

**IN THE EMPLOYMENT RELATIONS AUTHORITY
WELLINGTON**

[2013] NZERA Wellington 130
5410053

BETWEEN

MARK MAHONEY
Applicant

A N D

AOTEAROA TOURISM
MANAGEMENT LIMITED
Respondent

Member of Authority: G J Wood

Representatives: M Mahoney on his own behalf
T Shreves for Respondent

Investigation Meeting: 1 October 2013 at Taupo

Date of Determination: 18 October 2013

DETERMINATION OF THE AUTHORITY

Employment relationship problem

[1] Mr Mark Mahoney, the former Managing Director and a 25% shareholder in the respondent (Aotearoa Tourism/ATM), claims that he is owed \$21,850 in unpaid wages for work undertaken between May 2006 and May 2012, together with \$14,154.20 in vehicle and other expenses that were part and parcel of that work. He also claims holiday pay of \$1748, salary payments of \$34,000 to 31 August 2013 and a further anticipated loss of salary of \$2000 per month to 30 June 2014, together with compensation for hurt and humiliation, and costs.

[2] Aotearoa Tourism denies all of Mr Mahoney's claims on the basis that he was never an employee, but is rather a former director and still a significant shareholder.

Factual discussion

[3] Mr Mahoney is a professional consulting engineer and experienced businessman, with a strong interest in outdoor recreational pursuits. He has run a

number of businesses, operating as registered companies (some of which he was also an employee in) contemporaneously. As an experienced businessman he decided to go into business with another keen outdoorsman friend of his, Mr Garth Steven. Together they tendered for the management contract of the Whakapapa Holiday Park through the Department of Conservation. They were successful in their tender, which stated that their vehicle, Aotearoa Tourism, later incorporated, was a 50:50 partnership between Messrs Steven and Mahoney. Amongst its proposed staffing strategies it was stated that there would be *employment contract agreements for all staff, including casuals [which] will be fixed term*. The tender document also stated that ATM would *avoid any potential employment relation issues by strict adherence to all employment statutes, and legislative procedures, and by stressing the importance and understanding of individual employment contracts*.

[4] In terms of management structure, the tender documents stated: *Garth's primary role is to manage and operate the site, while Mark's is to manage the contract and provide management resources, services and support where required*. It was clear through the process that Mr Mahoney was the prime person in the company for developing contractual documents.

[5] The contract to run the holiday park was for two years. It was subsequently extended for another three years, with an option for a further three years, bringing the lease to an end in June 2014.

[6] In May 2006 the respondent company Aoteroa Tourism Management Limited was incorporated by Messrs Mahoney and Steven. The shareholding in ATM was held as follows: Mr Steven 50%, Mr Mahoney 25% and Mr Mahoney's then wife (who in actual fact played no role in ATM until after the Mahoney's' separation) 25%. Mr Mahoney was a director until May 2012. Mr Steven was only a director between 22 May 2006 and 23 June 2006 and from 20 December 2011. There were no other directors.

[7] Mr Mahoney, who attended to the legal obligations with the Companies Office, also prepared a proposal for a shareholders' agreement. For whatever reason, the shareholders' agreement was never signed and it was clear from its non-signature that Mr Steven would not and did not accept it in its entirety. Clause 2 sets out the objects of the company. While Mr Mahoney now describes the company as a

management company, the objectives of the company show something different then.

Clause 2.1 states:

The parties agree that the objectives of the company are to manage the contract with DOC in accordance with the provisions set out in clause 6 of this agreement.

Clause 6 dealt with contracts issues and it states:

6.1 Mahoney shall be appointed as the Managing Director and Chairman of Aotearoa Tourism Management Limited for a period of two years from the 1 June 2006 to the 30th June 2008. Duties include the day to day management of the company, contract management and overseeing operations in the Whakapapa Holiday Park. The fees shall be \$40,000 per annum.

