

RESTRUCTURING AND REDUNDANCY

**Report of the Public Advisory Group on
RESTRUCTURING AND REDUNDANCY**

June 2008

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EXECUTIVE SUMMARY

Restructuring is a natural part of the life cycle of most businesses as they grow or shrink, respond to changes in market conditions or other demands on the business, or change the business model under which they operate. Change may also be forced on the business through receivership or insolvency, and that change may be as radical as whole or partial business closure. Restructuring of a business therefore often entails redundancy of employees.

The world in which this life cycle occurs however has changed significantly over the years.

In particular, the phenomenon of globalisation has exposed businesses to greater and more frequent competitive pressures than ever before.

Restructuring and, often, redundancy can now be frequent rather than occasional features of employment relationships.

Notwithstanding changes in the underlying pressures, there have been few changes to the essential nature of employment and insolvency law over the same period. Such changes as there have been created some prescription and protection in relation to only some aspects of restructuring and redundancy compensation. There has not been a comprehensive review of the restructuring and redundancy framework.

It is therefore timely to look at legal policy arrangements that underpin the processes of restructuring and redundancy, with a view to aligning them with modern realities.

These realities include the need to balance commercial imperatives with social policy safety nets that ensure the support and retention of workers so that despite the incidence of redundancy they can have secure employment in the context of economic transformation.

Public Advisory Group on Restructuring and Redundancy

The Labour Party's 2005 policy manifesto stated an intention to establish "a Ministerial Advisory Group to examine the adequacy of redundancy law and provision".

The Public Advisory Group to the Minister of Labour on Restructuring and Redundancy (the Group) was established in 2007 to examine the adequacy of redundancy laws and provisions in New Zealand workplaces. The Group's terms of reference call for this report to be provided to the Ministers of Labour, Social Development and Employment, and Economic Development by 30 June 2008. This document is that report.

The Group is an independent body established to provide independent advice to the Ministers of Labour, Social Development and Employment, and Economic Development. The Group's members were nominated by the Minister of Labour and considered by the Cabinet Appointments and Honours Committee for appointment.

The Group includes representatives from the following three organisations:

- New Zealand Council of Trade Unions (two seats)
- Business New Zealand (one seat), and
- State Services Commission (one seat).

Purpose of Report

As required, this report assesses the adequacy of redundancy laws and provisions and recommends options for addressing perceived gaps and issues with existing laws and policy provisions. The details of the Group's Terms of Reference are set out in Appendix A (To obtain this appendix, please send email to info@dol.govt.nz).

This report reviews New Zealand's legislative framework for redundancy and provides a broad based comparative analysis with international frameworks. It also includes an analysis of key issues affecting the provision and legal framework of redundancy.

The Group has considered the adequacy of the legal framework in supporting successful transitions for workers and longer term mitigation of adverse labour market impacts. The adequacy of these laws and provisions has been examined at the level of individual employees and employers, and in respect of issues impacting on the wider economy.

The report is structured in four parts:

- Part one describes New Zealand's legal framework, an analysis of redundancy related research, describes and provides a summary of key themes from public and expert consultation
- Part two reviews how other systems (European Union (EU), North America, Scandinavia, Australia and international Conventions such as the International Labour Organisation (ILO)) regulate redundancy and provides a legal comparative analysis with New Zealand
- Part three examines the key issues resulting from the comparative analysis
- Part four provides recommendations based on the research and analysis conducted in this report.

The Group has considered the following areas of interest in its report:

- evidence from research on the extent of redundancy provisions in employment agreements, employer and employee experiences and extent of any problems with current arrangements
- whether any additional legal requirements should apply to all redundancy situations or should be more targeted
- the experience of other countries that have implemented similar requirements
- employees' and unions' experiences
- the costs of entitlements and compliance for employers
- relevant International Labour Organisation standards
- interface matters with the existing insolvency regime
- interface matters with Part 6A of the Employment Relations Act 2000, and
- portability of entitlements.

The Group also had regard for whether redundancy and restructuring situations disproportionately affect any particular groups, including any gender, ethnic and disability implications.

The Group's Terms of Reference require that the report provides recommendations on the following matters:

- statutorily prescribed consultation requirements
- the amount of notice employers must provide employees in the event of a redundancy
- consultation requirements to avoid mass redundancies, and
- a statutory requirement for redundancy compensation or other entitlements.

Recommendations

The Restructuring and Redundancy Public Advisory Group's recommendations are as follows:

RECOMMENDATION 1

That the government should consider the introduction of a statutory requirement for redundancy compensation and other entitlements incorporating the following features:

- a) notice of redundancy termination to the affected worker
- b) compensation based on length of service
- c) a maximum level of statutory compensation, and
- d) provision of redundancy support and other active labour market mechanisms to affected workers and organisations.

RECOMMENDATION 2

That the government considers the following options to implement Recommendation 1.

- a) A Code which acts as a guide to employers on notice, compensation, and other matters in respect of redundancy. Compliance with this Code will be voluntary but may form the basis of Government considerations of what constitutes a 'good employer' in the context of contracting and migration policy.
- b) A legal right to redundancy compensation with no specified formula. This could take one of two forms:
 - (i) First of all it could be a mechanism similar to that provided for 'vulnerable' employees in Part 6A of the Employment Relations Act 2000. This would mean that all workers would have the right to redundancy compensation. The quantum would be as agreed or could be referred to the Employment Relations Authority for settlement. The quantum set by the Authority or Employment Court could be subject to criteria which include firm size as well as length of service, industry practice and other matters.
 - (ii) The second option could be that all workers in a collective agreement have the legal right to redundancy compensation and the formula could be as agreed or as determined in the Employment Relations Authority or Employment Court.

- c) A statutory formula for notice and compensation. There are numerous options which include:
- (i) 4 weeks notice plus redundancy compensation based on 4 weeks for the first year of service and 2 weeks for each subsequent year up to a maximum statutory requirement for 26 weeks pay. This option is supported by the NZCTU.
 - (ii) A formula as in (c) (i) above but excluding workers on wages or salary of \$150,000 or more per annum.
 - (iii) A formula as in (c) (i) above but excluding workers with less than one year's service from compensation but including all workers for the 4 week's notice requirement.
 - (iv) A formula as in (c) (i) above but excluding employers of a specified size - for instance 1-5 workers.
 - (v) A formula as in (c) (i) above but with a maximum statutory payment - for instance 16-20 weeks, with the ability to negotiate additional payments above that level.
 - (vi) A formula as in (c) (i) above but with a sliding scale of notice based on length of service.
 - (vii) A combination of the above variations.
 - (viii) A formula based on the Australian National Employment Standard (see Appendix I, (To obtain this appendix, please send email to info@dol.govt.nz)).
- d) An insurance scheme to provide for redundancy compensation. There are several options including:
- (i) A levy based scheme similar to ACC which provides for payment only to those affected.
 - (ii) A levy based scheme with additional assistance from the Government.
 - (iii) A fund that is built up by contributions from employers, workers and possibly the Government but with 'worker accounts' rather than an insurance scheme.
 - (iv) A variation to KiwiSaver where there is a portion of contributions that can be accessed in a redundancy situation.
- e) A Redundancy Support Scheme which would exist alongside a statutory formula as in (c) (i) above. This would channel support to workers and employers in the form of active labour market assistance. However, it would also provide to employers that registered with the scheme and who employ fewer than 20 workers a rebate on the cost of redundancy compensation. This could be based on a maximum rebate of (e.g.) \$2000 per worker.

RECOMMENDATION 3

That if the government does introduce a statutory provision for redundancy notice and compensation it then considers ratifying ILO Convention 158.

RECOMMENDATION 4

That if the government does introduce a statutory provision for redundancy notice and compensation, it phases in such a provision with a one year delay. That in the one year period there is a major education and awareness arising campaign.

RECOMMENDATION 5

That if the government does introduce a statutory provision for redundancy notice and compensation then it ensures the Department of Labour and other relevant departments are resourced adequately to provide advice, develop calculators and other resources.

RECOMMENDATION 6

That notice of redundancy is a priority debt under the Companies Act 1993.

RECOMMENDATION 7

That redundancy compensation is non-taxable and that tax records are also used so that statistics on the incidence of redundancy can be recorded.

RECOMMENDATION 8

That the government enhance the Security in Change work programme. This should include:

- a) A major awareness raising programme on redundancy support.
- b) Developing connections with the Unified Skills Strategy so that lifelong learning is maintained throughout redundancy experiences and that Industry Training Organisations are actively involved in retraining support.
- c) Expanding the scope and level of support for workers made redundant.
- d) Widespread consultation with stakeholders on how to move to an 'employment security' framework.
- e) Consideration of cost implications for Government of enhanced Security in Change.
- f) Consider the possible interface between redundancy support, income maintenance, employment security and the investment in jobs for sustainability (e.g. home insulation).

RECOMMENDATION 9

That the consultation provisions required in case law between employers and workers in restructuring and redundancy situations are codified.

RECOMMENDATION 10

That employers are encouraged to notify the Ministry of Social Development of redundancies as early as possible but taking into account relevant commercial and other legal obligations for instance Stock Exchange disclosure requirements.

As can be seen from recommendation 1, the Group recommends work towards a formal framework incorporating notice and compensation. However, the report does not recommend a specific form for this outcome. The impacts of any one of the identified options on its own will not be uniform nor necessarily equitable. For that reason it will be necessary to undertake further work to determine the best mix of options for the wider New Zealand context. It is to be expected that wide consultation with interested groups will form a central feature of any implementation of the Group's recommendations.

PART ONE - BACKGROUND TO REDUNDANCY - NEW ZEALAND OVERVIEW

What is redundancy?

Redundancy is not defined in the Employment Relations Act 2000 ("ERA") but the commonly accepted definition today is that from the Labour Relations Act 1987. Section 184(5) of the Act defined redundancy as:

... a situation where...[a] worker's employment is terminated by the employer, the termination being attributable, wholly or mainly, to the fact that the position filled by that worker is, or will become, superfluous to the needs of the employer...

The emphasis in the definition, and in the case law since redundancy has been a feature of New Zealand's employment law jurisprudence, is on the position rather than the worker who occupies the position.

The common law accepts the right of the employer to determine the structure of the business and, therefore, to make positions redundant subject to any redundancies being genuine and carried out in a fair and reasonable manner (*G N Hale and Son Ltd v Wellington Caretakers etc IUOW*)¹. The ERA has overlaid this management prerogative with a statutory obligation to act in good faith, including specifically in relation to consultation over changes to the business (section 4(4)(c)), any proposal to contract out or sell or transfer all or part of the business (section 4(4)(d)) and making employees redundant (section 4(4)(e)).

Acting in good faith means, amongst other things, where the employer is proposing to make a decision that could mean an employee's employment is terminated, giving relevant employees access to information about the decision and an opportunity to comment on that information before a decision is made (section 4(1A)(c)).

The following situations may justify termination on the grounds of redundancy (subject to any termination having been carried out in a procedurally fair manner):

- reducing employee numbers for efficiency or cost cutting reasons, including on or following the appointment of a receiver to a business, or because the work can be done by other means, e.g. contracting out
- materially changing the job description applying to a position (changing duties and responsibilities), and
- relocating a business or position in a business more than a reasonable distance from its original place.

RESTRUCTURING

Restructuring is a process that often results in redundancy. For that reason it is also covered by the good faith obligations of the ERA whether or not redundancy is the final outcome.

¹ [1990] 2 NZLR 1079

TECHNICAL REDUNDANCY

A technical redundancy situation arises where an employee's employment with a particular employer is terminated as a result of the sale or transfer of the business to another owner, but the employee is offered the same position with the new owner on the same terms and conditions of employment, including recognition of service with the previous employer. In this situation there is a new legal employer and the employee cannot be compelled to transfer it. However, in most employment agreements providing for redundancy compensation, a technical redundancy situation is typically grounds to avoid payment of redundancy compensation. In these circumstances, if the employee elects not to transfer their employment to the new owner there is no entitlement to redundancy compensation.

Where ownership of the legal entity is transferred, as with a sale of shares rather than the business asset, there is not any form of redundancy.

Substantially similar positions

Most redundancy agreements provide for transfer into a substantially similar position as an exclusion to entitlement to redundancy compensation in circumstances in which redundancy compensation might otherwise be payable.

