

**IN THE EMPLOYMENT RELATIONS AUTHORITY
CHRISTCHURCH**

[2015] NZERA Christchurch 105
5538911

BETWEEN MICHAEL TALBOT BLAXALL
Applicant

A N D BLAXALL OPTICS VISION
LIMITED
Respondent

Member of Authority: Helen Doyle

Representatives: Michael Hanna, Advocate for the Applicant
Paul Bendall, Advocate for the Respondent

Investigation Meeting: 21 May 2015 at Christchurch

Further information
supplied : 28 July 2015

Date of Determination: 30 July 2015

DETERMINATION OF THE AUTHORITY

A The real nature of the relationship between Mr Blaxall and Blaxall Optics Vision Limited was not that of employment and the Authority does not have jurisdiction to deal with his claim.

B Costs are reserved.

Employment relationship problem

[1] Blaxall Optics Vision Limited (Blaxall Optics) is a duly incorporated company having its registered office in Christchurch. It carries on business as an importer and distributor of vision aids and optical products.

[2] Following the incorporation of Blaxall Optics on 1 June 2012 Michael Blaxall was the sole director and majority shareholder of the company. There were three other shareholders, Gang Cheng and Mr Blaxall's parents, Peter and Helen.

[3] On 16 January 2014 pursuant to a shareholders agreement Mr Cheng became a majority shareholder of the company and a director of Blaxall Optics.

[4] Mr Blaxall was removed by Mr Cheng as a director in December 2014.

[5] Mr Blaxall claims that he was an employee from the date that Blaxall Optics commenced trading in or about October 2012. He wants the Authority to make a determination that Blaxall Optics should have paid tax on his drawings and for directions about production of financial statements for financial years 2013 and 2014. He also says that Blaxall Optics ceased paying his salary from 2 October 2014 until 19 December 2014 when he was removed as a director. He wants to be paid the sum of \$11,126.52 being twelve weeks' salary for that period and be reimbursed expenses paid for on his credit card in the sum of \$1,328.87.

[6] Blaxall Optics does not accept that Mr Blaxall was ever an employee of Blaxall Optics. It says that in or about April 2014 there was an adjustment made to the manner of payment of his drawings. It says that correspondence confirms that there was a process of a fixed payment being made to Mr Blaxall negotiated by the directors and the company accountant and this was simply a package for a working director and shareholder rather than one of employment.

The issues

[7] The following issues are for determination:

- (i) Was Mr Blaxall an employee of Blaxall Optics?
- (ii) If Mr Blaxall was not an employee of Blaxall Optics then the Authority has no jurisdiction to consider his claim.
- (iii) If Mr Blaxall was an employee of Blaxall Optics is he entitled to payment of tax, production of financial accounts, payment of the sum of \$11,126.52 and reimbursement of expenses in the sum of \$1,328.87.

Was Mr Blaxall an employee of Blaxall Optics?

[8] Mr Blaxall until January 2014 held 55.71% of shares of Blaxall Optics. His parents Peter and Helen Blaxall held 7.14 shares each and Gang Cheng had a 30% shareholding.

[9] Mr Blaxall said that he was the general manager of Blaxall Optics and responsible for its day to day operation. He dealt with orders and stock including imports and had customer contact working about 50 hours per week. He claimed vehicle expenses and for his home office. He used his American Express card for company expenses and he was reimbursed for those expenses. Mr Cheng who resided in China was not I find involved in the day to day running of the company until he became a majority shareholder and director in 2014. In response to a question about holidays Mr Blaxall advised that for the period before April 2014 it was his company and *he did not need to check with anyone*.

[10] The evidence supports that until in or about April 2014 Mr Blaxall took weekly drawings throughout the year of \$650 but other drawings were taken by Mr Blaxall. Mr Blaxall in his evidence referred to taking drawings when he moved house and there is currently an issue between Blaxall Optics and Mr Blaxall about whether he had taken drawings from Blaxall Optics for tax for a period that predated the incorporation date of Blaxall Optics. Mr Blaxall had signing authority for Blaxall Optics cheques.

[11] Mr Blaxall said that Blaxall Optics was responsible for paying tax on the drawings and that at the year end the company would credit an amount to him to pay tax. He said that despite requests the financial accounts have not been prepared for years ending 31 March 2013 and 31 March 2014 by the company accountants Paul Bendall and Associates. The Inland Revenue Department has issued him with personal default assessments and in the absence of financial records he cannot assess his tax liability accurately. Mr Blaxall says in response to issues now raised by Blaxall Optics about drawings that he has put his own personal money into the company including from loan advances and that proper account needs to be taken of both drawings and loans.