6.2 Steven shall be appointed as the Site Operations Manager of the Whakapapa Holiday Park. Steven shall be employed under a standard employment contract (to be appended to this shareholder agreement). Steven will be paid a base salary of \$40,000 per annum + accommodation + power & phone. Duties include managing the Holiday Park, temp and cleaning staff, regular reporting and in general working for the two year contract period from the 30 June 2006 as per the contract agreement with DOC in Schedule 1...

[8] In actual fact the company operated informally. Mr Mahoney relies on an agreement he claims was reached with Mr Steven once the Whakapapa Holiday Park lease had been extended, in October 2007, that he and Mr Steven would be paid \$2000 per month salary for the duration of the contract, in addition to work each of them did for the company. Both were in fact paid this sum each month, commencing in 2009. These payments continued, effectively monthly, for the next three years.

[9] Mr Steven claims these sums were paid as an advance on shareholders' salaries and that it was never intended to constitute an employment relationship, but rather drawings, which are also known as shareholders' salaries. Mr Steven's evidence was supported by ATM's then accountant.

[10] No employment agreements were written up, but then none were for anyone at all in ATM, contrary to the tender document and ATM's legal obligations. No PAYE deductions were made in respect of the \$2000, but were in respect of Mr Steven's \$40,000 salary. No leave records were maintained for Mr Mahoney.

[11] Mr Mahoney had full control of the company's accounts and directly paid the \$2000 to wherever he felt it best at the time, including, on occasion, directly into the

companies he controlled, but did not own fully. I also note that when he paid the sum into his shareholders' account, this was in fact a joint account maintained on behalf of himself and his then wife.

[12] Mr Mahoney was the initial funder of ATM and has provided much of the leadership for ATM, particularly over matters such as contracts, tendering and matters of strategic importance. By contrast, Mr Steven was, as indicated in the tender document, more of a hands-on operator. Mr Mahoney attended ATM meetings when from time to time he went to Whakapapa. He also met with Mr Steven from time to time, as set out in his timesheets. Mr Mahoney had a card describing him as Managing Director of ATM, wore ATM branded gear when at Whakapapa and was an important face of ATM. Mr Mahoney was also given a ski pass paid by ATM for five years, and was listed as a staff member on the holiday park's Facebook page.

[13] Matters between Mr Mahoney and Mr Steven over ATM did not always proceed smoothly, but there were no serious difficulties until after Mr Mahoney separated from his wife in January 2011. In 2012 Mr Mahoney and Mr Steven considered removing all employees from the employment of ATM and replacing staff with contractors, given some employment issues. The proposed restructuring was undertaken by Mr Mahoney and it was agreed that he would be paid for doing so.

[14] Of particular concern was an employment relationship problem formally raised by one staff member. This led to a major falling out between Mr Mahoney and Mr Steven. Following an argument about the running of the park and the restructuring proposal in particular, Mr Mahoney withdrew some funds from the ATM account, believing it was monies owed to him.

[15] Around the same time Mr Steven purchased the shares of Mr Mahoney's ex-wife, which then gave him 75% control of the company. As a result of his concerns about the monies withdrawn by Mr Mahoney, the accounts were frozen. Mr Steven also determined to remove Mr Mahoney as a director of the company he had established, with effect from 3 May 2012.

[16] In response, Mr Mahoney filed timesheets for all the work that he had done for the company since May 2006, for which he did not believe he had been reimbursed. Essentially what he claimed was back pay of \$21,850 for work done at \$20 per hour,

together with expenses of \$14,925.20 for things such as travel, Mr Mahoney being based in Napier.

[17] Both parties appear to have used different language at different times in the on-going disputes between the parties. At one point Mr Steven said that he thought the payments to him of \$2000 were a salary, whereas Mr Mahoney had suggested to the accountant that the amounts above \$40,000 per year were drawings. This is the opposite position to what the two are now arguing. Similarly, after the dispute arose, Mr Mahoney asked for dividend payments, reduced by one-half to \$1000 per month after his wife sold her shares. Mr Steven's response was:

With regard to the "dividends" you claim, ATM has never at any point, distributed funds to shareholders as dividends. Previously you had been paid by ATM for services rendered to ATM as a salary. This is quite different to a dividend. My solicitor wrote you a letter on 25 May where I agreed to pay \$864 for services ... that offer still stands, but you are not entitled to anything more. Those services related to the restructure.