Review of current laws and provisions

The current law in relation to redundancy in New Zealand are covered as follows:

Section 4 of the Employment Relations Act 2000 which, among other things, provides that the duty of "good faith":

- a) requires the parties to an employment relationship to be active and constructive in establishing and maintaining a productive employment relationship in which the parties are, among other things, responsive and communicative, and
- b) requires an employer who is proposing to make a decision that will, or is likely to, have an adverse effect on the continuation of employment of one or more of his or her employees to provide to the employees affected:
 - (i) access to information, relevant to the continuation of the employees' employment, about the decision, and
 - (ii) an opportunity to comment on the information to their employer before the decision is made.

Section 4 is clear that good faith extends to:

- a) a proposal by an employer that might impact on the employer's employees, including a proposal to contract out work otherwise done by the employees or to sell or transfer all or part of the employer's business, and
- b) making employees redundant.

Part 6A Vulnerable Workers

The ERA defines some employees as "vulnerable employees". These employees attract special protections in the case of restructuring if their work is to be contracted out by their employer or their part of the business is to be sold. They may elect to transfer their employment to the organisation where the work has been transferred. A vulnerable employee includes the following categories of employees:

- a) cleaning services, food catering services, caretaking or laundry services for the education, aged-care and health sectors
- b) orderly services in the aged-care sector
- c) cleaning services or food catering services in the public service or local government sector
- d) cleaning services or food catering services in relation to any airport facility or for the aviation sector, and
- e) cleaning services or food catering services in relation to any other place of work. The new employer must decide how to best manage their resources. This may involve making transferred vulnerable employees redundant.

Justification

A redundancy can only be made for genuine commercial reasons and employers must be able to demonstrate that these reasons exist. The Employment Relations Authority or the Employment Court will consider the genuineness of the decision to make someone redundant, including whether the decision was made in "good faith".

Genuine reasons

Reasons for an employee's redundancy can include:

- the introduction of new technology
- rationalisations of staff to increase business efficiency
- restructuring business operations, including a change in the organisation's roles or location
- closure of business
- outsourcing, and
- sale of the employer's business.

In addition to having genuine reasons for any redundancy the employer must demonstrate they have carried out any termination on the grounds of redundancy to be procedurally fair.

In circumstances in which termination for redundancy is contemplated, it may be necessary for an employer to select between a number of potential candidates for redundancy. Selection criteria and the application of them must be consistent with the employer's obligation to act justified.

There may still be a genuine redundancy if the employee's tasks are delegated to other existing employees following the redundancy. However, if the employee is effectively replaced with someone else, then the redundancy is unlikely to be genuine. A genuine redundancy occurs when a position becomes superfluous to an employer's needs.

In the recent past, the test for whether a dismissal is justified has increasingly become contentious as the courts began to step back from considering the merits of an employer's decision to dismiss. Over time the test applied by the courts to determine whether a dismissal was justified gradually moved from objectively considering the conduct of an employer towards a subjective consideration of the actual employer's conduct. This shift was also seen increasingly in redundancy cases.

Amendments to the Employment Relations Act in 2004 introduced section 103A which established a new test for determining whether a dismissal is justified under the Act. Section 103A is intended to reinforce the concept of what a fair and reasonable employer would have done – determined on an objective basis. The policy intent is to ensure that there is balance between considering fairness to both the employer and the employee.

To date, only a small number of cases have considered the application of section 103A. In *Simpsons Farms Ltd v Aberhart*² the Employment Court specifically considered the application of 103A in a redundancy situation and confirmed that redundancy situations are within the ambit of the section. The Court also concluded that s.103 does not "revisit longstanding principles about substantive justification for redundancy" set out in earlier decisions such as *G N Hale and Son Ltd v Wellington Caretakers etc IUOW*.³ The Employment Court concluded that:

"Although Parliament was prescriptive in 2004 so far as process was concerned, on substance of justification for dismissal it appears to have been satisfied, by enacting s.103A, to return to the position espoused by ... Hale. So long as an employer acts genuinely and not out of ulterior motives, a business decision to make positions or employees redundant is for the employer to make and not for the Authority or the Court, even under s.103A."

A review of other relevant case law, which has been applied to other redundancy situations is attached as Appendix B (To obtain this appendix, please send email to info@dol.govt.nz).

Current New Zealand requirements

Notification

Knowledge of the possibility of redundancy is an obvious pre-requisite for consultation with unions and employees. This raises the issue of when such a possibility should be notified both to those affected, and wider. Notification to relevant government agencies is currently not required in employment statutes but is encouraged. There are some instances where notification is required; for instance, Stock Exchange disclosure requirements, requirements of employment agreements and any requirements relating to business failure i.e. receivership and liquidation.

² EC 2006 ARC 13/06

³ [1990] 2 NZLR 1079

Consultation

The requirement for consultation with affected parties before decisions are taken has been a central feature of procedural fairness for redundancy for many years.

More recently, the ERA expanded on historical provisions for consultation, aligning them to the concept of good faith and providing broad procedural guidelines.

The essential elements of “good” consultation are that the proposal must be precise enough to enable the employee to provide useful comment, employees are given a reasonable opportunity to consider the proposal, and feedback from the employee must be considered and taken into account before the final decision is made. Consultation therefore should begin as early as possible.

Underpinning these principles is the concept of “good faith”. This requires an employer who is proposing to make a decision that will, or is likely to, have an adverse effect on the continuation of employment of one or more of his or her employees, to provide employees with:

- access to information relevant to the continuation of the employees' employment, about the decision, and
- an opportunity to comment on the information to their employer before a decision is made.

Consultation does not require that the employer and employee agree on the employer's course of action. However, an employee who may be affected by a redundancy or restructuring must be given a real opportunity to provide feedback or input into the proposal, and the employer must consider such feedback with an open mind, and must make a genuine effort to accommodate those views.

The level and duration of consultation with an employee required in a redundancy situation will depend on the size of the business, and the urgency of the situation requiring the redundancy.

Notice of redundancies

Currently there is no statutory notice period that an employer governing when an employee must be advised that they will be made redundant. Notice periods where they exist typically are contained in employment agreements.

Redundancy compensation

In New Zealand, there is no statutory right to redundancy compensation, nor is there a common law right unless employers and employees or their union have agreed to one in the applicable employment agreement. The payment of redundancy compensation was most recently considered by the Advisory Group on Contracting Out and the Sale or Transfer of Businesses⁴ in 2003. Following this work, the Department of Labour considered a range of options relating to additional protections for vulnerable employees in contracting out or sale or transfer situations. This included considering whether there should be a statutorily prescribed minimum amount of redundancy compensation payable to vulnerable employees. This work subsequently resulted in Part 6A of the ERA and it

⁴ The Group comprised representatives of the New Zealand Council of Trade Unions, Employers' Federation and nominees from the State Services Commission, Minister of Labour, Ministry of Pacific Island Affairs and Maori Business Network. The Group was chaired independently by Nigel Haworth. A further Group was appointed to give further consideration to these proposals and advise the Government on options.

was therefore narrower in scope than this review. This review is the first comprehensive examination of redundancy matters for many years.

In 2003, Cabinet considered the question of whether redundancy compensation should be prescribed in the Act in relation to contracting out or the sale or transfer of a business. Cabinet agreed that if an employment agreement did not expressly provide for redundancy compensation to be payable, the parties would be entitled to negotiate over the matter [CAB Min (03) 18/11 refers]. This was reflected in Part 6A of the ERA which also provided for the Employment Relations Authority to determine the redundancy entitlements due to an employee in certain circumstances. Cabinet did not consider the broader question of whether redundancy compensation should be payable in wider circumstances in other redundancy situations.

Redundancy is a form of dismissal and is therefore subject to personal grievance provisions of the ERA. Compensation, damages and other remedies are available under these provisions.

Wage Adjustment Regulations 1974

The Wage Adjustment Regulations 1974 (reprinted in 1977) since revoked, dealt with redundancy in a negative way by restricting both the amount of redundancy compensation and the entitlement of claimants. Of particular interest is the reference to severance pay agreements between the Master Builders Federation and the Federation of Labour - see Appendix C (To obtain this appendix, please send email to info@dol.govt.nz).

They provided effectively for one week's pay (2 percent) for each year of service up to 20 years, and providing a minimum of one year that has been worked. The regulations also gave the then Industrial Commission power to approve redundancy agreements which provide better than the regulations - provided there were exceptional circumstances.

Other issues

Companies Act 1993

The Companies Act 1993 currently provides that a maximum of \$16,420 per employee is available for priority debts for unpaid wages, holiday pay and redundancy compensation when an employer is insolvent. Priority debts currently do not include notice of termination.

Holidays Act 2003

The Holidays Act provides minimum entitlements of annual holidays, public holidays, and special (including bereavement) leave. These entitlements also apply to employees made redundant and are not extinguished by redundancy.

Taxation of compensation

Currently, redundancy payments are treated as part of an employee's income; the tax rate used depends on the annual gross income of the employee. In previous years (up until 1992) only 5 percent of the redundancy payment was taxed this was at the earner's usual rate because payments were regarded as compensation.

The Income Tax Amendment Act (NO.4) 1992 provides that redundancy compensation is taxable assessable income in the hands of the recipients. Redundancy compensation

payments are treated as a lump sum payment in terms of PAYE but are not liable for the ACC earner levy or Fringe Benefit Tax (FBT). Redundancy compensation payments are, however, subject to student loan deductions.

The appropriate tax rate depends on the grossed up annual value of the employee's last 4 weeks' earnings and the payment. The tax rate applicable to the payment where the combined total of the payment and the gross value of the employee's income for the previous four weeks are:

- \$38,000 or less – is 21 percent or 21 cents in the dollar
- between \$38,000 and \$60,000 – is 33 percent or 33 cents in the dollar, and
- greater than \$60,000 – is 39 percent or 39 cents in the dollar.

Redundancy rebate

The redundancy tax rebate was introduced earlier this year to remedy the problem of overtaxing due to tax rates moving up a bracket when the redundancy payment was added to the employee's income. Legislation took effect as of 1 April 2008 to make the taxation of redundancy payments fairer to people who are pushed into a higher tax bracket when they receive the lump sum payment in the event of a redundancy. The rebate is based on a flat rate of six cents per dollar, for the first \$60,000 of the redundancy payment received per redundancy. The maximum amount claimable is \$3,600.

Redundancy compensation and effects on unemployment benefit

Prior to November 1992, redundancy payments were largely tax free. In addition, from March 1991, a separate stand down calculation for people who had received a redundancy payment and were applying for the unemployment benefit was introduced. This was calculated by dividing the amount of the redundancy payment by the weekly amount of benefit and family support the applicant would otherwise be entitled to receive. The maximum period of non-entitlement was 26 weeks. The separate redundancy stand down was removed in November 1992, when a withholding tax of 28 percent was introduced on redundancy payments. From this time, redundancy payments were included in the definition of income for the high income stand down.

Until recently, the stand-down for main benefits ranged from 1-10 weeks, depending on income prior to coming onto benefit. This has now been reduced to 1-2 weeks, which means that regardless of the amount of redundancy payment, people are able to qualify for a benefit relatively quickly.

The personal tax component of redundancy payments does not impact on clients benefit entitlement because the gross amount is used in the benefit assessment. Redundancy payments impact on commencement date of benefit since they form part of the average weekly income assessment to calculate the length of the stand-down (one or two weeks).

Reducing or removing the personal tax component of redundancy payments would deliver more disposable income, enabling employees to adjust their commitments to what is often a sudden and disruptive change in their circumstances. It may also increase the value of cash assets attributable to an employee. The value of cash assets is considered for a number of supplementary forms of assistance such as the Accommodation Supplement, Temporary Additional Support and Special Needs Grants.

Main benefits are not subject to a cash asset test, income earned (or forgone) from assets is charged against the benefit.

Portability of entitlements

There are limited examples of schemes internationally to assist the examination of portability of entitlements. This may stem from the difficulties inherent in establishing such approaches. One overseas example is, Manusafe, Australia.

"Manusafe has been described as a trust fund established by the manufacturing unions with the object of collecting, maintaining and distributing employee entitlements to long service leave, severance pay and accrued sick leave".⁵

Notwithstanding its good intentions, employers were reluctant to sign up to Manusafe for three main reasons:

- long service leave benefits purportedly secured through Manusafe are more generous than the current entitlement
- perceived cash flow difficulties from Manusafe in the manufacturing industry, and
- deficiencies in the Manusafe trust deed.⁶

Another issue with Manusafe, as with the perceived risk with other funding models, has been the potential for perverse business behaviour e.g. soft landings, and the fact that funding models more often than not rely on voluntary uptake. Many employers are reluctant to contribute "to funding other people's failure." For these and other reasons it seems portability oriented funding models have not been successful. The Group agreed, due mainly to the apparent costs associated with a model and the limited number of successful examples internationally, not to pursue this further in the context of this report. It may however be useful to explore for the longer term.

