

Attention is drawn to the order prohibiting publication of certain information in this determination

**IN THE EMPLOYMENT RELATIONS AUTHORITY
CHRISTCHURCH**

CA 109/07
5051485

BETWEEN MICHAEL REX McMILLEN
Applicant

AND PILATES PLUS LIMITED
Respondent

Member of Authority: Philip Cheyne

Representatives: Murray Withers, Counsel for Applicant
Scott Wilson and Sarah Townsend, Counsel for Respondent

Investigation Meeting: 10 July 2007 at Christchurch

Determination: 3 September 2007

DETERMINATION OF THE AUTHORITY

Employment relationship problem

[1] Michael McMillen worked for Pilates Personal Fitness Studio Limited as a pilates instructor part-time from February 2004 and then full-time from November 2004. The company operated a business called *Pilates Personal Fitness Studio* based in central Christchurch. That business was sold as a going concern to another company (Pilates Plus Limited) in February 2005. Pilates Plus Limited then employed Mr McMillen on his existing terms and conditions which include a written employment agreement.

[2] Tim Greene and Maria Greene-Smeele are the directors and shareholders of Pilates Plus Limited. On 2 September 2006 they dismissed Mr McMillen because they decided he had breached express and implied terms of his employment agreement not to compete in connection with the operation of a gym business run principally by Mr McMillen's wife. Mattson Arblaster was the principal of Pilates Personal Fitness Studio Limited. He was aware of Mrs McMillen's business and considered that it created no conflict for Mr McMillen's work with Pilates Personal Fitness Studio. Although the subsequent owners of the business became aware of Mr Arblaster's view, they nonetheless dismissed Mr McMillen.

[3] It will be helpful first to mention the relevant express terms of employment. I will then set out how the problem arose before applying the statutory test for justification of a dismissal. Following that it may be necessary to make findings about the relevance of some material which Pilates Plus Limited says has emerged after the dismissal. There are also claims by Pilates Plus Limited for damages and penalties against Mr McMillen.

Terms of employment

[4] Clause 15.4 of the employment agreement provides that the employee must not engage in any paid or unpaid employment which might adversely affect the performance of the duties of their position with the employer without the employer's written permission. Clause 15.5 requires the employee to declare any interest in any business which may potentially be in conflict or competition with the employer's business. It also prohibits the employee, during the employment, from investing personal moneys, or obtaining or establishing an interest in any business that may be deemed to be in competition with the employer without the employer's written permission.

How the problem arose

[5] On 24 July 2006 the Christchurch Star published an article and advertisement about Gymworkz Training Studio. The article identified Mrs McMillen, a former European ice skating representative, as the owner. It also referred to her husband by name as a former New Zealand Olympian. Mr Greene learnt of the article through a client.

[6] At the time there had just been some meetings of an unrelated disciplinary nature between Mr Greene and Mr McMillen. Both sides had been consulting solicitors. Mr Greene's solicitor included in a letter dated 11 August 2006, dealing with these matters, an allegation based on the published material that Mr McMillen was *clearly involved in another studio offering training and fitness services along with his wife* Further information was sought from Mr McMillen about his involvement in that business. A meeting was proposed to deal with this and the previous issues, not all of which had been satisfactorily resolved at that stage. In the end none of the previous issues were sustained or progressed.

[7] Through his solicitor, Mr McMillen's initial response was that a meeting was not required. However, the company set a meeting for 21 August 2006. In response, by fax dated 17 August 2006, Mr McMillen denied doing any outside work in breach of his employment agreement. He confirmed that he had on one occasion some time earlier assisted his wife with gym training and generally supported his wife in her business which was not in competition with Pilates Personal Fitness Studio. Mr McMillen maintained that a meeting was not required.

[8] On or about 28 July 2006 Mr Greene instructed a private investigator to conduct some surveillance on Gymworkz Training Studio. In evidence Mr Greene said that he had to take this step because of Mr McMillen's limited response to the concern but that evidence cannot be correct because the private investigator conducted surveillance at Gymworkz on Saturday 29 July 2006, nearly two weeks before the concern was first raised with Mr McMillen. The investigator's written report is dated 18 August 2006. It records details of the investigator's visit to Gymworkz Training Studio. The report says

... [Mrs McMillen] also mentioned that her husband had a background and training experience in speed skating ...

[9] That appears to be the basis for the investigator's conclusion that

It appears that [Mrs McMillen] indicated her husband to be having an active role in Gymworkz Training Studio.