[18] This shows that both Mrs Mahoney and Mr Steven used different terms (with quite different implications for this dispute) either interchangeably and/or in order to gain the maximum advantage from the other. I can therefore gain no benefit from those comments by either party.

The law

[19] A factual analysis based on the relevant provisions of the Act is required to determine whether a person is an employee or a contractor. Section 6, set out below, requires the Authority to consider and determine the real nature of the relationship between the parties. It states:

Meaning of employee

- (1) *In this Act, unless the context otherwise requires **employee** –*
- (a) *means any person of any age employed by an employer to do any work for hire or reward under a contract of service; and*
- ...
- (2) *In deciding for the purpose of subsection (1) (a) whether a person is employed by another person under a contract of service, the Court or the Authority (as the case may be) must determine the real nature of the relationship between them.*

- (3) *For the purposes of subsection (2), the Court or Authority –*
- (a) *must consider all relevant matters including any matters that indicate the intentions of the persons; and*
- (b) *is not to treat as a determining matter any statement by the persons that describe the nature of their relationship: s.6(3)(b).*

In *Tsoupakis v. Fendalton Construction Ltd* (unreported, Colgan CJ, WC 16/09, 18 June 2009) key principles were held to include (at para.5):

- *Section 6 defines an employee as a person employed by an employer to do any work for hire or reward under a contract of service, a definition which reflects the common law.*
- *The authority or the Court, in deciding whether a person is employed under a contract of service, is to determine “the real nature of the relationship between them”:s6(2).*
- *The Authority or the Court must consider “all relevant matters” including any matters that indicate the intention of the persons:s6(3)(a).*
- *The Authority or the Court is not to treat as a determining matter any statement by the persons that describes the nature of their relationship.*
- *“All relevant matters” include the written and oral terms of the contract between the parties, which will usually contain indications of their common intention concerning the status of their relationship.*
- *“All relevant matters” will also include divergences from, or supplementations of, those terms and conditions which are apparent in the way in which the relationship has operated in practice.*
- *“All relevant matters” include features of control and integration and whether the contracted person has been effectively working on his or her own account (the fundamental test).*
- *Until the Authority or the Court examines the terms and conditions of the contract and the way in which it actually operated in practice, it will not usually be possible to examine the relationship in the light of the control, integration and fundamental test.*
- *Industry practice, while not determinative of the question, is nevertheless a relevant factor.*
- *Common intention as to the nature of the relationship, if ascertainable, is a relevant factor.*

- *Taxation arrangements, both generally and in particular, are a relevant consideration but care must be taken to consider whether these may be a consequence of the contractual labelling of a person as an independent contractor.*

[20] It is clear that directors closely associated with a business can still enter into employment agreements on their own behalf, but that does not mean there will always be a contract of service. The United Kingdom Court of Appeal held in *Secretary of State for Trade and Industry v Bottrill* EATRF 98/013203:

... whether or not an employer/employee relationship exists can only be decided by having regard to all the relevant facts. If an individual has the controlling shareholder holding that is certainly a fact which is likely to be significant in all situations and in some cases it may prove to be decisive. However, it is only one of the factors which is relevant and certainly it is not to be determinative without considering all the relevant circumstances.

[21] The Court also held:

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 is 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. It 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.*

[22] In *Smith v Practical Plastics Ltd* [1998] 1 ERNZ 323 it was held at 340:

It is common ground that a company director is not, as such an employee of the company but is an office holder on appointment. It is clear that a director may however enter into a service contract and therefore become an employee, and that contract may be express or implied ...