New Zealand redundancy research

Redundancy provisions in collective agreements

Victoria University analyses and the Department of Labour captures information on provisions contained in collective employment agreements. A complete set of the University's 2007 redundancy tables and several key Departmental graphs are available at appendix D (To obtain this appendix, please send email to info@dol.govt.nz). Below are key excerpts from these data sources:

- *78 percent of all agreements have pay and notice. Across all industries and sectors, 78 percent of collective agreements (covering 309,900 employees) contain provisions for pay and notice in the event of a redundancy situation.⁷*
- *Some sectors are far less likely to have redundancy provisions. Agriculture and other community services are far less likely to have collective agreements with redundancy provisions than other industries.⁸*

⁵ *Manusafe entitlements and the Manusafe controversy*, issue 4, November 2001, Workplace Relations

⁶ Ibid.

⁷ Leda Blackwood et al, *Employment Agreements: Bargaining Trends & Employment Law Update 2006/2007*, Victoria University

⁸ Ibid

- *Four weeks notice is most common.* Four weeks notice continues to be the most common length of notice given to employees who are made redundant (57 percent).⁹
- *Union recognition and consultation is generally high.* Most collective agreements contain union recognition and consultation clauses in the event of redundancy (77 percent), however, they are far more common in the public sector (87.5percent) than the private sector (68 percent).¹⁰
- *The 6 + 2 compensation formula is most common in the public sector but a range of options prevail in the private sector.* Information collected by the Department of Labour suggests that:
 - approximately a third of all collective agreements contain provisions for redundancy counselling
 - almost half of all collective agreements provide leave for job interviews, and
 - an opportunity to comment on the information to their employer before the decision is made.

Redundancy provisions in individual agreements

There is little information available on redundancy provisions in individual employment agreements. While bargaining trends in the collective sphere will have some influence and cross over into individual bargaining outcomes, the extent of this crossover is insufficient to make any assumptions about individual bargaining trends.

New Zealand business environment

New Zealand is predominantly a nation of small businesses, with most enterprises in New Zealand operating as small and medium-sized enterprises (SMEs). SMEs can be defined as enterprises with 19 or fewer employees and that the average enterprise has 14 workers. At February 2006¹¹:

- *96.4 percent of enterprises employed 19 or fewer people*
- *86.8 percent of enterprises employed 5 or fewer people*
- *63.6 percent of enterprises had no employees, and*
- *70.4 percent of employees were employed by 3.6 percent of enterprises.*

SMEs provide a strong base for New Zealand's economy with value-added output created by SMEs accounting for approximately 40 percent in the economy. SMEs a significant contribution to employment figures by accounting for 29.6 percent of total employment at February 2006 employing 522,180 people, up 1.8 percent from the previous year (around 70 percent of workers in New Zealand are employed by 4 percent of enterprises). A large chunk of part-time employees are utilised in SMEs. The number of SMEs increased by 3.6 percent in the year ended February 2006, although the proportion of SMEs remained relatively constant. Internationally, SMEs account for the majority of firms in OECD economies.

⁹ Ibid

¹⁰ Ibid

¹¹ *SMEs in New Zealand: Structure and Dynamics*, July 2007, Ministry of Economic Development.

Between February 2001 and 2006, firms in New Zealand with 500+ employees were the greatest contributor to employment reduction (a reduction of 93,500 (net) jobs) followed by firms with 1-5 employees (a reduction of 81, 690 (net) jobs). However, over this period SMEs accounted for 59 percent of all net new jobs in the economy¹².

Firm size does have an impact the way a business operates. Larger businesses tend to engage more on research and development activity and are also more likely to engage in innovation than smaller businesses. Training (including management training) provided for employees is more likely as firm size increases.

Individual employment agreements perspectives from New Zealand small enterprises

On the request of the Restructuring and Redundancy Public Advisory Group, the Department of Labour contracted Massey University to survey 5,500 small to medium enterprises (SMEs) to fill information gaps on restructuring and redundancy practices to understand redundancy provisions in individual agreements; and specifically, frequency rates for notice periods, compensation, outplacement support, interview leave and relocation assistance provisions. The survey also examined consultation behaviours of SMEs in redundancy or restructuring events. The size of organisations in the survey was 1-49 people per business.

The information indicated that while there were differences in responses from firms of different sizes (such as responses from businesses with 1-19 people compared with 20-49), the overall sample was in favour of the 1-19 group, so the results give a good indication of employment relation practices amongst SME's in general.

Key findings from the summary were:

- all but a small number of the SME owners had written employment agreements with their employees
- in the micro-firm sector 67 percent of employees are on individual agreements and 77 percent in the small firm sector
- from those having individual employment agreement with staff, in the event of redundancy:
 - 69 percent of employees have a notice period
 - 20 percent of employees are entitled to compensation
 - 13 percent of employees are allowed to take leave for a job interview
 - 9 percent of employees receive outplacement support, and
 - 4 percent of employees get relocation assistance.
- in the event of restructuring or redundancy, SME owners are most likely to notify or consult their shareholders, lawyer and their accountant before notifying the employee, and
- of government agencies, the Department of Labour and Ministry of Social Development are most likely to be notified or consulted.

¹² Ibid

Business dynamics

The New Zealand business landscape has strengthened in the last few years, but there are indications that the economy is slowing and accordingly we may expect an adverse effect on some businesses and communities over the next few years.

Statistics New Zealand business entry and exit statistics relate to the movement of firms into and out of businesses. Entry and exit statistics are not start-up and failure statistics. Businesses may exit due to administrative changes in restructuring or ownership such as amalgamations, mergers or acquisitions by other firms. However, administrative changes cannot always be identified as such through the entry/exit datasets.

As of February 2007 there were over 460,000 enterprises in New Zealand. While there has been a net increase in the number of firms entering into business, the number of firms exiting has steadily grown over the past 6 years. Of these at least 315,000 enterprises were sole traders and almost 135,000 were enterprises consisting of 1-19 employees. The enterprises employed just over 1.9 million people.

The number of businesses has grown steadily in the past six years from over 370,000 in 2002, jumping to almost 420,000 businesses in 2004, which corresponds to the strong economic boom during that period. However, the economy has stabilised and is now growing at a slower pace. This gives rise to issues that affect business dynamics such as productivity and firm turnover.

Firm turnover in New Zealand is not unusual when compared with other economies. Most firms' initial level of labour productivity upon entry is below the industry average but grows rapidly thereafter. Continuing firms generally add to industry labour productivity growth. On average exiting firms experience stagnant or declining labour productivity in the years leading up to their exit, and when they eventually end most have below industry average labour productivity. This pattern persists even at a highly disaggregated industry level and indicates that firm turnover has positively contributed to labour productivity growth in NZ¹³.

SMEs account for the majority of all entries and exits and, in particular, are dominated by firms employing 5 or fewer employees. Larger firms remain longer in business than SMEs. The majority of firms with 1-5 employees remained the same size over the period 2001 to 2006 and did not evolve into a larger sized firm. Throughout the same period, firms with 6-9 employees were least likely to remain the same size, but were split as to whether they evolve into either a larger or smaller size. Just over half the firms with 10-19 employees remained the same size from 2001-2006, with those that moved most likely to have down-sized rather than expanded¹⁴.

Innovation in the business is often synonymous with creative destruction. The benefits of creative destruction, as the new replaces the old, often comes with workplace failure and worker displacement and subsequent reallocation to new jobs. A critical unknown factor in the framework is how best to encourage innovation and manage the resultant creative destruction to maximise the net benefits from innovation. Seeking to lift innovation and productivity across a broad base of workplaces is likely to reduce the costs associated with destruction. In this sense, creative destruction can be both positive in terms of encouraging innovation and destructive in terms of redundancy and potentially displacing

¹³ Law, David and McLellan, Nathan *The Contributions from firm entry, exit and continuation to labour productivity growth in New Zealand*, March 2005, Treasury

¹⁴ *SME's in New Zealand: Structure and Dynamics*, July 2007, Ministry of Economic Development

workers. This process can be managed efficiently and effectively if both employees and employers are involved adequately in the process.

Insolvency and business start-ups

Currently New Zealand's insolvency protection for employees is set out in the Companies Act 1993. The maximum priority amount is set out in the Companies (Maximum Priority Amount) Order 2006 and provides that the amount for the purposes of clause 6 of Schedule 7 (including for unpaid wages, holiday pay and redundancy compensation) of the Companies Act is \$16,420 per employee.

Clause 6 of the 7th Schedule provides that if "a liquidation of a company commenced before the Companies Amendment Act 2006 came into force, that company's property must be applied in accordance with the priorities stated in this schedule on the date the liquidation commenced as if the Companies Amendment Act 2006 had not come into force."

Therefore if a liquidation commenced before 1 November 2007 the priorities and clause 6 set out in the 7th Schedule (i.e. that Schedule in force prior to 1 November 2007 amendment) apply. Clause 6 (prior to Nov 2007 amendment) provides that the maximum amount for certain priorities must not in the case of any employee exceed the prescribed amount.

The Insolvency and Trustee Service (ITS) does not administer all of the company liquidations in New Zealand. The majority of liquidations are administered by private liquidators such as accountants and lawyers. Ministry of Economic Development statistics indicate that average annual figures for insolvencies for the year ended June 2007 are company liquidations commenced: 3,991 company receiverships commenced: 291. These figures can be skewed by the fact that liquidation can go on for many years and in some instances, companies do not provide adequate information. Some companies may also place themselves into liquidation unnecessarily.

Comparatively, company liquidations have increased gradually over the past six years since 2002 from 0.33 percent to 0.86 percent of businesses. The number of businesses that have gone into receivership in the previous six years has remained steady at around 0.04 to 0.05 percent, however in the year June 2006 - June 2007, receiverships increased to 0.06 percent of businesses. The increased number of insolvencies in 2007 may have significant effects on the occurrence of redundancy and may also be correlated to the slowing rate of growth in the economy. However, it is important to consider that, as the number of insolvencies has increased, the number of total companies on the companies register has also increased literally in this time.

It is difficult to measure exactly how many or what amount employees receive for redundancy compensation payments in the event of insolvency. The ITS unfortunately does not hold this information and neither do IRD or any other State agency. When a company becomes insolvent it can be placed in liquidation by its shareholders, its board or by the High Court. When a company goes into liquidation its available assets are realised by the liquidator for the benefit of its creditors. A liquidator must first pay secured creditors out of the proceeds realised. Next, the liquidator must pay those entitled to a preferential claim and then distribute the proceeds rateably among all unsecured creditors. If there is a surplus, it is to be distributed either in accordance with the terms of the company's constitution or in accordance with the default provisions of the Companies Act 1993.

The preferential claims which apply in the case of a company insolvency are set out in the Seventh Schedule to the Companies Act 1993. Wages, salary and compensation for redundancy owed to the employees are preferential claims, which are paid before the unsecured creditors of the insolvent entity. Any money representing the unclaimed assets of the company is paid into the Liquidation Surplus Account, which is administered by the Public Trust.

There is no accurate 'start up' figure as business 'start up' figures do not currently include sole traders or limited partnerships and many of the companies that are set up do not actually start doing business (e.g. they are set up for Loss Attributing Qualifying Company (LAQC) as trusts and for tax purposes etc).

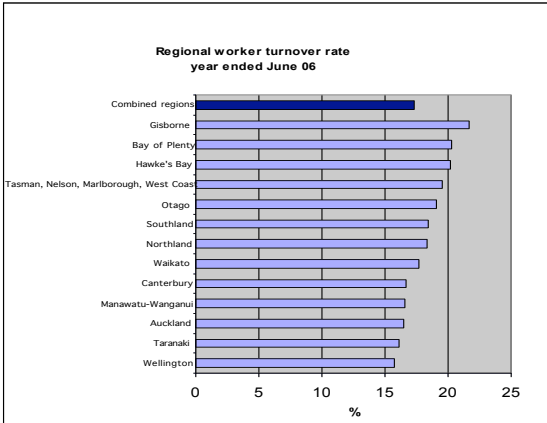
Incidence of redundancy and data on turnover rates

There are no official figures on the number of redundancies per year as redundancy notification to a state agency is not a statutory requirement.

Linked Employer-Employee Data (LEED) currently provides the best snapshot of overall churn in the labour market. LEED data measures the number of employees that leave businesses (separations) and job destructions. An unknown subset of these will be redundancies.

