for the poor performance of others.

Going forward I'd like to move to bottom line (not rev) as my KPI.

[18] A restructuring of Compass occurred shortly after the writing of this email, as a result of which Mr Georgetti was offered the position of General Manager Sales and Service, as confirmed in an email from Mr Hussona dated 11 August 2010:

Further to our recent discussions, I would like to offer you the role of GM Sales and Service for Compass Communications Limited.

....

Your objectives are to maximise the profitability of each business unit to meet agreed operating profit targets.

...

The bonus will be based on achieving targets related to growing the quarterly operating profit of each business unit ... We should base this on achievement against budgeted operating profit numbers, but in the absence of these, I suggest we link it instead to achieving \$10,000 per month operating profit growth per month for each business unit.

...

I envisage this taking formal effect on 1st September.

[19] Mr Georgetti responded to the offer in an email dated 12 August 2010 stating: *“I’ve had a little time to consider your offer, and think we should treat it as a starting point in the package discussion. I think the at-risk amount is fair, but I would need to look at the respective P&Ls a bit more closely re the starting target of \$10k operating profit per month per division, it’s probably fine though...”*. He referred to the base salary and to his concern about the bonus proposal, concluding the email: *“Perhaps we deal with base salary first, and then finalise bonus split and targets.”*

[20] Mr Hussona stated that following a meeting, it had been agreed that Mr Georgetti would have one additional week of holiday and a \$5,000.00 gross per annum increase in his base salary plus a \$5,000.00 gross increase in the ‘at risk’ bonus component.

[21] In an email dated 3 November 2010 addressed to Mr Hussona and Mr Paul Carter, Chief Financial Officer, Mr Georgetti raised further concerns about the salary and bonus package for the General Manager Sales and Service position stating:

After the last 2 months, I find I’m really reluctant to accept your (Karim) proposed bonus scheme based on \$10k op profit growth pm for both Bus. This would have meant hardly any bonus payment if we look back 12 months, ...

[22] Mr Hussona responded by email that same day, stating: *“Your role as GM requires you to be responsible for P&L of the business units and as such the most appropriate measure is profit based”*. He also offered: *“ to consider making a one-off adjustment for the last quarter”* and concluded:

I would also be willing to consider proposals from you for alternative bonus structures going forward, but it would need to be in line with the overall objectives of the business, which are to deliver certain levels of profit.”

[23] There was an exchange of emails between Mr Georgetti and Mr Hussona on 15 December 2010 and 16 March 2011 which were concerned with clarification of the bonus payments basis. In the email dated 16 March 2011 Mr Hussona stated:

...

We subsequently agreed to modify this to be a rolling quarter and payable monthly, so the bonus is now to be calculated

- OTE of \$1,333.33 per month for GB bus unit achieving \$10,000 per month (\$60k per rolling quarter) operating profit growth
- OTE of \$1,333.33 per month for Res unit achieving \$10,000 per month (\$60k per rolling quarter) operating profit growth
- OTE of \$1,250.33 per quarter for Calling card bus unit achieving \$10,000 per month (\$60k per rolling quarter) operating profit growth
-

[24] I note that 'OTE' has the ordinary meaning in sales/commission terms of 'On Target Earnings', indicating how much bonus it is possible to earn if the set targets are achieved.

[25] There were no further issues concerning the bonus scheme raised until June 2013 despite Mr Hussona stating that from February 2011 onwards the Compass residential business unit had started to record losses until there was a small profit in the quarter ending February 2012 which had resulted in a bonus payment being made to Mr Georgetti in that quarter.

Events 2013

[26] Mr Hussona stated that in June 2013 he initiated a discussion with Mr Georgetti about a restructure and downsizing.

[27] On 18 June 2013 following a request by Ms Mabel Vivera of the Payroll department for bonus payments clarification, Mr Georgetti emailed Mr Hussona asking if he had reviewed his bonuses. Mr Hussona responded that same day stating:

Dave,

I have looked at it and am having some difficulties agreeing to it.

- *We hadn't discussed doubling the commission following the restructure, so I would struggle to agree to this*
- *In any case I find it hard to justify paying such a bonus while the business is making such significant losses. The commission is based on profit growth – I'm not sure if a reduction in losses counts as a growth in profits.*

Can we discuss.

[28] In July 2013 Mr Georgetti had received a letter advising him of a restructure which could impact upon his role at Compass. On 5 September 2013 he was advised that his position as General Manager Sales and Service was to be made redundant and his last working day would be 30 September 2013.

[29] On 10 September 2013 Mr Georgetti stated that he had been offered a contract position by Compass, and on the 30 September 2013 he had emailed Mr Hussona stating that he would send him the bonus spreadsheet and asking if they could meet to discuss it.

[30] Mr Hussona responded by email dated 4 October 2013 stating:

As I mentioned before I have a number of difficulties with this – the res bus unit has not made a monthly profit since Jan 2012.