[10] By facsimile dated 23 August 2006, Pilates Plus Limited required Mr McMillen to attend a disciplinary meeting to respond to the allegation that he was in breach of clauses 15.4 and 15.5 of the Employment Agreement by being involved

in another studio potentially, or actually, competing with Pilates Plus studio. A copy of the private investigator's written report was provided.

[11] There was a prompt written response on behalf of Mr McMillen criticising the use of a private investigator and the content of the report. The allegations were again denied. Subsequently a meeting was arranged for 29 August 2006. Mr Greene, Mrs Greene-Smeele, their solicitor, Mr McMillen, his solicitor and the solicitor's colleague were all present.

[12] Mr McMillen explained that Gymworkz employed two staff and conducted cross training. He said he was not involved in the business. Mr McMillen said that the newspaper article had been written by a journalist without incorporating amendments to the proof that had been returned to the journalist. The amendments to the proof clarified that Mr McMillen was not involved in the business. Mr McMillen asserted that core strength was a generic term rather than something associated specifically with pilates. In response to Mr Greene's question, Mr McMillen said he did not consider it necessary to discuss the possible expansion of his wife's business with Mr Greene as the previous owner (Mr Arblaster) had not considered it as a competing business. Mr McMillen confirmed his commitment to Pilates Plus Limited. The meeting ended with a tentative arrangement for a further meeting and with Mr McMillen to seek further information from Mr Arblaster and the exchanges with the journalist.

[13] Pilates Plus Limited approached Mr Arblaster directly, as did Mr McMillen. Mr Arblaster sent an email to both and Mr McMillen forwarded his email on to Pilates Plus Limited. In response to both Mr McMillen and Pilates Plus Limited, Mr Arblaster confirmed that there had been discussions with Mr McMillen during the earlier employment about Mrs McMillen's intention to set up a home-based gym. He said that he did not regard this business as competing with the Pilates Personal Fitness Studio because the services and market scope and location were completely different. To Pilates Plus Limited, responding to a question asked by Mr Greene, Mr Arblaster explained that he did not refer to this matter at the time of the sale and purchase of Pilates Personal Fitness Studio because it had been appropriately dealt with some time before then.

[14] Mr McMillen provided Pilates Plus Limited with the exchanges with the journalist about the article. That shows that Mrs McMillen sought an amendment

clarifying that she had devised the group training system being offered at Gymworkz. The journalist's email with the proof, however, was addressed to both Mr and Mrs McMillen.

[15] A further meeting was arranged for 31 August 2006. Before then Pilates Plus Limited's solicitor sent some further material to Mr McMillen's solicitor. That correspondence noted Mr McMillen's assertion during the first meeting that he was not involved in any way with the operation of Mrs McMillen's business. However, Pilates Plus Limited had discovered a file on its computer system and diary notes that indicated that the assertion *appears to be inaccurate*. These materials were provided to Mr McMillen. The diary notes are dated from June 2006. They record phone messages for Mr McMillen from a supplier of fitness equipment about the supply of fitness balls, presumably for Gymworkz. The computer file was a letter from Mr McMillen to the Christchurch City Council concerning planning and consent issues arising from a proposal to purchase a property for Gymworkz. The text of the letter in several places suggests that Gymworkz was a joint venture of some sort between Mr and Mrs McMillen.

[16] At the meeting on 31 August 2006, Mr McMillen again denied any involvement in Gymworkz and asserted that it was not a competitor of Pilates Personal Fitness Studio. Mr McMillen also provided a letter from the fitness equipment supplier confirming that Gymworkz was one of its clients and that the business dealt with Mrs McMillen not Mr McMillen. The meeting ended with Pilates Plus Limited to consider its decision.

[17] A further meeting was arranged for 2 September 2006. At that meeting Mr Greene told Mr McMillen that they believed, contrary to the denials, that Mr McMillen was involved in Mrs McMillen's business; that the Christchurch City Council letter, comments and messages confirmed this; that Mrs McMillen's business had changed since initially assessed by Mr Arblaster and was now in competition with Pilates Plus Limited; that Mr McMillen was in breach of clauses 15.4 and 15.5 of the Employment Agreement and his duty of fidelity; and that they had therefore decided to dismiss Mr McMillen. Arrangements were then made for final pay and the return of property.