In the year to June 2006, over three hundred thousand employees per quarter began work in a business location (accessions) and almost three hundred thousand employees per quarter separated from a business, resulting in an average quarterly worker turnover rate of 17.3 percent. During the five-year period to June 2006, the worker turnover rate has remained at between 17.1 and 17.6 percent.¹⁵ Further trend series graphs showing job destructions and overall employee numbers are available in appendix E (To obtain this appendix, please send email to info@dol.govt.nz).

From an industry perspective, the agriculture, forestry and fishing industry had the highest average quarterly worker turnover rate, followed by the accommodation, cafes and restaurants industry. Both these industry groupings provide short-term seasonal work. The lowest average quarterly worker turnover rate was recorded in the manufacturing industry.¹⁶



¹⁵ Worker turnover rate is a measure of employment stability. A region or an industry with a low worker turnover rate is more likely to have stable employment. The worker turnover rate is the worker flow (or the sum of accessions and separations) as a percentage of the average of total jobs in consecutive periods. The average quarterly worker turnover rate for the year is the average of the turnover rates for four consecutive quarters.

¹⁶ Statistics New Zealand, Linked Employer-Employee Data: June 2006 quarter, released August 2007.

In addition to LEED data, a study by Statistics New Zealand is currently underway investigating the employment outcomes for displaced workers. It looks at the impact of closures on the future employment, earnings, and benefit receipt of the affected and unaffected employees. The project will provide information on labour market adjustment costs and the ease and speed with which displaced workers are re-employed. It is intended to support the Department of Labour's priority of increasing labour market participation.

Data from the Inland Revenue Department

Although, there is little information on redundancy compensation received, Inland Revenue (IRD) has attempted to estimate volumes of redundancy payments. The work was done as a one-off and there are no plans to update or replicate this analysis in the near future. However, there are some tangible results to come out of the work on redundancy payments. There is no variable for redundancy monies in IRD data, and so the data gathered resulted from a detailed process of elimination.

The analysis was performed for two years of employer data; the years ended 31 March 2004 and 31 March 2005. The numbers of workers found to be receiving redundancy compensation were almost 29,000 in 2004 with a total value of \$235.5 million and almost 30,000 in 2005 with a total \$238.9 million. IRD excluded employees over 60 years to avoid confusion with retirees.

The average value of a redundancy payment was approximately \$8,000 per each redundancy payment across both years. The analysis suggests that approximately 1.5 percent of employees were paid redundancy pay in 2005.

Redundancy information in the media

A review of media articles, spanning the last 12 months, has shown that the causes of redundancies are various, however, within certain industries there are common themes. For example:

- exporting and manufacturing business often cite the high New Zealand dollar as the primary reason for redundancies or closures
- larger businesses have relocated customer service and IT operations overseas in an effort to cut costs
- relocation to other parts of New Zealand
- business collapse, business going into receivership/liquidation, merging/consolidation of business operations, and
- cost cutting/efficiency factors enabling employer to meet budgets.

A table summarising key indices from all of these media articles is available in Appendix F (To obtain this appendix, please send email to info@dol.govt.nz).

Gender, ethnic and disability implications

Data from the 2006 census indicate that there are certain industries and geographical areas with a relatively high proportion of Maori or Pacific Island workers or female workers. According to the Household Labour Force Survey (HLFS) as of March 2008, there were just over 990,000 women in employment. They appear to be over represented in some industries such as Accommodation and Hospitality, Health and Social Services, Personal Services and Education. A number of jobs in these industries include vulnerable and low pay work, such as Homecare and Residential Care.

As of March 2008, there were approximately 205,000 Maori in employment (according to the HLFS). They appear to be highly represented in industries related to Manufacturing including Meat Processing, Sawmilling and Timber Dressing, Printing and Services to Printing, Construction, Transport, Wholesale, Personal Services, Health and Social Services. A number of these industries have large firms in smaller communities which are dependent on the firm for a large proportion of their economic activity. Pacific Island workers are also highly represented in Manufacturing, Transport, Health and Social Services, and Accommodation and Hospitality industries, particularly in the Auckland area.

Many of these industries identified above are also associated with low paid and low skilled jobs and the relatively high proportion of females and Maori and Pacific Island employees can increase the vulnerability of these groups, particularly in the event of a redundancy where it may be harder for them to gain a new job and also to have financial resources to support themselves through the transition period. More often than not a number of these industries can also be located in smaller communities, which can have an adverse effect not only on the worker but also on the community. The incidence of mass redundancies occurring is more frequent due to a slowing economy and the impact of globalisation, therefore attention must be given in the policy setting for possible implications of vulnerable workers and their displacement in the event of redundancy.

There is little information on the effects of redundancy on people with disabilities or any barriers they may face in re-employment.

Length of service

Women are more likely to have shorter service due, for example, to parental leave and related considerations. The proportion of women who hold the same job for over a year is approximately 30 percent for women compared to just over 34 percent for men. They are also disproportionately represented in part-time work with approximately 36 percent of employed women working part-time as compared to approximately 12 percent of working men employed part-time. Both these factors impact on the quantum of compensation due to redundancy that men receive as compared to women taken as a group¹⁷.

Older Workers

New Zealand is rapidly becoming more dependent on older workers to maintain the size of the labour force as the population ages, therefore it is prudent to encourage older workers to stay in the workforce for a longer period of time. International evidence suggests that once older workers have time out from employment, they are more likely to need assistance to re-enter the job market. It would seem wise when there is a rapid transition to give older workers a longer consultation period, particularly if trying to retain older workers from leaving the labour market altogether.

Labour market dynamics

The Department of Labour's regular forecasting activity and environmental scanning of the economy point to employment growth slowing over the next five years. In particular the manufacturing primary processing sector¹⁸ is forecast to barely grow over the next five years. These projections have been used to identify industries that are more likely

¹⁷ Based on Statistics New Zealand, LEED Job Tenure data, 2006

¹⁸ Primary processing includes Food, Beverage and Tobacco Manufacturing (such as freezing works and dairy plants), and Wood and Paper Products Manufacturing

to experience adverse labour market events. The industries within the manufacturing sector are very diverse but the specific industries that may be at a larger risk of job losses in the medium term are the Food, Beverage & Tobacco, Textiles & Apparel, Wood & Paper Products, Metal Product, Machinery & Equipment and Furniture Manufacturing Industries (which together employ around 160,000 people). These industries are exposed to outsourcing risks, have low projected employment growth and generally have large sites that would have a significant impact were they to close down.

At risk communities have been identified by examining current regional and employment data on the types of industries in these communities which are potentially exposed to a company or industry restructuring and large site closures. Areas considered are outside of the main urban centres which have a much greater ability to absorb employment shocks. The analysis showed that there are 61 non-metropolitan areas¹⁹ across New Zealand where more than 20 percent of employment, or 100 employees, are concentrated in a single industry (which may or may not be concentrated in a single firm). The attached maps in appendix G show the geographical locations of these at risk areas (To obtain this appendix, please send email to info@dol.govt.nz).

While many industries have some concentration in small areas, there are two or three main industries that dominate the data. Meat and Meat Processing, and Dairy Product Manufacturing are the two most frequently identified industries. Timber and its related industries are the next largest group of industries. There is a reasonable geographical spread of these concentrated areas of employment. There is a high share of concentrated employment in Waikato, but most regions in the North Island have some areas where employment is concentrated in a single industry. There is less concentrated employment in the South Island, with a high proportion of it located in Southland.

Public and expert consultation

Written submissions

The Group invited written submissions from members of the public seeking their views on the adequacy of current redundancy laws and provisions. Twenty-two written submissions were received, of which fourteen submissions (from businesses and professional groups) generally supported the current legal framework as adequate, while eight (from individuals, union representatives, community law advisers and academics) claimed that the current framework was not adequate and advocated changes.

A full list of the submitters, with an analysis of the common themes to emerge from the submissions, is attached as Appendix H (To obtain this appendix, please send email to info@dol.govt.nz).

Summary of the views from those advocating change indicated:

- Many workers are unable to bargain for redundancy entitlements and can only gain these by statutory means
- The "good faith" requirements of the ERA are overly broad and often avoided
- Compensation should be statutorily prescribed (and tax-free)
- Consultation and notice provisions should be strengthened
- Clarification of law and statutory definition is needed, and

¹⁹ We have excluded area units that are within 'City' territorial authorities

- Education about rights and responsibilities is also needed.

Views of those advocating status quo:

- Current law provides a workable platform
- “One size fits all” legislation would be inappropriate to the widely varying circumstances of restructuring/ redundancy situations
- Flexibility, not regulation, is needed for competitiveness in global market and to promote innovation
- Compliance costs are already heavy, particularly for SMEs
- Statutorily mandated provisions, especially regarding compensation, would do more harm than good, and
- Management prerogative is a fundamental tenet of employment law in New Zealand.

Specific issues raised in submissions:

In addition to comments for and against further legislation regarding consultation, notice and redundancy compensation, specific issues raised in submissions included:

- Whether special considerations apply in the case of:
 - SMEs (less able to cope with additional compliance costs and liabilities), and
 - Temporary, fixed-term and/or individual agreement workers (these groups particularly in need of statutory protection)
- Whether a Code of Good Practice to cover restructuring and redundancy situations should be developed, in lieu of regulation
- Whether the protection currently provided to “Vulnerable Workers” under Part 6A of the ERA should be extended to other employees
- Whether the Grievance Procedure provisions of the ERA (s103A) need clarification to provide an objective test for redundancy dismissals
- Whether the “Good Faith” requirement of the ERA should be clarified, e.g. regarding:
 - any situation in which consultation is not required, and
 - any situation that does not constitute a redundancy
- Tax treatment of redundancy payments.

Oral submissions

The Group consulted expert advice from key stakeholders, business groups, government agencies and academics to provide written and/or oral submissions. Oral submissions were received from eight submitters, other experts were invited but were unable to meet with the Group due to other commitments.

Key themes to emerge from oral consultation included:

- a greater focus was required for vulnerable employees and vulnerable sectors in the labour market
- the scale and impact of mass redundancies – especially in smaller centre and towns
- the balance between disclosure and notification – both for the employee and also for the market to manage

- current good faith principles are adequate for consultation requirements, and
- compensation – a fund model may create perverse business behaviour amongst employers e.g. soft-landings.

In particular, the New Zealand Stock Exchange highlighted the implications of redundancy notification and the effects on companies on the Stock Exchange. They indicated that although notice of an impending redundancy situation to a worker and State agency should be considerate of the worker's employment situation and provision of adequate redundancy support, any move to make redundancy notification a statutory requirement would have implications for the Stock Exchange. Confidentiality and a lack of assurance around disclosure of company information due to notification can have an adverse effect on corporate competitiveness.

The New Zealand Stock Exchange indicated that vulnerable workers are most at risk in the event of a redundancy. High income earners generally have the ability to look after themselves in the event of redundancy and do not need compensation protection as much as low income earners. In light of possible statutory requirements for compensation, income splitting was identified as a possible option to address equity issues through performance appraisals. This may mean that those who are made redundant and earn a high salary e.g. \$150,000+ may be exempt from performance appraisals in return for no compensation in the event of a redundancy.

The Small Business Advisory Group (SBAG) also provided a submission on the impact of regulatory requirements for small businesses. They highlighted the differences in business structure and resources available to small and larger firms, and that smaller sized businesses would struggle with additional compliance costs if statutory requirements were introduced. An impending redundancy or restructuring situation have far reaching effects in a smaller firm than a larger firm as many SME owners often have their own life-savings and homes on-the-line with their business and if the business goes under the owner risks losing everything they own as well as legal credibility in the case of bankruptcy. There is no one-size-fits-all approach to designing regulations and if a framework were to be explored for redundancy the implications for small businesses should be considered (which make up to 97 percent of businesses in NZ) and adapted separately for larger firms who have more resources and have a far greater impact on employment and communities through mass redundancies. They also pointed out that the small employer is often disadvantaged where an employee decides to leave, yet the employer simply has to cope with that situation.

It is also important to note the New Zealand Institute of Chartered Accountants (NZICA) view on accounting for redundancy provisions in business accounts. A redundancy situation cannot be accounted for in the accounts until the situation actually arises and only then can redundancy be crystallised in the financial reports.