In addition to the issues I have outlined below, I believe the calculation must be on a rolling quarter – this smoothes out any lumpy results and better allows for the transition between GB/res combined and solely Res in Feb 2012.

We would also need to take into account bonus payments made and the period that those payments relate to adjust the ebitda.

[31] Mr Georgetti replied to this email the same date, stating:

... I think it's important to remember the rapid decline in profitability was due in a large part to the move to UCLL. ...

On a positive note, Res would have had positive EBITDA of \$6k in August if we hadn't paid \$10,900 to ... for web design

[32] On 17 October 2013 Mr Hussona emailed Mr Georgetti stating:

I have discussed with Paul and Dave and there is reluctance to paying significant bonus when the business has been in such a loss making position for so long.

In particular we are not able to recognise a reduction in losses as a growth in profit

[33] Mr Hussona further emailed Mr Georgetti on 1 November 2013 stating:

Apologies for not getting back to you sooner.

Having met with Paul and Dave, our position is that bonus payments for EBITDA growth can only apply where there is positive EBITDA, and in the period that we are talking about the Residential business unit has incurred a loss of over \$1m.

Furthermore the business as a whole is under increased financial pressure, and we have very limited scope for making discretionary payments

That said, I can offer \$10,000 as a discretionary payment to cover performance for the period to end September 2013.

[34] Mr Georgetti responded by email dated the same day, 1 November 2013, rejecting the offer of a discretionary payment and observing:

... My bonuses are 25% of my remuneration package. They're not discretionary and payment of them shouldn't be affected by the business' current financial pressure.

I'm not sure if Paul and Dave are aware that we have used the same calculation to apply to the bonus criteria since I started in 2007 and that there was no negotiation or advice prior to the 19 month period outstanding, that the terms of my bonuses had changed. In addition bonus payments have been paid in the past for EBITDA growth where there has not been positive EBITDA.

[35] On 20 November 2013 Mr Georgetti emailed Mr Hussona after receiving the September 2013 P&L result, stating his expectation of bonus payment based upon the spreadsheet in the sum of \$87,664.37.

[36] Mr Hussona responded by email dated 21 November 2013 stating that Compass's position was that no bonus was payable to Mr Georgetti for the management of the residential business unit for the period from March 2012 to August 2013 as the residential business unit did not make an operating profit in any month in that period and therefore no profit growth on which the bonus could be calculated.

[37] Mr Hussona concluded the email by stating: “... *in the interests of continuing to reduce the costs to the business I have decided to terminate your short term contract giving you required 4 weeks written notice to terminate from today. Accordingly your last day will be 20th December 2013.*”

[38] The parties attended mediation but this did not resolve the matter. On 23 May 2013 Mr Georgetti filed a Statement of Problem with the Authority.

Determination

[39] In accordance with Schedule 5, clause 6 of the Employment Agreement Mr Georgetti was: “*entitled to get a bonus of \$60,000.00*”, such entitlement to be calculated on the achievement of margin and revenue targets. The quantum of the bonus was subject only to the method of calculation, and the maximum OTE amount which was changed from time to time.

[40] I find that Mr Georgetti had a contractual right to a bonus to a maximum of \$60,000.00 per annum and that, with the exception of the achievement of the targets, no terms or conditions of payment of a bonus are specified in the Employment Agreement, specifically there is no reference to bonus not being payable in the absence of a profit.

[41] As previously observed, the achievement and revenue targets are not defined in the Employment Agreement, and it is not disputed that the amount of bonus payable, up to a maximum of \$60,000.00 per annum, was agreed between Mr Georgetti and Mr Hussona in accordance with spreadsheet analysis produced by Mr Georgetti.

[42] The quantum of calculations submitted by Mr Georgetti in the form of spreadsheets has not been disputed by Compass, and accordingly I have accepted it as the basis of numerical calculation.

[43] The targets set out in the spreadsheets indicate that the revenue growth target had been agreed assuming a standard gross profit margin of 30%. Therefore whether or not the standard gross margin was actually achieved did not influence the calculation prior to 2010.

[44] There is no other indication that any elements of the revenue and/or gross margin were defined as any type of profit, which is confirmed by analysis of the headings in the spreadsheets of results for this period which show only headings for Net Revenue and Revenue Growth.

[45] Therefore for the period 2006 – September 2010 the set target was the achievement of revenue (sales), there is no element of profit involved in the calculation of the results to achieve any bonus earned, other than by reference to the standard gross margin.

[46] In accordance with clause 25.1 of the Employment Agreement Compass had the sole discretion to alter the contents of the Schedules. There was no proviso that any alteration of the Schedules had to be reduced to writing and signed by the parties as was the case regarding other terms and provisions pursuant to clause 25.2.

[47] No such alteration was made to Schedule 5 of the Employment Agreement and therefore I examine the course of dealings between the parties to see if such an alteration in the operation of the bonus scheme occurred post-2010.