Justification for dismissal

[18] Justification must be determined, on an objective basis, by considering whether the employer's actions, and how the employer acted, were what a fair and reasonable employer would have done in all the circumstances at the time of the dismissal.

[19] Pilates Plus Limited concluded that Mr McMillen was involved in some way in Gymworkz. It took from the messages left for Mr McMillen to pass on to his wife that he was actively involved in the day-to-day operation of Gymworkz. It also took from the published article, notwithstanding the intended corrections, and the Christchurch City Council letter, that Mr McMillen was involved in the business. Pilates Plus Limited then concluded that Mr McMillen's involvement in his wife's business placed him in breach of the express duties referred to above and the implied duty of fidelity.

[20] From the perspective of a disinterested observer, what would an employer acting fairly have concluded on the available evidence as to Mr McMillen's involvement in the business? First, the report of the private investigator offered no support for the conclusion that Mr McMillen was involved in Gymworkz except for the reference by Mrs McMillen to her husband's background as a speed skater. Secondly, there is the Christchurch Star article. As published, that indicated that Mrs McMillen owned the business but that both she and Mr McMillen had devised the *group training system* available at Gymworkz. The intended amendments stated that Mrs McMillen devised the *group training system* based on her and her husband's experience as successful athletes. However, a reasonable inference that Mr McMillen had had some contact with the journalist about the article arose from the journalist's email which started *Hi, Manuela and Mike*. The messages left for Mr McMillen at his workplace in June 2006 indicated some involvement with seeking and passing on to Mrs McMillen information about equipment and advertising for Gymworkz. The Christchurch City Council letter also indicated Mr McMillen's involvement in Gymworkz at least in the proposal in January 2006 to purchase a residential property with facilities capable of conversion into a home-based gym. The information from Mr Arblaster also indicated that Mr McMillen had some role in the establishment of Gymworkz.

[21] At the beginning of the disciplinary process Mr McMillen stated that he had assisted his wife's business about a year earlier by running one non-pilates training session, that he supported her business endeavours but did not work at Gymworkz. There is nothing in the information that was available at the time of the dismissal to cast any doubt in the mind of any reasonable employer on the truth of Mr McMillen's statement. That put Mr McMillen's support for his wife's business within what would have been acceptable to Pilates Personal Fitness Studio Limited and Mr Arblaster. However, Pilates Plus Limited concluded that, with Gymworkz's expansion and growth, it was competing. The latter conclusion was based on the material referred to above.

[22] Mr Greene's evidence is that he was particularly concerned with the reference to *core strength* exercise and the *no membership fee* slogan. Mr Greene says that the former is the cornerstone of pilates taught at his business, while the latter is offered by his business and is unusual in the fitness industry. Mr McMillen's evidence is that *core strength* is a generic term and that charging no membership fee is not uncommon in the fitness industry generally.

[23] In his email, Mr Arblaster identified the factors leading him to conclude that Gymworkz was not a competitor. He understood the idea to be a drop-in exercise place aimed at residents within the local suburb who did not wish to travel a long distance to a gym. Gymworkz offered standard exercise equipment and aerobics classes and did not include pilates. It did not offer the unique selling features of a clinical pilates studio. He considered that there was no risk of *client transfer* because of the completely different price, purpose and demographic. The only evidence after Pilates Plus Limited's disciplinary investigation indicating a change to these business differences was the relocation from Mr and Mrs McMillen's home in Burwood to a nearby commercial building in Marshlands Road. From this, no reasonable employer would have concluded that Mrs McMillen's business had changed its character from that assessed by Mr Arblaster.

[24] I turn now to consideration of the express terms of the Employment Agreement. The only terms mentioned during the investigation were clauses 15.4 and 15.5.

[25] Clause 15.4 is about personal activities impeding the employee's work performance. Before the present issue arose, Mr Greene had been corresponding with

Mr McMillen about him not working on Saturdays. When the present issue was first raised with Mr McMillen, there was a suggestion that he had not been working on Saturdays because of some involvement in Gymworkz. However, there is no evidence to sustain that view. At some point, Mr Greene thought that Mr McMillen habitually worked elsewhere on Saturdays as a security guard, but the evidence establishes that Mr Greene was wrong about that too. There was no other information available from the disciplinary investigation to indicate that there was any risk that Mr McMillen's limited involvement in his wife's business would adversely affect the performance of his duties for Pilates Plus Limited. Accordingly, I find that no reasonable employer would, on the available evidence, have formed the view that Mr McMillen's involvement in his wife's business adversely affected his work for Pilates Plus Limited.