NZICA also made reference to accounting processes in the European Union:

Regulation (EC) No 1606/2002

The International Accounting Standards (IAS) Regulation places an obligation on European companies whose securities are admitted to trading on a regulated market in the EU to prepare their consolidated accounts, as of 1 January 2005, in conformity with IAS/IFRS (International Financial Reporting Standards) and Standing Interpretations Committee/International Financial Reporting Interpretations Reporting Committee (SIC/IFRIC) issued by the International Accounting Standards Board (IASB) and endorsed by the EU.

Member states may permit or require this accounting framework to be applied to the consolidated accounts of companies whose securities are not admitted to trading on a regulated market in the EU and/or to annual (individual) accounts regardless of whether the company is admitted to trading on a regulated market in the EU. For a summary of the oral submissions please refer to Appendix H (To obtain this appendix, please send email to info@dol.govt.nz).

PART TWO - INTERNATIONAL REVIEW

Overview of legal protections in international jurisdictions

The relevant international instruments are the International Labour Organisation (ILO) Termination of Employment Convention, 1982 (No. 158) ("Convention 158") and the Termination of Employment Recommendation (No. 166) (Recommendation 166). These instruments set out the key principles relating to the dismissal of workers, including redundancy situations. In addition to placing emphasis on severance pay (funded directly by the employer or a fund constituted by employer contributions, or social security benefits or a combination of both), notice periods and appeal periods, it also focuses on member States encouraging employers to consult with worker representatives to consider alternatives to mass layoffs.

New Zealand has not ratified Convention 158 and is therefore not bound by its provisions. Recommendations by the ILO are not able to be ratified by member States and therefore New Zealand is not bound by the provisions of Recommendation 166.

Convention 158 includes:

- a) Article 12 which provides for employees to be entitled to a severance allowance upon termination of employment
- b) Article 13 which requires employers to consult workers representatives when they are "contemplating termination of employment for reasons of an economic, technological, structural or similar nature", and
- c) Article 14 which requires employers to provide notification to the competent authorities where the employer is contemplating redundancies.

The New Zealand Government's long-standing policy and practice – applying to all international treaties – is that it will only ratify such conventions, and thereby incur legal obligations thereunder, when it can fully comply with them. Many of the principles under Articles 1-11 in the Convention 158 have been implemented into New Zealand redundancy law. Several countries with similar legal systems to New Zealand including Canada, Ireland, the United Kingdom and Australia have not ratified Convention 158.

The review on legal protections in international jurisdictions provides an interesting basis to consider New Zealand's position comparatively to international trends. While statutory provisions for redundancy are intrinsically linked to some labour market policies and international obligations, this does not prevent New Zealand taking guidance for what does work well in other jurisdictions.

The majority of jurisdictions limit their requirements to collective redundancies, however unfair dismissal claims are still available for individual redundancies. These are not explicitly considered in this review.

European Union and international labour standards play a key role in setting the framework for legal protections for redundancy and restructuring situations. Legal protections in Europe tend to be more prescriptive and are largely driven by European Union directives. While there are differences between European economies and the New Zealand context, European developments are still informative.

In considering notice and redundancy compensation requirements, the Australian National Employment Standards (NES) was recently released by the Federal Labour Government. The Standards will apply to all Australian employees regardless of their

industry or occupation from 1 January 2010 - see Appendix I (To obtain this appendix, please send email to info@dol.govt.nz).

In summary, there are a number of international initiatives, statutory provisions and social plans which New Zealand could seek value in from either considering or adopting. While New Zealand provides consultation requirements which are on par with other jurisdictions, this is the extent of statutory protection that employees are entitled to. The provision of notice periods and social plans in other jurisdictions are worthy of consideration. The breakdown of requirements reviewed for the respective jurisdictions and a comparative analysis are attached in Appendix J (To obtain this appendix, please send email to info@dol.govt.nz).

PART THREE - ANALYSIS OF ISSUES

Notification

Notification of the possibility of the redundancy is an obvious pre-requisite for consultation with unions and employees. Notification to relevant government agencies is currently not required in employment statutes but is encouraged. There are some instances where notification is required for instance Stock Exchange disclosure requirements, requirements of employment agreements and any requirements relating to business failure i.e. receivership and liquidation.

It is difficult to measure the number of redundancies that occur every year, in various sectors, regions and for what reasons. A review of media coverage on recent redundancy situations and information from Ministry of Social Development (MSD) indicates that there are a large number of redundancies occurring in particularly small communities which has not only an adverse effect on employees but also the community both economically and socially.

Relevant aspects of notification include:

- informing a state agency of a redundancy situation
- informing and working with unions and employees, and
- disclosure of information to the Stock Exchange.

Commercial sensitivity is important to consider when notifying agencies and unions of the potential event of redundancy. A balance has to be struck between when MSD and employees are notified and also when the Stock Exchange should be notified. The employer may have good intentions by notifying MSD as early as possible, allowing appropriate assistance measures to be deployed for when the announcement occurs, however, there is always the risk that the news maybe leaked to employees particularly if it is in a smaller town. On the other hand, it can be difficult for State assistance to be deployed effectively if they are only told a few days or in some circumstances the day before a redundancy situation is announced.

Confidentiality and assurance of information provided in the notification can also have an impact on the share market. Information in the public domain on an impending redundancy can have an adverse effect on the share market as investors may 'catch wind' of the commercial status of a business, resulting in the share value of the business falling. Regardless, a balance must be struck between the fairness to shareholders and equitable notion of informing the employee in the event of a redundancy: it should not come as a shock to the employee if there is an impending redundancy situation.

The comparative analysis of New Zealand and international jurisdictions indicates that there are a number of countries who require compulsory notification of redundancies to a State agency, for example, the United Kingdom requires notification of redundancies over 20 employees and in the United States notification is required of a redundancy situation of more than 100 employees in a firm.

The Group's view

The Group recognises the obvious advantages of having compulsory notification of redundancies to a State agency, particularly in the event of mass redundancies in New Zealand and the potential impact on smaller communities. Compulsory notification to an

appropriate State agency is beneficial in dealing with displaced employees in advance of mass redundancies being announced and businesses closing.

The Group is however mindful of the balance required in notifying appropriate parties in a redundancy situation. Parties to a redundancy event include employees, unions, State agencies, and also the share market. Too much information in the public domain through notification have an adverse effect on the share market as investors may 'catch wind' of the commercial status of a business on the Share Market, affecting corporate competitiveness.

An non-compulsory option which would to ensure State assistance is provided in a timely manner and in consideration of providing fairness to the employee, is that the employer could inform the State agency of the 'potential' of a redundancy during the consultation process with employees during which assistance is not 'officially' deployed but resources are organised and information from the employer regarding skill-sets of the employee/s is matched to appropriate jobs as quickly as possible. If the 'potential' redundancy does arise, then it will:

- not be of surprise to the employee, and
- the State agency can be event ready and release resources immediately once the decision is final.

It is important to note that regardless of how much time a State agency has, the assistance provided should always be as best, event ready.

Other options could include a Code of Practice or minimum requirement in legislation for notification to a State agency. Compulsory notification to a State agency may require a threshold, such as 20 or more redundancies will need to be notified by the employer. The balance between incentivising compliance and penalising employers who do not comply may also need to be considered. Resourcing and administrative costs will also have to be considered if a compulsory notification of redundancies to a State agency is to be considered.

The Group has explored current policy work being done by MSD and the Department of Labour (DoL) in tracking redundancies and Security in Change work to providing earlier support for people at risk of redundancy. The outcomes of a pilot approach to tracking redundancies, and the assessment of the impact of redundancy events on the local communities, should provide a better overview of the requirements and costs associated with pursuing statutory notification to a State agency of a redundancy event.

The Group considers that it is preferable at this stage to encourage employers to provide early notification to relevant government agencies rather than introducing a statutory notification requirement.

Consultation

It is generally accepted that "good faith" requirements in s.4 of the ERA relating to redundancy require consultations with the employees or the union prior to declaring redundancies. In the past, good faith principles has been applied accordingly to employment relations matters including redundancy. In general, "good faith" principles have a strong basis in New Zealand's employment relations in comparison to international jurisdictions.

Employers have to follow a fair process when dismissing an employee for any reason. The required procedural steps in a redundancy situation depend on the individual

circumstances of each case. It is not just the act of consultation that is important, but the quality of the consultation should be meaningful in determining the right decision making processes.

Case law has stopped short of making consultation an absolute requirement. In *Aoraki Corp Ltd v McGavin*²⁰ it was noted that to impose an absolute requirement to consult would lead to impracticalities in some situations e.g. mass redundancies.

Relevant factors when considering the need for consultation include:

- the position held by the employee, e.g. whether they are in a management role²¹
- the size of the company, in a small workplace consultation will usually be expected²², and
- the employee's length of service²³

Victoria University's 2007 analysis of employment agreements suggests that for the most part, collective agreements recognise a role for the relevant union(s) in the event of a redundancy. However, union recognition clauses in the private sector are much more likely to be limited to advising the union of a redundancy prior to, or at the same time as, giving redundancy notice to employees.

CONSULTATION PROCESS

In any consultation process the employee should be given the opportunity to consider any proposal to disestablish his or her position and to comment on it. The employee should be given a reasonable opportunity to consider the proposal and feedback from the employee must be considered before the final decision is made. If a fair and meaningful procedure has been followed, then the employee should already be aware that his or her job is at risk and that their comments and suggestions regarding the situation would have been considered by the employer.

Alternatives to redundancy should be considered by the employer in the consultation process, ideally considered with the employee. The prevalence of redundancy counselling, job interview leave and relocation assistance is common in collective agreements, unfortunately there is little known about individual agreements. However, other alternatives a business should consider when consulting is retraining, positions in other companies within the same group and voluntary redundancy.

The Group's view

Consultation is a statutory requirement in any process of restructuring and redundancy. In addition, there is extensive common law on this matter. The Group's view is that this appears to be adequate but that consideration be given to codifying the relevant common law.

²⁰ *Aoraki Corp Ltd v McGavin* [1998] 1 ERNZ 601

²¹ *Dymocks Franchised Systems (NZ) Ltd v Robson* unreported, Shaw J, 4 December 2001, AC 80/01

²² *Holmes v Ken Rintoul Cartage & General Contractors Ltd* [2002] 2 ERNZ 130

²³ *McGuire v Rubber Flooring (NZ) Ltd* unreported, Travis J, 2 March 2006, AC 9/06

Notice

Currently there is no statutory notice period that an employer must comply with when an employee is advised that they will be made redundant.

Employers are entitled to make employees redundant, but any redundancy needs to be conducted in "good faith". Redundancies need to be genuine and employers must carry out a fair process. The focus should always be on whether the position is redundant, and not on the person. Redundancy cannot be used to dismiss an employee for misconduct or poor performance.

Providing adequate notice is imperative in allowing the employee to prepare for a redundancy event and for government assistance to be deployed appropriately.

The issue of adequate notice period has been brought before the courts and explored in case law. The courts have made a number of comments on the purpose of notice periods in redundancy situations.

Notice periods:

- give employees certainty over when their employment will end and allow them to plan accordingly²⁴
- allow for negotiation of redundancy agreements²⁵
- give employees the opportunity to adjust to the changed circumstances²⁶, and
- enable employees to try and find employment whilst employed, which is of itself a position of advantage.²⁷

It is important that employers comply with the notice provisions set out in their employment agreements and failure to give the required notice will make the employer liable for arrears of wages.²⁸ The denial of adequate notice is also a breach of an employer's obligations of fair dealing and good faith.

Although "reasonable" notice may be implied into employment agreements²⁹, redundancy is a special case where common law principles relating to reasonable notice offer little guidance.³⁰ "Reasonable" notice depends on the circumstances of each situation and has recently ranged from one week³¹ to two months.³²

Data gathered on collective agreements for 2007, indicate that four weeks notice period seems to be the most common allowance, but there are still some sectors who either provide little or no notice to their employees other than that specified for ordinary termination. Differential periods of notice may exist in some agreements but the practical effect maybe that some employees may get compensation instead of adequate notice period.