[12] Mr Bendall is the company accountant and says that until 31 March 2014 the basis of Mr Blaxall's declared shareholder salary was on the distribution of the

company's pre-tax net profit. Drawings were taken in anticipation of an annual declared and taxable salary being sufficient to cover all the drawings. Mr Bendall says that Mr Blaxall's annual shareholders salary was not sufficient to meet total drawings.

[13] Pursuant to a shareholders agreement dated 16 January 2014 (the shareholding agreement) Mr Blaxall transferred 4,200 of his shares to Mr Cheng and Mr Cheng became a majority shareholder and a director at that time. At that time the respective shareholdings of Mr Cheng and the Blaxall family became 60% and 40%.

[14] Clause 7 of the shareholding agreement provided that until determined otherwise the company shall be controlled and managed by a board of two directors. Each director had the right as long as he held shares in the company to appoint and remove one of the directors.

[15] The shareholding agreement and constitution which was, Mr Bendall said, the standard companies office issued one did not deal with employment of directors/shareholders.

[16] There were discussions following Mr Cheng becoming a majority shareholder. Mr Blaxall was concerned for reasons set out earlier about his tax situation. Mr Cheng said that there were cash flow problems with the company but he did not have authority to see the bank accounts so had to ask Mr Blaxall to look at them and was concerned about excessive drawings by Mr Blaxall. There is some evidence that supports there were no funds available to put towards any tax payments for Mr Blaxall for earlier years.

[17] There was a shareholders meeting on 15 February 2014 about the cash flow issues and Mr Blaxall agreed to make a payment into the company of \$11,000 and Mr Cheng an injection of funds of \$10,000.

[18] Following discussions after that meeting Mr Bendall sent an email to Mr Blaxall and Mr Cheng about establishing a current market salary on 7 March 2014. He proposed a package which included the following:

Gross Annual Salary \$65,000 which includes Employer Kiwi Saver of 3% minimum and the ESCT tax on that.

Total estimated value \$2,500.

Company vehicle – Toyoto RAV4 with an FBT fringe benefit tax on a contribution basis for private use days. (a change to current account).

Mobile phone – existing one with company paying the account.

Standard as per NZ employment law – Public holidays, annual leave, sick & bereavement leave.

Weekly Payments based on 85% of agreed salary with a further payment at Financial year end based on either a distribution of company net profit OR the business achieving performance measures such as sales or net profit set at mutually agreed budgeted levels.

Agreement to be recorded as an addendum to the Shareholder Agreement.

Effective dates: TBA (suggestions either 16 January with adjustment to recorded drawings since that date or 1 April for the start of the new financial year).

[19] Some further emails were then sent between Mr Blaxall and Mr Bendall on 27 March 2014 to see if there could be some agreement. Mr Bendall encourages discussion by Mr Blaxall with Mr Cheng in one email. He suggests a net profit basis rather than performance measures mainly because no budget has been prepared. In one email Mr Blaxall refers to Mr Cheng as the employer but Mr Bendall corrects him and states that the company is the employer.

[20] An issue then arose about the hold back of the salary which had been proposed at 15% in Mr Bendall's email of 7 March 2014. Mr Blaxall was not happy with that. By 8 April 2014 Mr Blaxall, as he sets out in an email to Mr Bendall and Mr Cheng, believes an agreement on his salary has been reached. He does make it clear in his email that it is not a level of remuneration that meets his need for tax and retirement but he would be prepared to accept it for a year to see how the company progresses and what if any future dividend would be paid out. Mr Blaxall concluded his email by recording a hope that *as primarily a director and shareholder* they could move forward with a common goal.

[21] Mr Bendall then sent an email dated 11 April 2014 to Mr Blaxall and Mr Cheng in which he referred amongst other matters to Mr Blaxall's salary package being documented in an addendum to the shareholder agreement not in an individual employment contract.

[22] As it transpired the agreement was never documented as an addendum to the shareholders agreement or otherwise. There was some dispute as to a meeting of

directors on or about 12 June 2014 as to what was said. Mr Cheng and Mr Bendall said that the meeting was to discuss overdraft and loans and that Mr Blaxall said he did not need the agreement recorded in writing. Mr Blaxall did though record in handwriting on Mr Bendall's email of 11 April 2014 *This ended up being a verbal agreement in a meeting of directors at Mr Bendalls suggestion at his offices.* Mr Bendall denies that he said that. I find his evidence likely on that point given that he had recorded in his email that he wanted the salary package documented in an addendum to the Shareholder agreement.