The leading case is a decision in the Privy Council in Lee v Lee's Air Farming Ltd [1961] NZLR 325 (PC) which allowed an appeal from the New Zealand Court of Appeal. The Privy Council decided that a governing director who held practically all the shares in a private company may still enter into a valid contract of service which would make that person a "worker" in terms of the Workers' Compensation Act 1922. Although the deceased was a governing director, he was performing arduous and skilful duties, flying a topdressing aircraft and was paid wages for doing so which were recorded in a wage book.

The Privy Council held that when discharging the topdressing duties it could not be said that he was discharging his duties as a governing director but as a "worker" for the purposes of the legislation. The Privy Council also observed that the facts of the case lent no support to a contention that if the contract existed, it was a contract for services, holding instead that it was a master and servant relationship. It had been argued that the deceased could not both give orders and obey them and that therefore there was no power of control over him. The Privy Council held (at p 336):

"It is true that an inquiry as to whether a person is or is not employed upon the terms that he will, within the scope of his employment, obey his master's orders may constitute an important inquiry if it is being tested in a particular case whether there is a contract of service as opposed to a contract for services. ... But in the present case their Lordships can find nothing to support the contention that there was or may have been a contract for services but not a contract of service."

...

There is a line of English authority which suggests that there is a presumption that there will be a contract of service if a director is required to work full time for the company in return for a salary, see Trussed Steel Concrete Co. Ltd v Green [1946] Ch115 and Newtherapeutics Ltd v Katz [1991] 2 All ER 151. The position was summarised in Folami v Nigerline (UK) Ltd [1978] ICR 277 by the UK Employment Appeal Tribunal as follows:

*"It seems to us that where it is established that a person has been appointed managing director of a company, that his duties include effective management of the affairs of the company in all its aspects, that he has discharged those duties, and that he has been remunerated by that company in the sense that he has received a salary from the hands of that company, the prima facie conclusion to be drawn is that he is an employee of a company. Whatever may at one time have been thought, it seems now to be established that a director appointed managing director, with duties of this kind, even though he has no separate contract, is in contractual relationship with the company and is, for some purposes at least, to be considered an employee of the company: see *Anderson v James Sutherland (Peterhead) Ltd*, [1941] SC 203, and *Palmer's Company Law*, 22nd ed (1976), vol 1, pp 667-671. ..."*
[p 280]

Mr Hollister-Jones relied on Parsons v Albert J Parsons & Sons Ltd [1979] ICR 271 (CA) where an applicant for compensation for unfair dismissal was one of four directors in a family company who worked full-time for the company. He had been paid by way of director's "fees and emoluments" but there was no provision for his wage or salary in the company's accounts. He had not been treated as an employee for National Insurance purposes, but instead was regarded as "self employed" receiving remuneration by way of director's fees. There was no written contract of service or memorandum setting out its terms, contrary to an express requirement in the UK Companies Act. The English Court of Appeal concluded that the applicant was not employed under a contract of service and therefore was not entitled to claim for unfair dismissal. The learned authors of Palmer's Company Law observed that Parsons involved a family company and in such cases if no express contract of service had been entered into it may be difficult to persuade a Court to deduce from such circumstances that a managing or working director is an employee. They also contrasted the Parsons decision with Folami.

Recent English cases have held that, notwithstanding Lees, 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 company. In Buchan v Secretary of State for Employment [1997] IRLR 80 the Employment Appeal Tribunal held that Lees could not be relied upon in the context of employment protection legislation to support the proposition that a shareholder with full and unrestricted control over all of the operations of a company is nevertheless employed under a contract of service if he works for it full-time. The Employment Protection (Consolidation) Act 1978 ensured that an employee of a company could recover redundancy payments from the redundancy fund if a company had become insolvent. In such a context it is hardly surprising that the Appeal Tribunal held that a managing director who owned 50% of the shares in the company was effectively running his own business enterprise, and was therefore not entitled to the redundancy payment.

The result in any particular case will depend on its facts and there will always be points of agreement or 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 a contracting party is a director and/or shareholder of the company.