²⁴ *A-G in respect of DGSW v Richardson* [1999] 2 ERNZ 866

²⁵ *Hands v WEL Energy Group Ltd* [1992] 1 ERNZ 815

²⁶ *Kitchen Pak Distribution Ltd v Stoks* [1993] 2 ERNZ 401

²⁷ *Farmers Transport Ltd v Kitchen* unreported, Shaw J, 14 December 2006, WC 26/06

²⁸ *NZ (with exceptions) Electrical etc IUOW v Remtron Lighting Ltd (in rec)* [1990] 1 NZILR 583

²⁹ *Ogilvy & Mather (NZ) Ltd v Turner* [1995] 2 ERNZ 398

³⁰ *Charta Packaging Ltd v Howard* [2002] 1 ERNZ 10

³¹ *Muller v Taam Gardens Ltd and Ors* unreported, YS Oldfield, 21 June 2005, AA 226/05

³² *Ayers v Advertising Works Ogilvy Ltd* unreported, L Robinson, 20 October 2006, AA 324/06

Four weeks notice seems to be the most common notice period amongst collective agreements, however there are some sectors where it is less than one week and can have a far greater impact on the employee. For example, in service sector industries such as restaurants, hospitality and retail – one week notice is the most common amount of notice period. Workers in these jobs are often on minimum wage and with one week's notice it is difficult to consider options or find other work given the short time to adjust.

4 WEEKS NOTICE OPTION

Providing adequate notice is primarily an adjustment issue. The consequence of a minimum four weeks notice period is that employees will at best be prepared for the redundancy event, look for other work and seek assistance where possible such as counselling, training, government assistance etc. Notice is particularly important in the event of mass redundancies and for smaller communities where the impact of redundancy can be felt far greater both through economic and social circumstances.

A four week minimum notice period may also be important in the event of insolvency as it allows employees, employer and State agencies to prepare adequately before the firm is closed down. In the event of some insolvencies, a four week notice period maybe of no value, however a business should have some knowledge of its commercial status to be able to provide notice at an earlier stage. Voluntary redundancy and notice may also be different depending on requirements. Currently, Schedule 7 of the Companies Act does not have any requirements around notice period for redundancy in the event of insolvency.

Another issue related to time apart from providing adequate notice to the employee is untaken leave. This should not be offset by the notice period e.g. four weeks notice and if there is leave owing for the employee they should be able to take that leave. Another option is of course unless otherwise agreed, requirements stated in an individual agreement.

Some countries operate their mandatory notice requirements on a slide scale based upon services and age of employee in recognition of a greater time period required for some employees to prepare for their dismissal e.g. in Australia where the notice requirement is adjusted where an employee is over 45 years of age and with at least 2 years continuous service with the employer. This takes into account the difference that increased age can make for older workers as they are re-entering the workforce and to provide greater opportunity to find a new job. This may have some advantages for New Zealand, particularly in the area of skills shortages and the potential that older workers can have on workforce numbers and the economy.

Fairness is important in the event of redundancy, as the redundancy announcement should never be a shock or a surprise to the employee. If adequate notice period is provided, then this allows time for the employee to adjust to the news and make appropriate plans for their future particularly for those who are in vulnerable labour markets.

In providing adequate notice period, the length of service may be of value from an employee's perspective and for the employer to note. Business continuity when notice is provided is crucial in regards to the timing and who the notice goes to. In smaller business', employees maybe in touch with their employers on a more day-to-day basis and are more often than not aware of the businesses commercial position. In larger

organisations, employees may not be in touch with their employers on a frequent level as might be in smaller businesses or aware of the company's commercial position.

The Group's view

The Group agrees that the Government should consider the introduction of a statutory notice requirement of redundancy termination. This requirement could possibly be a code of practice or introduced through legislation as an appropriate vehicle to administer the minimum notice requirement e.g. four weeks.

The Group views a statutory requirement of four weeks notice, which is currently implied in most collective agreements as adequate in ensuring that employees are treated fairly in redundancy situations.

Another option is a notice period based on service.

Where the Group has recommended consideration of options for redundancy compensation that could exclude either the employees of small firms or employees with less than one year's service, separate consideration should be given to providing statutory notice of redundancy applying to all employees.

The Group has separately recommended that notice should be a priority debt under the Companies Act 1993.

Compensation

In New Zealand, there is no statutory right to redundancy compensation, nor is there a common law right unless employers and employees or their union have agreed to it in the employment agreement.

Currently, compensation is accounted for in at least 78 percent of collective agreements. A common formulation in the public sector is the 6+2 formula, which is 6 weeks wages for the first year of service and 2 weeks wages for each year of service thereafter. Outside the public sector there is wide variation but a breakdown is provided in Appendix D (To obtain this appendix, please send email to info@dol.govt.nz). There is little information available for those on individual agreements, however it can be said with some confidence that 'management' and higher income earners are commonly provided redundancy compensation.

There appear to be trends in given sectors ranging from the finance and business services sector which is at the high end to mining and metals manufacturing at the low end.

WHAT IS THE PURPOSE OF COMPENSATION?

Redundancy compensation generally recognises:

- that the termination is involuntary and not due to individual performance
- the loss of service related benefits
- the opportunity cost for the employee of the period invested with that particular employer, and
- the risk of not finding a comparable job and the impact generally on the earning power of the employee.

The Group note also that the Courts have formed views that compensation for redundancy also provides some income assistance for the period following termination.

An entitlement to redundancy compensation can also act as a deterrent where an employer might otherwise make an employee redundant without due consideration of alternatives.

In addition for employees, redundancy compensation contributes to employment security and can encourage prospective employees to consider employment in situations where there is a perceived risk of redundancy.

OPTIONS TO PROVIDE FOR COMPENSATION

There are several options for delivering statutory options for redundancy compensation. These include:

- a code
- a legal right to redundancy compensation with the amount to be determined by a third party (e.g. ERA Part 6A)
- a statutory formula, and
- a redundancy fund or levy based arrangement.

Aligned with any of the chosen options there could be a variety of support systems and approaches to assist workers affected by redundancy.

Code

Options include:

- an enforceable code of employment practice to apply to redundancy situations and including a guide on redundancy compensation or statutory compensation requirements, and
- a set of guidelines illustrating best practice.

Either option will require information and education prior to implementation.

A legal right to redundancy compensation with the amount to be determined by a third party

This option would be similar to the provisions of Part 6A of the ERA. It would provide for redundancy compensation. However, the amount would be agreed between the parties or, in the event that agreement was not possible, be determined judicially.

This approach would allow for the amount of compensation to be appropriate to the particular circumstances.

However, this approach does have some disadvantages. For employees, lack of information and bargaining power may result in little or no compensation. For employers, there is the risk of time-consuming and costly legal processes.

It may be that a pattern of compensation would emerge from a series of court decisions that would act as an effective guide to employers and employees.

Another option is to require that all workers in a collective agreement have a right to redundancy compensation based on the above approach.

Statutory formula

There are a considerable number of options in how to provide for a statutory formula. These include a simple formula based on length of service such as 4 weeks first year of

service and two weeks pay for each subsequent year. A number of adaptations could apply.

There could be an exclusion above a specified level of remuneration e.g. \$150,000. This would recognise that senior employees at or above this level of pay commonly have compensatory provisions in their employment agreements.

There could be an exclusion below a specified number of employees. This would recognise that there are a large number of very small businesses for whom standard statutory approaches may create disproportionate effects. However, such an exclusion from a statutory requirement in employment law would represent a departure from the usual New Zealand approach of universal application of statute regardless of firm size.

Employees with less than one year's service could be excluded. This would be consistent with other statutory entitlements based on length of service. This would also mean that statutory compensation would be targeted at those with a reasonable period of employment. It is estimated that up to a third of all employees would have less than one year's service based on current turnover statistics. This would mean that the first year of service would count towards compensation but eligibility would be for employees of one year's service or more.

There could be a maximum statutory level of compensation with the provision for negotiated payment above that level.

There could be a combination of the above adaptations.

The mix of options needs to take account of such things as basic business demographics.

Funding models

In considering options for compensatory funding models the Group agreed that the primary aim for any model is that there should always be money available to distribute for compensation to employees in the event of a redundancy.

- a) Self Insurance – Employers remain responsible for funding statutory redundancy entitlements, and can fund that either through their own balance sheet or by taking insurance with a third party provider.
- b) Compulsory Compensation Insurance - Employers remain responsible for funding statutory redundancy entitlements, and must take insurance with a third party provider to ensure payments are available even in an insolvency situation.
- c) Levy – Employers (and possibly employees) pay a payroll-based levy to a centrally managed fund which then meets statutory redundancy payment costs (similar to the levy collection under ACC scheme, but with only lump sum compensation payable as per the statutory formula).
- d) Contributions – Employers and employees (and possibly government) make contributions representing a small proportion of wages into one or more managed funds (similar to Kiwisaver) which then provides any lump sum compensation payable as per the statutory formula.
- e) General Taxation – Government funds statutory entitlements from general taxation (effectively an enhanced social security or unemployment benefit in redundancy situations).

Options (b) through (e) offer higher funding certainty, but with varying degrees of compliance and administration costs. Options (b) through (d) potentially open another source of short and medium term investment funding in New Zealand, potentially

assisting capital deepening and through that productivity. Options (b) through (e) could have reduced administration costs, greater efficiency and lower risks if they were firmly aligned with a similar funding scheme already in operation for another purpose (e.g. (b)) private income protection insurance, (c) ACC, (d) Kiwisaver, (e) Unemployment Benefit payments made by MSD) rather than set-up on a stand-alone basis.

Self insurance

This option has minimal compliance costs, and is effectively the funding status quo for current redundancy entitlements contained in employment agreements. It provides no greater certainty of payment of any statutory entitlement than does the current system of meeting redundancy entitlements in employment agreements.

Compulsory compensation insurance

This option would be similar to a normal business insurance type model, whereby the employer seeks income protection for their employees who may in the future be made redundant. This is a competitive business insurance type model, and insurance companies could specifically cater for these business costs that would be incurred by the employer in ensuring their employees are secured for redundancy compensation. Some form of insurer of last resort may be required to cover firms who do not actively seek or gain insurance cover.

In the event that the business goes into receivership, the money would then be transferred from the insurance fund to the receiver and the insurance company effectively becomes a creditor to the receiver. However, redundancy payments will be paid to employees and any monies that is left over from the receivership will be credited back to the insurance company.

The benefit of this is that similar to a levy option the cost of the insurance can be borne by the employer but matched in employee contributions. An insurance model would ensure payments are made to employees in the event of redundancies.

The risk is that larger organisations may be able to afford insurance costs related to business income protection whereas smaller sized firms may struggle to bear the cost of an insurance levy. Similar to a levy option, premiums may have to be set according to the history of the business and as such an appropriate criteria will have to be set.

There may also be scope for perverse business behaviour, where businesses may deliberately go under, either to start afresh or to get rid of employees in order to recoup some money for personal benefit or to start another business. To counter-act perverse business behaviour, strict conditions and criteria would need to be set, to ensure this does not happen. However, for this reason and also for genuine redundancy cases, some employers may be put in the position where they have to subsidise either perverse business practices or a genuine case of a business going under when they may be in a financially secure position that they may never need to access the funds.

Similar to a levy option, the added business cost for the employer may mean that the employer does not increase the employee's wage or salary due to another business compliance cost.

Another risk is that the insurance company will go under, but in most insurance companies it would be considered that they would have an underwriter – essentially a global insurer underwriting the insurance company which is insuring the business for redundancy compensation.

Levy

A compensation levy option could be developed, which could be based on a scheme similar to the current ACC funding model, whereby firms are rated according to their industry, number of injuries or deaths per industry etc and a levy cost is then identified according to criteria for the type of the business.

In the context of employment relations and redundancies, this would require a business to be rated in regards to a set criteria and a levy rate would then be set for the employer. A rating criteria could involve:

- length of existence for business
- profits, and
- industry average.

So, for example, a business that has been in existence for a period of time, has consistently demonstrated good returns on profit and in an industry with low average for redundancies would have a lower risk rating and as such a lower rate set for a levy. The levy could be contributed via a payment solely from the employer or the levy cost could be divided between employer and employee.

The benefit of this approach is that the cost of the levy could be shared by both employer and employee, and the levy fund ensures that there will be money available to pay redundancy compensation if required.

The risks associated with this option is that it could be extremely expensive to establish and allocate resources to as it would need to be setup in a similar format to the current ACC corporation. Given the cost associated with resourcing, administrating e.g. who will develop criteria and rate businesses annually for their redundancy compensation levy may not be very cost effective.

A funding model can also create disincentives for employers by creating opportunities to engage in perverse business behaviour e.g. to access the compensation fund for either their personal benefit or to start another business.

For this reason and also for genuine redundancy cases, some employers may be put in the position where they have to subsidise either perverse business practices or a genuine case of a business going under when they may be in a financially secure position that they may never need to access the funds.

Due to the added business cost for the employer there maybe the risk that the employer does not increase the employee's wage or salary.

