DISCRETIONARY BONUSES AND SICK PAY AFTER BRAGANZA

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1. In Braganza v BP Shipping [2015] UKSC 17, [2015] 1 WLR 1661, the Supreme Court clarified the application of public law principles to the employer's exercise of a contractual discretion.

2. The issue in Braganza was the proper approach to a challenge to the employer's decision that Mr Braganza had committed suicide such that no death benefit was payable to his widow. The case was not about discretionary bonuses or sick pay, but the court's reasoning drew heavily upon earlier bonus cases and it is now the leading authority on the approach to be taken where the employer, rather than the Court, is the decision-maker under the contract.

3. Mr Braganza was the Chief Engineer on MV British Unity. He went missing between 1am and 7am on 11 May 2009 while the ship was sailing in the mid-north Atlantic. He was presumed to have drowned. BP undertook a thorough investigation. While the company ruled out foul play, it could not rule out the possibility of accident. Indeed there were proper grounds for thinking that Mr Braganza might have wished to check the weather in the night given the plans to undertake operations on 11 May which could only be undertaken in calm seas. The company, however, concluded on balance that he had taken his own life.

4. At trial, Teare J held that he would not himself have been able to make any finding as to the cause of death. He found BP's conclusion to be irrational. The Court of Appeal allowed BP's appeal, but the majority of the Supreme Court restored the judgment in favour of Mrs Braganza. While the Supreme Court was divided as to the result, the justices were unanimous as to the proper legal approach to such cases.

The pre-Braganza bonus cases

5. Three earlier cases merit mention. First, in Clark v Nomura [2000] IRLR 766, the company had moved away from formulaic bonuses to a discretionary approach. Nevertheless it had made clear that bonuses remained an important component of its remuneration policy and that bonuses were paid to reward top performance. In finding that the company was in breach of contract in failing to award a bonus for the final months of Mr Clark's employment, Burton J observed, at [40], that the company did not enjoy an unfettered discretion and that it could not exercise the discretion capriciously. He held that the proper test was one of irrationality or perversity, and that the Court would only therefore interfere if no reasonable employer would have reached the conclusion reached by the defendant.

6. In Horkulak v Cantor Fitzgerald International [2004] EWCA Civ 1287, [2005] I.C.R. 402, Potter LJ, at [46], applied the test of whether the company's decision not to pay a bonus was a *"bona fide and rational exercise"* of discretion.

7. In Keen v Commerzbank [2006] EWCA Civ 1536, [2007] I.C.R. 623, Mr Keen complained that he had only received bonuses of €2.8 million for 2003 and €2.95 million for 2004 despite earning very substantial profits for the bank. Further he had received no bonus for 2005 since he was no longer employed by the bank when the bonuses were paid in March 2006.

8. Applying the rationality test, Mummery LJ said, at [39]:

"… it is not the function of the court to usurp the bank's exercise of its discretion. It is for the bank to decide whether to pay a bonus and, if so, how much, when and in what amount and form. The court is not entitled to substitute itself for the bank. The court is not a bank. It does not employ the staff of the bank or pay them. The court's function is limited to deciding whether the bank acted in breach of the contract term relating to the discretionary bonus decisions …"

9. Claims challenging a company's bona fide assessment of the quantum of a bonus will be particularly difficult. As Mummery LJ observed, at [59]:

"The burden of establishing that no rational bank in the City would have paid him a bonus of less than his line manager recommended is a very high one. It would require an overwhelming case to persuade the court to find that the level of discretionary bonus

payment was irrational or perverse in an area where so much must depend on the discretionary judgment of the bank in fluctuating market and labour conditions."

10. By contrast with Clark, the object of the bonus clause in Keen was to motivate future performance. Consistently with this, no bonus was payable unless Mr Keen was still employed in March 2006.

11. In Keen, the Court of Appeal held that employers should give reasons for their decisions but that a lack of reasons did not of itself establish that the decision had been irrational.

The discretionary sick pay cases

12. While there is less case law on the point, the same approach was taken to challenges to discretionary sick pay clauses in West Yorkshire Fire & Civil Defence Authority, EAT, 29 June 2004 (HHJ Birtles) and Merseyrail Electrics 2002 Ltd v Taylor, EAT, 18 May 2007 (HHJ Clark).

Braganza

13. And so back to Braganza. Baroness Hale observed, at [18], that the contractually agreed decision-maker was BP and accordingly it was necessary to review the company's decision, and not for the court to substitute its own view. She pointed out that there is a clear conflict of interest where one contracting party has a discretion, the exercise of which affects the parties' rights. She observed that such conflict is heightened where there is an imbalance of power, as one would typically find in a contract of employment. It was therefore necessary to prevent abuse.

14. Baroness Hale held that the law would imply a term that the discretion would be exercised rationally, in good faith and consistently with the contractual purpose.

15. Referring to the seminal public law case of Associated Provincial Picture Houses Ltd v Wednesbury Corporation [1948] 1 KB 223, Baroness Hale held that the proper approach involves two steps:

15.1 First, the court should consider whether the employer took into account matters which it ought not to have taken into account, or failed to take into account relevant matters. This review considers whether the employer took a proper approach to the decision.

15.2 Secondly, the court should consider whether the decision was so unreasonable that no reasonable employer could have come to it. This is the irrationality or perversity test applied in the bonus cases, and in particular Clark and Keen. It focuses on the outcome rather than the methodology.

Discretionary bonus and sick pay clauses after Braganza

16. The following approach is now required:

16.1 Start by construing the contract. In particular, identify the decision-maker. If the decision is that of the employer then the case is in Braganza territory.

16.2 Consider the purpose of the clause. In bonus cases, is it to reward past performance (Clark) or motivate future performance (Keen)?

16.3 Consider, by reference to the contract and circumstances of the case, whether the decision maker has taken into account the proper considerations. Or whether he/she has been influenced by irrelevant factors.

16.4 Stand back and look at the decision. Consider whether it was irrational or perverse, in the sense of being so unreasonable that no reasonable employer would have some to such decision.

16.5 While a lack of reasons does not of itself prove that the decision was irrational, it may place an evidential burden on the employer to explain its thinking where there is prima facie evidence of an irrational decision.

17. The Braganza approach has been applied on a number of occasions since but not always with enthusiasm.

18. In Patural v DB Services (UK) Ltd [2015] EWHC 3659 (QB), Singh J sounded a note of caution, at [61], as to whether it was appropriate to import public law principles to private law contracts.

19. Notwithstanding such doubts, that is the effect of Braganza.

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