[23] Mr Blaxall commenced receiving a salary from April 2014 and PAYE was deducted from his gross earnings. Mr Blaxall said that not a great deal changed on a day to day basis although he did not claim expenses for the car which attracted under the new arrangement fringe benefit tax for private use. His mobile phone account was paid for.

[24] Mr Cheng said that he never regarded Mr Blaxall as an employee. He regarded him as a director and shareholder. I accept from Mr Cheng's business plan for a long term visa application prepared in or about March 2013 that he did not consider there were any *wage earners* in the company.

[25] Mr Cheng said that Mr Blaxall retained the ability to sign cheques until September/October 2014 when there was a change whereby Mr Cheng was also required to sign cheques as co-signatory. Mr Cheng said that the password for the company computer was controlled by Mr Blaxall and he could not see emails sent to customers. I could not be satisfied that this was the situation for the whole time but there were some concerns raised about this in November 2014.

[26] Mr Cheng was required to employ someone to amongst other matters fulfil his visa requirements after January 2014. He did not consider that Mr Blaxall was an employee for that purpose and an employee was employed from about May 2014. An employment agreement was prepared for her. Mr Cheng did instruct Mr Blaxall to employ someone for the role although Mr Blaxall did have input into who would be suitable. Mr Cheng said that he did not have any real appreciation of Mr Blaxall's duties on a day to day basis.

[27] The financial situation of Blaxall Optics deteriorated in early October 2014. There are emails from Mr Blaxall to Mr Cheng from 1 October 2014 advising that the

company was over its overdraft limit and cheques were returned dishonoured from the bank. There was no money for salaries and Mr Blaxall noted in an email dated 14 October 2014 that a serious situation had been reached for all directors.

[28] Mr Cheng consulted a lawyer, Ken Jones who wrote to Mr Blaxall on 23 October 2014 advising that from his instructions the company was insolvent with outstanding debts, including to the company's major supplier. Mr Jones stated that the company cannot continue to trade without introduction of capital of \$30,000 from the shareholders. He advised that Mr Cheng was able to make a 60% contribution and the other shareholders will need to contribute 40%. Mr Blaxall disputed the insolvency of the company.

[29] There was a meeting in late October with Mr Blaxall and his parents and Mr Cheng and Mr Hanna at Mr Jones' office. There was discussion that the company was insolvent and could not make payments. The evidence supports presentation of an asset and liabilities schedule at the meeting. No agreement was reached to inject further funds into the company.

[30] There was some evidence that Mr Blaxall was regarded in late November 2014, at least by Mr Cheng, as having effective control of the business and that he had changed the password to the company computer – see letter from Ken Jones to Mr Blaxall's lawyer Greg Hair dated 25 November 2014. It was clear there was not to be any further injection of money into the business and there was a proposal that the company be put into voluntary liquidation. Mr Blaxall was removed as a director at a shareholders meeting on 19 December 2014 although is still a shareholder.

[31] Mr Blaxall retained possession of the company vehicle after he was removed as director although there was a request for it to be returned by 7 April 2015 and the minutes of a special meeting of Blaxall Optics regarding removal of a director record Mr Cheng requested that additional company property such as passwords and files be returned to him but Mr Blaxall refused to do so.

Determination

[32] The Authority has exclusive jurisdiction under s.161 of the Employment Relations Act 2000 (the Act) to make determinations about employment relationship problems generally. This includes, under s.161(c) of the Act, matters about whether a

person is an employee. If the relationship is not one of employment then the Authority has no jurisdiction to determine the matter.

[33] Section 6 (1) (a) of the Act provides the meaning of employee as any person of any age employed by an employer to do any work for hire or reward under a contract of service. Section 6 (2) provides that in determining whether a person is employed the Authority must consider all relevant matters including those that indicate the intention of the parties and is not to treat as a determining matter any statement by the persons that describes the nature of their relationship.

[34] Both parties were represented by accountants. I would emphasise that the fact Mr Blaxall was paid as an employee for a period and may therefore be regarded as one from the perspective of the Inland Revenue Department is not a determining matter as to whether he was an employee or not. The Authority must determine the real nature of the relationship under s.6 of the Act.

[35] The intention of the parties is therefore relevant although not decisive and the Authority will apply other tests - control, integration and fundamental to ascertain the real nature of the relationship. The fundamental test is whether the alleged employee performed work as a person in business on their own account.