Contributions

This model would operate on a similar level to kiwi-saver in that there would be employee, employer and government contribution to a fund. But the government contribution does not necessarily need to be a fiscal contribution towards a monetary compensation it could also be in the form of providing training. The State already provides similar initiatives, whereby training initiatives are subsidised by the government for employees.

Data obtained from IRD from 2005 indicate that nearly thirty thousand compensation payments were taxed and the value of these compensation payments was \$238.9 million which roughly equates to \$8000 per payment for each redundant worker. This data

indicates that if a contribution either from the State or the employer were to be introduced it could be at a cost of \$2.50 per week per employee.

The benefit of this option is that the cost is borne by all three parties – employer, employee and the State ensuring credibility to the fund and that money will be available for employees in the event of redundancy. Redundancy compensation need not be associated with a wholly monetary compensation option for the employee. The form of compensation should also allow for training initiatives for the employee to engage in, which would make for better skilled employees re-entering the workforce.

As with the levy type option, there are resource and administrative costs associated with this option which could be very costly. The scope for perverse business behaviour also exists, so strict requirements would need to be developed for the fund so as to avoid perverse practices. It can be roughly calculated that from the IRD data, 1.5 percent workers were made redundant in 2005. This indicates the economic life cycle issues as 2004-2005 respectively were strong years economically, but when the economy is slower it would be expected that redundancy payouts would be more commonplace as economic activity and GDP is lower leading to more incidences of redundancy. The economic life-cycle would potentially affect the above options too via higher premiums.

Similar to the other options, the added business cost for the employer may mean that the employer does not increase the employee's wage or salary due to another business compliance cost. Again as mentioned in other options, some employers may be put in the position where they have to subsidise either perverse business practices or a genuine case of a business going under when they may be in a financially secure position that they may never need to access the funds.

Income protection for the above options would be tax deductible.

General taxation

This option could be delivered through a number of ways:

- it may require extending some parameters around the unemployment benefit so as to include a compensation equivalent of four weeks work (which the employee would have been doing had they not lost their job) on top of the unemployment benefit, and
- through active labour market policies (ALMP) such as providing for a counselling service, CV writing course, training.

The Government could establish a fund dedicated to redundancy provisions by providing an amount e.g. \$50 million to a labour market dynamics fund and which can be applied to employees made redundant.

A criteria may need to be established so as to ensure uptake of the ALMP, and that the benefit can only be accessed if the ALMP services have been approached.

The benefit of this approach is that this would enable better State assistance to be deployed to those who need it, particularly those who have been in the same job for a long time and may need assistance with searching for new jobs.

It also ensures that people do not take up the unemployment benefit immediately after redundancy and not utilise any other services available to them, to find a new job.

However, the cost of this option would be borne by the tax payer and as discussed earlier the cost may be high or low for the respective year depending on the economy and the number of redundancies.

KiwiSaver

Further options the Group discussed included using the KiwiSaver scheme as a fund. This option may be in the form of an additional employer contribution in KiwiSaver to provide redundancy insurance. It could alternatively be a provision that allows a proportion of employer and worker contributions to be withdrawn in the case of redundancy. However, the Group agreed these options would work best if the KiwiSaver option was compulsory. The Group's view is that the KiwiSaver options are too complex and risks undermining the objectives of the KiwiSaver scheme.

Funding models – overseas

The international review indicated that there are some funding models in international jurisdictions which support the payment of redundancy compensation. For example, in Ireland there is a scheme, where employers who comply with all redundancy requirements are entitled to a 60 percent rebate from the Social Insurance Fund. Employers are required to make regular payments into this fund through Pay Related Social Insurance contributions. Where an employer is unable to pay the employee their entitlement, the Department of Enterprise, Trade and Employment pays the full amount directly to the employees from the Social Insurance Fund. This system guarantees payment to employees, and provides incentives for employers to comply with redundancy requirements such as notice.

Summary of funding models

The funding models identified above all provide some level of benefit but more so risks for those involved. The benefit in the models is that they all ensure compulsory compensation to the employee, which is vital allowing the employee to find other work whilst still managing to pay for expenses.

The risks identified indicate that any one of these models would be costly, resource and administratively intensive to operate. The models may also be unfair for employers who may end up subsidising the cost for businesses with bad practices and it may also encourage perverse business behaviour amongst some employers.

Affordability of the funding models is a crucial issue that could affect businesses. The cost of providing for compulsory compensation via these models may see employers cutting back on other parts of their business such as investing in training or increasing wages or salary of staff.

The cost of the funding model may be dictated also by the state of the economy as with any economic cycle, if the economy is slow and GDP is low then it could be predicted that redundancies may occur more frequently given the business climate and as such may push the cost of the funding model and premiums high.

It is important to note that as there is little data available on the number of people who actually receive a redundancy payment, it may be worth reviewing data or developing a mechanism by which this information can be obtained. This information will help inform a better understanding of the requirement of a funding model and the structure of a mechanism.

Redundancy support scheme

The Group has included the option of a redundancy support scheme. This builds on the initiatives already developed on "Security in Change". A Redundancy Support Scheme provides a way to consolidate and expand the scope of current MSD assistance as well as provide access to a rebate for small employers on the cost of redundancy compensation.

This would also have the effect of increasing the number of employers that engage on active labour market mechanisms.

It is recognised that active labour market mechanisms work best when many employers are engaged. However in practice it is likely that only larger firms will participate. What is proposed in the Redundancy Support Scheme is that all employers that register with the scheme are eligible for a range of services and that workers and unions can also notify the MSD to ensure that redundancy support mechanisms are made available in a redundancy situation. In some cases it may be possible to avoid redundancies due to high levels of information about possible firm closures and new employment opportunities.

However, it is also possible for such a scheme to include provision for a rebate for small employers for the cost of redundancy compensation. This would be on way to ensure that all workers have the same entitlements regardless of firm size, assist small employers with the costs of compliance with the statutory requirements, and promote active labour market mechanisms. If the statutory formula excluded workers with less than one year's service, the Group does not believe that the cost to Government of a rebate needs to be of a very large sum. In any case such a provision can be calibrated based on the definition of small firm that applies and the extent of the rebate.

It is suggested that only employers that register with the scheme are eligible but that the effect of registration for a small employer should not be onerous. The Group notes that there is already in operation a payroll subsidy for small employers that recognises the disproportionate cost to small employers in the provision of PAYE details to Inland Revenue.

The Group's view

The Group was able to reach agreement that the Government should consider the introduction of a statutory requirement for redundancy compensation based on length of service. However, we did not reach a firm conclusion on the quantum delivery mechanism for such an entitlement. Accordingly the Group has also discussed a range of options as set out above. These options will need further analysis and policy development. They include a statutory formula for all workers and variations, which exclude some workers, some employers, and cap the statutory minimum compensation.

The Group has also considered a fund or levy-based scheme.

The Group has proposed further consideration of a Redundancy Support Scheme, which would channel support for workers and employers affected by redundancy and in the case of small employers provide a rebate on redundancy pay.

ILO CONVENTION

International Labour Organisation Convention 158 and Recommendation 166 relating to the termination of employment set out the key principles relating to the dismissal of

workers in redundancy situations. This includes placing emphasis on severance pay, notice periods and appeal periods.

The Group's view

The Group discussed the implications of New Zealand ratifying ILO Convention 158. The Group's view is that there is no point in attempting to ratify the Convention unless a statutory provision for redundancy compensation is provided and only then should the Government initiate the ratification process.

TAX TREATMENT OF COMPENSATION

Redundancy compensation is currently fully taxed. The current tax treatment appears to be unfair given that redundancy compensation is not an earning in the normal sense of the word. The tax treatment could be more generous to redundant employees. In previous years (up until 1992) redundancy compensation were taxed at a rate of 5 percent of the redundancy payment and at the earner's usual rate because payments were regarded as compensation. The Group proposes a tax free option or a lower tax rate, e.g. five percent.

The Group notes that some relief was provided earlier in 2008 through the Income Tax Act 2004, Income Tax Act 2007, and the Tax Administration Act 1994 being amended to provide a new rebate (renamed "tax credit" in the Income Tax Act 2007) for redundancy payments. The rebate is a flat rate of six cents in the dollar, capped at the first \$60,000 of redundancy payments in relation to each redundancy event.

Before this amendment, depending on the level of a person's earnings, receipt of a redundancy payment arguably could result in over-taxation when the redundancy payment pushed the person's total earnings over an income threshold and therefore onto a higher marginal tax rate. There was no tax relief available for redundancy payments. The rebate will mean low and middle income workers will not be adversely affected by having an artificial tax rate applied to their redundancy payments.

For example, an employee receives a redundancy payment of \$80,000. His redundancy payment rebate is capped at the maximum of \$60,000 redundancy payment, giving a rebate of \$3,600 ($\$0.06 \times \$60,000$).

A new definition of "redundancy payment" has been included in legislation. A definition is required so that redundancy payments qualifying for the rebate relate to payments which arise from a genuine redundancy and have been subject to the PAYE rules.

In Australia, redundancy payments up to a certain amount are tax free. The tax-free limit for the 2006–07 year is a flat dollar amount of \$6,783 plus \$3,392 for each completed year of service. ($\$7,020^* + \$3,511^*$ for each completed year of service * for the 2007/08 financial year and will be indexed each financial year).

Anything paid over that is an ETP (Eligible Tax Payment). This amount will be taxed but at a special low tax rate. The employer is responsible for paying the compensation, there is no Government funded redundancy scheme.

The Group's view

The Group agrees that the tax rate of redundancy compensation should either sit as tax free – similar to Australia and other jurisdictions or that 5 percent of the payment should be taxed as was previously done before 1992.

PRIORITY DEBT

Pay in lieu of notice is not currently regarded as priority debt under the Companies Act 1993.

The Group's view

The group considers that at least 4 week's pay in lieu of notice should be included as a priority debt within the overall limit of \$16,420 per employee.

TIMING OF IMPLEMENTATION

It is recognised that implementation of a statutory provision for compensation and other matters is a significant change to the minimum code. It would therefore be advisable to allow a reasonable time before such requirements come into force to allow employers to adapt. During this period there should be an extensive education and information campaign.

Redundancy compensation does not crystallise as a contingent liability until a redundancy situation arises. However, a statutory obligation for employers to compensate redundancy workers is a realisable and potentially significant cost and that is further reason to allow time to adapt.

A disadvantage of a delayed introduction is that it could build momentum around a date of application and result in some works being made redundant just before the statutory requirement comes into force. However, this is unlikely as it would be a one-off situation with few or no long term benefits to the employers.

The Group's view

The Group considered that depending on the nature of any statutory requirements an implementation period of one year was appropriate.

RESOURCES

It is important to recognise that any addition to the minimum code needs to be enforced. Ideally there should be a major education campaign advising employers and workers of their rights and obligations. But in addition there would be requirements for ongoing resources, calculators, staff who are trained and available to provide advice and labour inspectors. Further, if there is an extension in active labour market policies (ALMP) such as Security in Change, there needs to be adequate resources provided.

The Group's view

The Group recognises that implementation of a statutory provision implies a need for additional resources in relevant government departments and agencies.

THE IMPACT OF POSSIBLE STATUTORY REQUIREMENTS ON THE UNEMPLOYMENT BENEFIT

It could be argued that having statutory provision of redundancy pay may ensure that people to some extent have sufficient means to look after themselves for a longer period before the need to grant a benefit. For example, if the minimum statutory redundancy

pay was the equivalent of 2 weeks pay, it could be argued that it would be appropriate for people to wait that long before MSD are prepared to look at granting a benefit, similar to what MSD do with holiday pay.

It is worth noting that a person is not entitled to benefit for any period of paid notice whether notice period is worked or not worked. It is regarded as a continuing payment from employer when it is determined the 'cessation date of employment'. Another point to consider is that setting a statutory notice period gives a guaranteed period during which MSD can work intensively with people to find them other suitable employment.

An important issue to note is how the redundancy payments are treated for Working for Families (WFF) Tax Credit purposes. If the payments are not taxed, they may not want to include them as income for WFF tax credit purposes, if they are taxed they would almost certainly be included as income. Therefore, people getting WFF tax credits might experience an unexpected reduction in their entitlement and possibly a debt as a result of a new statutory redundancy payment.

Government services

The Government is currently engaged in a number active labour market policy work in relation to redundancy. The implementation of the Employee Security in Times of Change project is being led by MSD and is developing ways to engage with industry, unions and government to provide support earlier on in redundancy processes to affected employees.