[48] During 2010 there was discussion between Mr Georgetti and Mr Hussona about changing Mr Georgetti's then current remuneration package away from revenue growth targets to operating profit targets using the concept of EBITDA as referred to in the email from Mr Georgetti dated 22 April 2010: *"I wanted to suggest that we convert today's revenue growth targets into operating profit targets based on their ratios over the last 12 months ..."*.

[49] Subsequent emails refer to the operating profit targets in particular:

- the email written by Mr Hussona dated 11 August 2010 refers to *"agreed operating profit targets"* or in their absence to: *"achieving \$10,000 per month operating profit growth per month for each business unit"*;
- the email written by Mr Georgetti on 12 August 2010 refers to the at-risk amount being fair: *"... but I would need to look at the respective P&Ls a bit more closely re the starting target of \$10k operating profit per month per division, it's probably fine though..."*;
- the email written by Mr Hussona to Mr Georgetti on 16 March 2011² refers to: *"operating profit growth"* as being the basis for bonus payments; and
- the email written by Mr Hussona on 4 October 2013 which states: *"We would also need to take into account bonus payments made and the period that those payments relate to adjust the ebitda"*.

[50] Accordingly I find that post-2010 the agreed target for bonus payment was \$10,000.00 per month operating profit per business unit using an EBITDA basis.

[51] This measure of the business unit performance includes both losses and profits, both of which form part of the EBITDA calculations set out in the spreadsheets supplied by Mr. Georgetti and Mr. Hussona. It does not deal only with profit but can be viewed as a movement for the purpose of understanding trends such as growth.

[52] I note that EDITDA is reported in both negative and positive scenarios as exemplified in the following company performances reported on the internet:

Mainfreight nz: 'Ebitda performance in Mainfreight USA improved to breakeven compared with a negative \$1.74m for the prior period.'

*Amplifon: 'EBITDA was negative €4,017 thousand in 2011 as against negative €4,259 thousand in 2010 - an improvement of €242 thousand or 5.7%'.
'*

Spirits maker 42 Below NZ: 'EBITDA losses improved by 15 per cent compared to the same period last year.'

Outokumpu Group: 'Looking at our biggest profitability improvement levers, we saw Stainless Americas to reach break-even quarterly EBITDA for the first time.'

[53] I find it is therefore reasonable to assume that EBITDA includes losses and that as such, reductions in losses are referred to as profitability improvement, which must include the term 'growth in profitability'.

[54] When determining the EBITDA movement over a time period to establish a movement pattern it is reasonable to use the arithmetic method of adding both positive and negative numbers to achieve the result which is used in the spreadsheets submitted.

[55] During the period June 2010 to February 2012 EBITDA includes both positive and negative numbers which are totalled quarterly from which a movement in terms of negative or positive growth is achieved. In two of the quarters positive growth was achieved for which Mr. Georgetti earned and was paid the relevant bonus. The positive EBITDA growth was achieved from a combination of positive and negative EBITDA monthly numbers.

[56] I observe that Compass acknowledged the fact that EBITDA growth occurred when negative EBITDA was added to positive EBITDA by having paid Mr. Georgetti bonus for that period as per his calculation.

[57] Accordingly I find that EBITDA growth as a result of reducing losses can be viewed as profitability improvement.

[58] I determine that Mr Georgetti is entitled to a payment in respect of bonus earned but not paid during the period March 2012 to August 2013.

Remedies

[59] Mr Georgetti's claim is for bonus earned but not paid during the period March 2012 to August 2013 in respect of the "Residential Business" in accordance with the terms set out in Schedule 5 clause 6 of the Employment Agreement as subsequently amended.

[60] The maximum bonus (OTE) payable during this period in respect of the Residential Business (as shown on the submitted spreadsheets and Mr Hussona's email dated 21 November 2013) I find to be \$2,291.67 per month; \$6,875.00 per quarter, based on a maximum of \$27,500.00 per annum.

[61] There are two relevant time periods: Period 1: March 2012 to February 2013, and Period 2: March 2013 to August 2013, which reflect the per annum maximum bonus payable.

[62] Utilising the spreadsheet financials provided by Mr Georgetti, as amended by Mr Hussona to reflect the rolling quarterly EBITDA numbers (which have not been disputed by Mr Hussona) and applying the monthly OTE per month maximum, I find that the total bonus payable to Mr Georgetti as a bonus payment in respect of Period 1 is \$9,451.61.

[63] Utilising the spreadsheet figures financials provided by Mr Hussona which shows the rolling EBITDA numbers, and applying the monthly OTE per month maximum, I find that the total bonus payable to Mr Georgetti in respect of Period 2 is \$6,875.61.

[64] I order that Compass pay Mr Georgetti the sum of \$16,327.22 in respect of unpaid bonus payments.

Costs

[65] Costs are reserved. The parties are encouraged to agree costs between themselves. If they are not able to do so, the Applicant may lodge and serve a memorandum as to costs within 28 days of the date of this determination. The Respondent will have 14 days from the

date of service to lodge a reply memorandum. No application for costs will be considered outside this time frame without prior leave.

Eleanor Robinson
Member of the Employment Relations Authority