[23] In *Practical Plastics* Mr Smith was found to be an employee because this was not a family company, but rather the directors were at arms-length and only had a business relationship. Mr Smith was under the control of another director and exercised little if any control over others in the company. Mr Smith was solely involved with production work in the factory and played no part in sales, marketing or administration and was required to work continuously in full time employment. He had no real involvement in approving accounts or dealing with any other aspect of the management of the company. It was also noted that Practical Plastics treated Mr Smith as an employee in the way that it dismissed him and in its categorisation of him in associated correspondence.

Determination

[24] Upon being removed as a director, Mr Mahoney's involvement with ATM effectively ceased. He has not been paid any money, whether by way of salary, contractual entitlements such as the \$864 referred to above, drawings, director's salary or dividends. It is therefore of little wonder that he wishes to dispute his treatment by Aotearoa Tourism through Mr Steven. However the issue for determination by the Authority is whether he is in the right forum. If the real nature of the relationship that Mr Mahoney had with ATM was not one of employer and employee, then his claims must fail.

[25] Mr Mahoney made it clear that he was relying on an agreement reached at a previous time and that in his view the agreement never changed. It is therefore a matter of ascertaining what the real nature of the relationship was at the time of the agreement, and whether subsequent actions have made any change to that agreement, when determining the real nature of the relationship several years later.

[26] I conclude that the intention of the parties was most likely that Mr Mahoney and ATM did not intend that he be an employee. First, on the balance of probabilities, i.e. what is more likely than not, I conclude that it was Mr Mahoney's intention in setting up the company that he not be an employee. His own draft shareholder's agreement makes the difference between him and Mr Steven very clear in this respect.

[27] I do not accept that the situation changed when he and Mr Steven agreed, when the contract was extended, to claim \$2000 per month each. First, no PAYE was deducted at source for either of them, although it remained so for Mr Steven's \$40,000 salary. ATM's accountant was never instructed to do so by either Mr Mahoney or Mr Steven. The \$2000 per month payments were never treated as a company expense, unlike Mr Steven's \$40,000 salary. Similarly, there were never any PAYE records, and no leave records were kept either. I note also that in accounting circles drawings are sometimes described as a shareholder salary, which is not a salary of an employee, but akin to dividends, which may be taken in advance. Second, the \$2000 per month only makes sense in the context of Mr and Mrs Mahoney being treated equally because they were equal shareholders, which is consistent with the \$2000 going into their joint account. Third, the arrangement as

submitted by Mr Mahoney would also have attracted secondary tax for him, given that he was an employee of at least one other company at the same time. I do not accept that he would have approved of that had he given it any consideration. Fourth, Mr Mahoney made it clear that he paid the sums out of ATM into any account he saw fit. This included the payment of sums, which he now says are salary to him, directly into companies controlled but not owned totally by him. This is quite inconsistent with an employment arrangement, whereby Mr Mahoney personally would have to have been the sole recipient of funds, given that he was the employee. While there may have been a wash-up tax at the end of the year, this course of conduct does tend to show that he did not necessarily treat himself as an employee of Aotearoa Tourism's management. I also find it of some significance that Mr Mahoney did not make a claim, apart from the restructuring work he undertook on behalf of the company, for any unpaid remuneration until after the parties were in significant dispute. Fifth, the tender document enforces the point that ATM was going to have written employment agreements for all staff, and that it recognised the importance thereof.

[28] In terms of the language used by the parties, I conclude that this does not show a clear intention by either party. Both have used terms to suit themselves or out of an understandably imprecise use of language. The best interpretation of the parties' intentions for the \$2000 per month payments is thus of drawings as an advance on profits, also known as a shareholder salary. As noted above, that does not equate to an employee salary. Overall, the intention of the parties is a clear indicator that those were not payments made to Mr Mahoney as an employee, but rather as a director and shareholder.