[36] The Employment Court judgment in *Smith v Practical Plastics Limited*¹ provides a company director is not, as such, an employee of the company but is an office holder upon appointment. It is clear that a director may however enter into a service contract and thereby become an employee and that contract may be express or implied.

[37] In *Lee v Lee's Air Farming Ltd*² which was a decision of the Privy Council it was held that the governing director who held practically all the shares in a private company may still enter into a valid contract of service. The governing director was paid wages which were recorded in a wage book. The articles of association in *Lee* did deal with employment of directors.

[38] In *Smith* Judge Travis referred to a line of English authority which suggests that there is a presumption that there will be a contract of service if a director is

¹ [1998] 1 ERNZ 323 at 340

² [1961] NZLR 325 (PC)

required to work full-time for the company in return for a salary³. There was also reference though to more recent English cases where sufficient control to constitute an employment relationship was lacking and a director has a controlling interest, that director should not be regarded as an employee of the company⁴.

[39] I have also had consideration to a judgment from the United Kingdom Court of Appeal in *Secretary of State for Trade and Industry v Bottrill*⁵ because it provides some guidance in such cases⁶:

“The first question which the Tribunal is likely to wish to consider is whether there is or has been a genuine contract between the company and the shareholder. In this context, how and for what reason the contract came into existence (for example, whether the contract was made at a time when insolvency loomed) and what each party actually did pursuant to the contract are likely to be relevant considerations.

If the Tribunal concludes that the contract is not a sham, it is likely to wish to consider next whether the contract, which may well have been labelled a contract of employment, actually gave rise to an employer/employee relationship. In this context, of the various factors usually regarded as relevant (see for example, Chitty on Contracts 27th ed. (1994) para.37-008), the degree of control exercised by the company over the shareholder employee is always important. That is not the same question as that relating to whether there is a controlling shareholding. The Tribunal may think it appropriate to consider whether there are directors other than or in addition to the shareholder employee and whether the constitution of the company gives that shareholder rights such that he is in reality answerable only to himself and incapable of being dismissed. If he is a director, it may be relevant to consider whether he is able under the Articles of Association to vote on matters in which he is personally interested, such as the termination of his contract of employment. Again, the actual conduct of the parties pursuant to the terms of the contract is likely to be relevant. It is for the tribunal as an industrial jury to take all relevant factors into account in reaching its conclusion, giving such weight to them as it considers appropriate.”

[40] The Employment Court in *Smith*⁷ confirmed that ultimately each case depends on its own facts:

“The result in any particular case will depend on its facts and there will always be points of agreement and disagreement between the various authorities. The issue is whether, viewed as a totality, the evidence establishes the existence of a contract of service, whether express or implied, notwithstanding that the contracting party is a director and/or shareholder of the company.”

³ [1978] ICR 277

⁴ *Buchan v Secretary of State for Employment* [1997] IRLR 80

⁵ EATRF 98/013203

⁶ At [58]

⁷ At pg 341

Determination

[41] Mr Blaxall presents to the Authority what at first glance is a simple claim for 12 weeks' salary for the period from early October 2014 until he was removed as a director. He also seeks reimbursement of expenses and payment of an amount toward tax liabilities for earlier years. The claim though is not straightforward and requires some careful assessment of the relationship between Mr Blaxall and Blaxall Optics. I asked for further information at the time Mr Blaxall was removed as a director. The Authority is required to look at the evidence viewed as a totality to determine the real nature of the relationship and not simply a snapshot of a limited period of time.

[42] I'll turn firstly to the broader claim that Mr Blaxall was always an employee of Blaxall Optics. Mr Blaxall says that he was from after incorporation of Blaxall Optics an employee because he was a working director and shareholder. I will start with looking at the period before January 2014.

[43] There is no evidence of any intention that Mr Blaxall would be an employee of Blaxall Optics after its incorporation or evidence that he was regarded as an employee. I will consider the other tests to establish the real nature of the relationship.

[44] Mr Blaxall was until January 2014 in sole control of the management of Blaxall Optics. He had a majority shareholding and could exercise control over the operation of Blaxall Optics. He was not supervised and did not have his day to day work controlled or restricted like the plaintiff in *Smith*. He agreed in evidence as it was his company he did not have to apply for holiday leave. I find that it is more likely that he could control his working hours and come and go as he pleased. Under the control test there is an absence of the type of control that may be found in a contract of service and this test does not favour a contract of service.