EMPLOYEE SECURITY IN TIMES OF CHANGE

MSD is leading the implementation of the Employee Security in Times of Change work programme. In April 2007, Cabinet agreed to introduce a range of processes to help ensure that workers at risk of redundancy are better identified and provided with the services and support they need to obtain alternative employment at an earlier stage than at present.

The initiatives involve developing ways of proactively engaging with unions, associations and firms, and providing support to workers being made redundant. These initiatives are relationship-based, and in November 2007, Cabinet agreed that it was desirable to widen both industry and governmental agency involvement in the partnership scheme.

An employee redundancy support fact sheet developed by the Security in Change Steering Group is attached as appendix K (To obtain this appendix, please send email to info@dol.govt.nz). This describes support that MSD provides to workers in the event of a redundancy.

MINISTRY OF SOCIAL DEVELOPMENT SERVICES

MSD is most actively involved with providing assistance to employees in the event of a redundancy by ensuring services such as counselling, CV writing, employment search etc are all provided where possible. In some situations, employment may be found for employees made redundant but the new job may be some distance away from their hometown. MSD is able to provide support to workers who are displaced as a result of redundancy, such as providing assistance in relocation costs or travel costs for those who may have to travel some distance from their home and community to another part of the country to work.

There is also a 'jobs for you' (Jobs4U) scheme, which is a mechanism that MSD applies to reduce matching time for the employee to the new job. MSD does this by matching the appropriate skill-set of the employee to jobs available whether in the same community or at a location which is in travelling distance of their home.

In providing assistance, early notification would enable MSD to activate rapid response units to affected areas, particularly if they are smaller communities and have the risk of negative flow on effects affecting more than just the employees. However, as discussed earlier notification must be balanced with commercial sensitivity both for the employee and the employer in order to communications about redundancy are handled in a timely tactful, appropriate and direct way.

A challenge facing Government agencies is in ensuring that appropriate support services are delivered in a timely manner at the point of need. This implies the need for contingency planning to ensure that the appropriate infrastructure and support mechanisms, involving a range of government departments, other agencies such as territorial authorities, tertiary providers, relevant ITOs and others, can be quickly and smoothly brought in to play as and when necessary.

The MSD also provides Redundancy Support pages on the Work and Income website at <http://www.workandincome.govt.nz/employers-industry/redundancy-support.html>, which describes the employment training, financial support, job search, mentoring and other services that MSD can offer in the event of a redundancy.

Work and Income officers are often deployed to areas where redundancies have occurred and provide first hand support to employees who have lost their jobs as a result of a redundancy.

DEPARTMENT OF LABOUR SERVICES

Department of Labour provides information on the Employment Relations Act 2000 on its website www.dol.govt.nz to guide employers when they are faced with making a redundancy decision. The Department's Workplace Contact Centre also provides information to both employers and employees on the Employment Relations Act 2000 and dispute resolutions.

Department of Labour supports competency, and champions workplace practices that lift productivity and drives innovation. It also works to assist workers who are displaced by the process of creative destruction that is often associated with innovation, by providing information on skills that are in shortage, and better matching training available to workplace demands. Employment regulations can also modify the creative destruction process (such as restrictions on the use of contracting out). Government has a strategy to increase the adoption of global knowledge (Treasury is preparing policy on this), which needs to more explicitly incorporate increasing the absorptive capacity of workplaces.

ACTIVE LABOUR MARKET POLICIES (ALMP)

There is also scope to address redundancy and restructuring in smaller and rural areas through ALMP. Cabinet has recently agreed that the DoL pilot an approach with up to ten firms in small towns and rural areas to investigate ways to improve access to, and take-up of, business assistance services so that labour market and community outcomes are

improved. This approach will support both economic and social objectives. Improving government support for firms in rural areas or small towns could result in:

- firms remaining viable over the long term, which will help secure the labour market outcomes of rural communities and small towns
- individual workers accessing government services, for example work-based training programmes, so that they develop transferable skills that help secure their longer-term employment outcomes, and
- communities strengthening and, where possible, diversifying their employment base through engagement with economic development agencies, territorial authorities and government agencies.

It is envisaged that the Department of Labour's Labour Market Knowledge Managers (LMKMs) would facilitate this approach in close collaboration with the regional networks of other agencies including New Zealand Trade and Enterprise, the Tertiary Education Commission, the Ministry of Social Development and the Ministry of Economic Development.

Tracking redundancies

A number of activities are in train to provide earlier support for people at risk of redundancy. As part of the Security in Change approach, Ministry of Social Development and Department of Labour are piloting an approach to tracking redundancies. This work will monitor the labour market outcomes of people who have been made redundant and speed up the provision of customised support. An innovative feature of this pilot is the involvement of the National Distribution Union, acting as the main provider to deliver services to all affected staff, such as assessment interviewing, the preparation of personal employment plans, providing a resource centre and mentoring services. The wider impact of the redundancy events on the local communities is also being assessed.

Unified Skills Strategy

The Unified Skills Strategy is aimed at improving the skills of the existing workforce and ensuring firms have access to skilled workers whilst mindful of the need to increase productivity.

Action six of the strategy proposes 'Improved access to careers and labour market information and advice for adults in the workforce, including enabling pathways within and between industries'. This strategy is anticipated to help employees in times of job transition when affected by redundancy, by increasing awareness of current government provision of career and labour market information and enhancing the range of information and tools on the Career Services website and their other suite of services. Other training initiatives that could be leveraged off include iwi training initiatives that engage with employees in affected communities.

Worker displacement issues

In the consultative process, Te Puni Kokiri raised the issue of worker displacement especially amongst Maori, who in the event of a redundancy (particularly if they receive a redundancy payment) may tend to head back to their Whanau, iwi and land to gain security during an unsecure time in their life. The redundancy approach taken here is more of a collective approach where the effects of the redundancy are shared by the Whanau and not just by the employee. Redundancy compensation provides opportunities

that can be utilised in many ways to assist not only the affected employee but also their Whanau and iwi.

Worker displacement can often have an impact not only on the community they leave but also on the new communities they enter (especially in the event of mass redundancies in a small area such as Oringi, April 2008). For example, demographic movements of redundant employees from an urban centre to rural areas where employees may want to connect with their iwi, land or Whanau again - in a time of insecurity can have a big impact economically on the smaller centres. Similarly, the same effect can apply to redundancies that occur in small centres and employees move to larger, urban areas putting at risk the economic viability of many businesses in the smaller centres.

This indicates the issue of job transition and managing the shift in skills and workforce from one geographical area to another when redundancy occurs. This places pressure on both old and new communities to provide employment to affected employees and to those who have returned to be with their Whanau or iwi (this issue is also dependent on the length of time the employee will stay in the region). This shift, during a time of skills-shortages in New Zealand poses a broader policy interest in terms of productivity, skills retention and recruitment and job prospects/ employment security.

The Group's view

Redundancy has many implications for (ALMP), which are targeted at assistance for employees, skills retention, productivity, and employment security (job transitions). The Group agrees that further work needs to be done in addressing these issues, especially in retaining redundant employees in New Zealand and in the workforce and to address productivity and skills-shortages issues.

The scope of assistance needs to be wide and the appropriate government agency should be event ready – in New Zealand's case it is MSD – with other agencies ready and able to provide assistance as may be needed in the circumstances of specific redundancies. The role for government can also be extended to research and development, which can be encouraged further with qualification or tax incentives.

In addition there may be opportunities to link workers affected by redundancy into new opportunities that are emerging – for instance around home insulation, solar heating, major construction projects and so forth. The Group recognises that this will not be easy as there are many factors that impact on a successful matching of worker and employer needs.

PART FOUR – RECOMMENDATIONS

Recommendation 1

That the government should consider the introduction of a statutory requirement for redundancy compensation and other entitlements incorporating the following features:

- a) notice of redundancy termination to the affected worker
- b) compensation based on length of service
- c) a maximum level of statutory compensation, and
- d) provision of redundancy support and other active labour market mechanisms to affected workers and organisations.

Recommendation 2

That the government considers the following options to implement Recommendation 1.

- a) A Code which acts as a guide to employers on notice, compensation, and other matters in respect of redundancy. Compliance with this Code will be voluntary but may form the basis of Government considerations of what constitutes a 'good employer' in the context of contracting and migration policy.
- b) A legal right to redundancy compensation with no specified formula. This could take one of two forms:
 - (i) First of all it could be a mechanism similar to that provided for 'vulnerable' employees in Part 6A of the Employment Relations Act 2000. This would mean that all workers would have the right to redundancy compensation. The quantum would be as agreed or could be referred to the Employment Relations Authority for settlement. The quantum set by the Authority or Employment Court could be subject to criteria which include firm size as well as length of service, industry practice and other matters.
 - (ii) The second option could be that all workers in a collective agreement have the legal right to redundancy compensation and the formula could be as agreed or as determined in the Employment Relations Authority or Employment Court.
- c) A statutory formula for notice and compensation. There are numerous options which include:
 - (i) 4 weeks notice plus redundancy compensation based on 4 weeks for the first year of service and 2 weeks for each subsequent year up to a maximum statutory requirement for 26 weeks pay. This option is supported by the NZCTU.
 - (ii) A formula as in (c) (i) above but excluding workers on wages or salary of \$150,000 or more per annum.
 - (iii) A formula as in (c) (i) above but excluding workers with less than one year's service from compensation but including all workers for the 4 week's notice requirement.
 - (iv) A formula as in (c) (i) above but excluding employers of a specified size - for instance 1-5 workers.

- (v) A formula as in (c) (i) above but with a maximum statutory payment - for instance 16-20 weeks, with the ability to negotiate additional payments above that level.
 - (vi) A formula as in (c) (i) above but with a sliding scale of notice based on length of service.
 - (vii) A combination of the above variations.
 - (viii) A formula based on the Australian National Employment Standard (see Appendix I (To obtain this appendix, please send email to info@dol.govt.nz)).
- d) An insurance scheme to provide for redundancy compensation. There are several options including:
- (i) A levy based scheme similar to ACC which provides for payment only to those affected.
 - (ii) A levy based scheme with additional assistance from the Government.
 - (iii) A fund that is built up by contributions from employers, workers and possibly the Government but with 'worker accounts' rather than an insurance scheme.
 - (iv) A variation to KiwiSaver where there is a portion of contributions that can be accessed in a redundancy situation.
- e) A Redundancy Support Scheme which would exist alongside a statutory formula as in (c) (i) above. This would channel support to workers and employers in the form of active labour market assistance. However, it would also provide to employers that registered with the scheme and who employ fewer than 20 workers a rebate on the cost of redundancy compensation. This could be based on a maximum rebate of (e.g.) \$2000 per worker.

Recommendation 3

That if the government does introduce a statutory provision for redundancy notice and compensation it then considers ratifying ILO Convention 158.

Recommendation 4

That if the government does introduce a statutory provision for redundancy notice and compensation, it phases in such a provision with a one year delay. That in the one year period there is a major education and awareness arising campaign.

Recommendation 5

That if the government does introduce a statutory provision for redundancy notice and compensation then it ensures the Department of Labour and other relevant departments are resourced adequately to provide advice, develop calculators and other resources.

Recommendation 6

That notice of redundancy is a priority debt under the Companies Act 1993.

Recommendation 7

That redundancy compensation is non-taxable and that tax records are also used so that statistics on the incidence of redundancy can be recorded.

Recommendation 8

That the government enhance the Security in Change work programme. This should include:

- a) A major awareness raising programme on redundancy support.
- b) Developing connections with the Unified Skills Strategy so that lifelong learning is maintained throughout redundancy experiences and that Industry Training Organisations are actively involved in retraining support.
- c) Expanding the scope and level of support for workers made redundant.
- d) Widespread consultation with stakeholders on how to move to an 'employment security' framework.
- e) Consideration of cost implications for Government of enhanced Security in Change.
- f) Consider the possible interface between redundancy support, income maintenance, employment security and the investment in jobs for sustainability (e.g. home insulation).

Recommendation 9

That the consultation provisions required in case law between employers and workers in restructuring and redundancy situations are codified.

Recommendation 10

That employers are encouraged to notify the Ministry of Social Development of redundancies as early as possible but taking into account relevant commercial and other legal obligations for instance Stock Exchange disclosure requirements.

As can be seen from recommendation 1, the Group recommends work towards a formal framework incorporating notice and compensation. However, the report does not recommend a specific form for this outcome. The impacts of any one of the identified options on its own will not be uniform nor necessarily equitable. For that reason it will be necessary to undertake further work to determine the best mix of options for the wider New Zealand context. It is to be expected that wide consultation with interested groups will form a central feature of any implementation of the Group's recommendations.