[29] Traditional tests relating to control and integration do not fit well in the context of a managing director and effective full partner in a company. It can not be said that Mr Mahoney is under the control of the company in any significant way, given that he had total control over the bank accounts, was the driving force behind ATM, in a strategic sense at least, and operated the company as if the joint shareholding with his wife was his alone (although this is not surprising given her lack of involvement in the running of ATM). There are no provisions in the company (which basically had no written constitution, policies, or procedures) that provided for the engagement of directors as employees, or any way of controlling such an

employee. Thus, considered overall, it can not be said that ATM exerted any degree of control over Mr Mahoney.

[30] Similarly, Mr Mahoney was integrated into the business of ATM because he was the driving force behind it. When he was at Whakapapa Holiday Park he was integrated with the company. He was known to be the boss, he wore company branded gear and used ATM business cards. However Mr Mahoney was not regularly at the Whakapapa Holiday Park. Day to day running of the park was Mr Steven's job. Any person coming across Aotearoa Tourism in the ordinary course of events, which would usually be at the holiday park, would not necessarily have any dealings with Mr Mahoney, who was based in Napier. The integration test therefore provides little assistance either way.

[31] Assessing matters under the fundamental test, Mr Mahoney can be seen as conducting business on his own account as a major shareholder in ATM. Mr Mahoney was taking a financial risk in his involvement with the company and stood to make half the profits (in partnership with his wife) by providing effective direction to ATM. His timesheets appear to reflect almost all the time he ever spent on any ATM business after the incorporation of the company, detailing matters such as company set up, contract management, and liaison with DOC. Mr Mahoney therefore appears to be claiming that all his work as a director is effectively also as an employee. I conclude that the more appropriate interpretation of the real nature of the relationship is that Mr Mahoney was in business on his own account as an owner, shareholder and director of the company he co-founded, ATM. While that may also coincide with employment with the same company in some businesses, that has not been established in these circumstances.

[32] There was no evidence of industry practise one way or the other. Indeed, it is clear that small businesses may or may not have director shareholders as employees. That is a matter for the owners of any particular business.

[33] Applying the tests in *Pacific Plastics* (which I hold still provides useful statements of principle despite the law having been amended in 2000), the outcome can be clearly distinguished from the one in that case. This is because, unlike *Practical Plastics*, this was a firm established not wholly at arm's-length, given that the principals were friends. There was nothing in the set up and operation of ATM that allowed for the employment of directors, although Mr Steven was a director

during some periods. Effectively Mr Mahoney held an equal controlling interest with Mr Steven, at least until his separation from his wife. Mr Mahoney was in effective control of the management of ATM and in particular investment and finance. He was under no direct supervision whatsoever. Mr Mahoney, unlike in *Pacific Plastics*, had a major control over the key decisions involving the company, although not its day-to-day operation. He did not work full time in the business, unlike Mr Steven. As noted above, he was remunerated by way of a director's salary and his duties could be characterised throughout as the performance of the duties of a director of a company. Another distinguishing factor from *Pacific Plastics* was that Mr Mahoney was removed as a director and was no longer involved in the running of ATM as a result. He was not dismissed as if he was an employee.

[34] Standing back and looking at the matter overall, I conclude, on the balance of probabilities, that the real nature of the relationship between Mr Mahoney and ATM throughout his association with it was not that of employee and employer.

[35] For all the reasons given above, Mr Mahoney clearly has some genuine concerns with the way in which he was treated by ATM, particularly once Mr Steven became the majority shareholder. These include:

- the failure by ATM to pay him fees for work he did on the restructuring, which ATM has agreed should be paid; and
- ATM's failure to pay him any of the profits of the company since the time he was removed as a director, despite the fact that he is still a 25% shareholder; and
- unresolved issues over the freezing of accounts.

[36] However, because Mr Mahoney was never an employee of Aotearoa Tourism Management Limited, those concerns will need to be addressed in another forum. I therefore dismiss Mr Mahoney's claims before the Authority.

Costs

[37] Costs are reserved.

G J Wood
Member of the Employment Relations Authority