[26] Turning to clause 15.5, Mr McMillen complied by declaring his interest in Gymworkz to Mr Arblaster at the point that there was a potential for it to conflict with or be in competition with Pilates Personal Fitness Studio. Mr Arblaster confirmed this to Pilates Plus Limited. I have already found that no reasonable employer acting fairly would have concluded, on the information available, that there had been any change in Gymworkz to bring it into competition with Pilates Personal Fitness Studio. It follows that Mr McMillen did nothing to breach this express term of the employment agreement.

[27] In *Tisco v. Communication and Energy Workers' Union* [1993] 2 ERNZ 779 the Court of Appeal held that conduct by an employee which is likely to damage the employer's business or undermine significantly the trust which the employer is entitled to place in the employee could constitute a breach of an implied duty. Part of the duty of fidelity is an obligation not to undermine the relationship of trust and confidence. Pilates Plus Limited partly relied on breach of the implied duty of fidelity when it dismissed Mr McMillen.

[28] It is useful to compare the present matter with the facts of *Tisco*. In *Tisco*, the employee worked as an electronics technician. In his own time, he obtained old television sets and video equipment, repaired or refurbished then sold them by auction for profit. Evidence indicated damage or potential damage to the employer or undermining of confidence. He used a staff buying concession to source components for this commercial work, but the concession was intended only for personal use.

There was a risk that Tisco customers might sell the faulty equipment to the employee instead of getting Tisco to repair it. There was also evidence that retailers who contracted repair work to Tisco considered the employee a competitor, causing a souring in the relationship between the retailers and Tisco. In the present matter, Mr McMillen had a limited involvement in his wife's business having declared that to his previous employer. The subsequent employer's investigation uncovered no information suggesting any abuse of his position to the advantage of Gymworkz by Mr McMillen. There was no evidence of any risk to Pilates Plus Limited's business. In short, there was no basis on which any reasonable employer would have concluded that Mr McMillen had breached the duty of fidelity.

[29] It follows from the foregoing findings that Mr McMillen did not breach the express or implied terms of his employment agreement and that there was no basis for his dismissal. He has a personal grievance.

Post dismissal discoveries

[30] There are a number of items which Pilates Plus Limited says it has discovered on its computer system only after the dismissal. Those items are said to be further evidence of Mr McMillen's breaches of duty.

[31] There is a document headed *Gymworkz Backyard Gym!*. The metafile information indicates that the document was created and last saved on 15 September 2005 but last printed on 8 February 2005. The document is a flyer intended to publicise Gymworkz and includes reference to pilates sessions. It lists *Mike or Manuela McMillen* as contacts. There is also a second iteration of this document. Mr McMillen's evidence is that the flyers were created by Pilates Personal Fitness Studio's receptionist before the business was purchased by Pilates Plus Limited. Mr McMillen says that he had Mr Arblaster's permission to use the printer at work as their home printer did not work. He also says that the flyers were never distributed and that Mr Arblaster pointed out that pilates could not be offered. There is no reason to doubt Mr McMillen's evidence. It follows that these documents, apparently discovered in early September 2006 after the dismissal, do no more than confirm Mr McMillen's approved limited involvement in his wife's business.

[32] There is an email and document referred to as *Mike's financials* sent from Mr and Mrs McMillen's home email address to Pilates Personal Fitness Studio on

2 November 2005. The document contains financial and business information in connection with the proposed purchase of a Prestons Road property, the subject of the Christchurch City Council letter mentioned earlier. The document includes a number of questions about business structure and the like. The text indicates Mr McMillen's involvement in the business as discussed above, so takes the matter no further. I should note that Mr McMillen's personal use of Pilates Personal Fitness Studio's computer and printer pre-dated a directive issued by Mr Greene in February 2006 banning such personal use. There are several other documents, apparently found after the dismissal, that relate to Gymworkz. These also confirm Mr McMillen's involvement as above and were printed before the directive.

[33] In essence, Mr Greene believes, and sought to persuade the Authority, that Mr McMillen had been actively involved training clients in pilates at Gymworkz. However, there is no cogent evidence for this belief.

[34] None of the material apparently found after the dismissal (or the earlier material) amounts to blameworthy conduct on Mr McMillen's part contributing to the circumstances giving rise to the grievance.