[45] I have then considered whether the work Mr Blaxall did was an integral part of the business. I find that the work Mr Blaxall did was an integral part of the business which is consistent with a contract of service. He took weekly drawings for the same amount. This could be a factor indicating a relationship in the nature of employment. Mr Blaxall also took drawings for other purposes such as moving house expenses and claimed expenses. Mr Blaxall took a loan out for the purpose of introducing funds

into the company. Those matters are not consistent with a contract of service. The factors under this head are fairly evenly weighed.

[46] In terms of the fundamental test I find that Mr Blaxall made financial decisions about the company. He took risks by taking out a loan and injecting funds into the company. He could by his efforts increase the profitability of the business of Blaxall Optics. The factors under this test do not favour a contract of service.

[47] When I consider these factors I do not find that Mr Blaxall was an employee for the first period the Authority is being asked to consider. The Authority does not have the jurisdiction to consider Mr Blaxall's claims relating to tax and production of financial records before January 2014.

[48] After 14 January 2014 Mr Cheng became a majority shareholder and there were then discussions about fixing Mr Blaxall's payments. Subsequent emails on their face in parts disclose some intention to have a relationship in the nature of employment. These emails though arose against the background of concerns from Mr Cheng about excessive drawings and Mr Blaxall about his tax situation. Mr Cheng said that it was not until after he became a majority shareholder that he was able to understand the financial state of Blaxall Optics. The agreement was never reduced to writing as an addendum to the shareholders agreement or as an employment agreement.

[49] Looking as I must at the totality of the evidence the focus at that time was more on changing the method of payment and taxation to Mr Blaxall and that was proposed to be done in a manner which broadly fell within the statutory and taxation framework for an employee. I could not be satisfied that the email exchanges were clear evidence of an intention by both parties to create a relationship in the nature of employment. I place some weight on the final email from Mr Bendall dated 11 April 2014 in which he refers only to the salary package for Mr Blaxall and not any other matters relevant to an employment agreement. I need to consider the other tests to determine the real nature of the relationship at that time.

[50] The evidence did not support any noticeable change in control of Mr Blaxall on a day to day basis after April 2014. There was a change in the method of signing cheques when Mr Cheng asked to be a co-signatory however that appears to be when there were financial issues in September/October 2014. Mr Blaxall was removed as a

director at the special meeting of the company on 19 December 2014. He voted against that. There was nothing in the minutes to the effect that Mr Blaxall was terminated as an employee at that meeting but he did raise issues of payment for the Blaxalls of salaries/wages. He also raised that there were employment agreements in place for the employees although it was not clear if he was referring to himself. The minutes record that Mr Jones noted this matter would be discussed at another time as it was a shareholders meeting.

[51] Mr Cheng I accept had little knowledge of what Mr Blaxall did day to day and there was no evidence that there was any change in control in that regard. Mr Blaxall remained involved in the financial and other aspects of the management of the company. The evidence supports that Mr Blaxall maintained some control inconsistent with an employment relationship over the company car and was permitted to retain that until April 2015. He appears from the special meeting minutes on 19 December 2014 to have retained some control over passwords and files which is less consistent with an employment relationship. I do not find that the factors under the control test favour a contract of service.

[52] Mr Blaxall was integrated into the operation of Blaxall Optics and undertook work. There was a change in the manner in which he was paid. He was paid a salary and PAYE was deducted. There was no evidence of any leave having been recorded although I accept he may have felt that he should advise Mr Cheng if he was to take leave. For most of the period until the financial situation became problematic Mr Blaxall had unrestricted access to the company bank accounts.

[53] I find the various factors weighed under this test fairly evenly balanced more favouring a contract of service.

[54] Under the fundamental test I find that Mr Blaxall continued to make financial decisions about Blaxall Optics including whether or not to inject further funds into the company. He could determine whether or not to take a financial risk in that regard and he along with his parents decided not to in late October when the financial situation was preventing payment of salaries. Mr Blaxall under the changed payment regime did have some opportunity of profiting. He was going to revisit the salary after 12 months to see how the company progressed and whether future dividends would be paid out. He identified in his email of 8 April 2014 what was required to increase sales and the need for Mr Cheng's input on financing new products.

Mr Blaxall could exercise some control over the operation. Assessing the evidence as a whole I find that the factors under this test do not favour a contract of service.

[55] When I look at the totality of evidence in this matter I am not satisfied that the real nature of the relationship with Blaxall Optics was that Mr Balxall was an employee as well as a shareholder and director.

[56] The Authority does not have jurisdiction to deal with his claim.

Costs

[57] I reserve the issue of costs.

Helen Doyle
Member of the Employment Relations Authority