Remedies

[35] The statement of problem refers to a claim of \$15,000 compensation for distress. However, in his evidence, Mr McMillen seeks \$5,000 to compensate him for the distress arising from the unjustified dismissal. The latter figure is a reasonable claim in the circumstances of this problem. I order Pilates Plus Limited to pay Mr McMillen \$5,000 compensation for distress.

[36] There is a claim for six months lost remuneration. Once dismissed, Mr McMillen set about establishing himself in business as a pilates instructor. The employment agreement did not include any post termination restraint of trade provision. A number of Pilates Plus Limited's clients sought him out and have become clients of Mr McMillen's pilates business. Mr McMillen estimates that earnings from his business still do not exceed the level of the salary while working for Pilates Plus Limited. However, no details have been provided.

[37] There is no evidence that Mr McMillen took any steps to mitigate his loss of income following the dismissal except for the establishment of his own business venture. In the circumstances, I find that Mr McMillen's losses are attributable to the

establishment of the business rather than the dismissal. I note also that the Authority is obliged to assess remedies in a manner that is fair to both parties. Given that many of Mr McMillen's clients appear to have been clients of Pilates Plus Limited, there would be a measure of injustice in further requiring Pilates Plus Limited to subsidise the establishment of this business by an award of compensation for lost remuneration. Accordingly, there will be no order.

Counterclaim

[38] Pilates Plus Limited's amended statement in reply sought an account of profits or damages against Mr McMillen for an alleged breach of duty relating to his involvement with Gymworkz and soliciting Pilates Plus Limited's clients for Gymworkz. However, in closing, counsel acknowledged that there was no evidence of loss to support these claims. Nothing more needs to be said about them.

[39] There is a further claim for a penalty for an alleged breach of agreement and a breach of good faith. The latter claim cannot succeed because there was no attempt to relate the facts to s.4A of the Employment Relations Act 2000, the only basis on which a penalty for breach of good faith may be imposed: see s.133(1)(b) of the Employment Relations Act 2000.

[40] The former claim is based on evidence from Raewyn Idoine, a client of Pilates Plus Limited. I accept the evidence that Ms Idoine told Mr Arblaster of the following matters only after Mr McMillen's dismissal. Ms Idoine trained under Mr McMillen at Pilates Personal Fitness Studio. Her evidence is to the effect that Mr McMillen spoke to her over the period of several weeks about financial issues associated with the intended purchase of a property for Gymworkz, causing her to think he was angling to borrow money from her for that purpose. Mr McMillen does not deny discussing matters with Ms Idoine but does deny that he was trying to solicit a loan. I see no reason to disbelieve Mr McMillen's evidence on that point.

[41] Ms Idoine also says that Mr McMillen spoke to her about doing some aerobic fitness sessions at Gymworkz. Mr McMillen did not deny this and I accept Ms Idoine's evidence on the point. Pilates Personal Fitness Studio did not offer aerobics fitness training.

[42] The final aspect of Ms Idoine's evidence is that Mr McMillen spoke to her about doing pilates sessions with him at Gymworkz or getting a group together for

him to do pilates training for the group at Ms Idoine's house, this being cheaper than training at Pilates Personal Fitness Studio. Mr McMillen acknowledged the discussion about group training and his evidence is that this was a service being offered on behalf of Pilates Plus Limited. There is evidence that Pilates Plus Limited offers this facility to other clients as well. Mr McMillen's evidence is to the effect that Ms Idoine must have been mistaken to think he was offering her Pilates instruction at Gymworkz or on his account, evidence which I accept.

[43] In his oral evidence, Mr McMillen referred to several matters personal to Ms Idoine that are not relevant for current purposes and which have not been mentioned here. To protect Ms Idoine's privacy, I make an order prohibiting publication of Mr McMillen's evidence about Ms Idoine except as outlined in this determination.

[44] It follows from the above findings that there was no breach of the employment agreement by Mr McMillen arising from his dealings with Ms Idoine. Accordingly, Pilates Plus Limited's counterclaims are dismissed.

Summary

[45] Pilates Plus Limited unjustifiably dismissed Mr McMillen. Pilates Plus Limited is to pay Mr McMillen \$5,000.00 compensation pursuant to section 123 (1) (c) (i) of the Employment Relations Act 2000.

[46] The claims by Pilates Plus Limited against Mr McMillen are dismissed.

[47] Costs are reserved.

Philip Cheyne
Member of the Employment Relations Authority