



EMPLOYMENT RELATIONSHIP PROBLEMS: COSTS, BENEFITS AND CHOICES

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EXECUTIVE SUMMARY

This report presents key findings from recent Department of Labour research on employment relationship problems (ERPs), and the processes for resolving them. The research included surveys of the public and private sectors, and qualitative case studies of individual ERPs.

Incidence

- The incidence of employment problems is low. The survey found that in the past year, businesses experienced 1.5 ERPs per 100 employees. The incidence rate of ERPs for the public sector organisations responding to the survey was 0.8 ERPs per 100 employees.
- Despite claims of rising numbers of ERPs, the research uncovered no evidence that the incidence of ERPs is increasing over time and some evidence of decreasing levels. However, given the snapshot nature of this research and the shortage of comparable previous research, this conclusion must be tentative.

Costs and Benefits

- The median direct cost of all ERPs in the survey of private sector employers, including those proceeding to litigation, was about \$5000, of which \$2800 represented payouts to employees. The remainder included legal representation/advice, investigation costs and any replacement staff used to cover for participants in the ERP.
- The total direct costs for all employers (that is multiplying the average costs found in the survey by the number of ERPs estimated for the whole economy) would be around \$146 million for the 12 month period. This amounts to around 0.4% of private sector wages and salaries for the year.¹ Adding in lost management and staff time and productivity during the course of the ERP would increase the total cost to employers of ERPs to \$214 million (0.6% of private sector wages and salaries for the year).
- There was no evidence that the presence of no win no fee advocates has greatly changed the environment for ERPs other than by allowing some lower income employees to access personal grievance procedures.
- The lowest costs of ERPs arose where resolution took place entirely in-house with neither the employer nor the employees having representation. This was also the process most favoured by employers for resolving future problems and which produced the highest level of satisfaction for employers. Unsurprisingly, costs increased if problems progressed through the hierarchy of problems resolution methods (mediation, Employment Relations Authority, Employment Court).

Effective Problem Resolution

The most effective employers (those who had few employment relationship problems and dealt with them in cost effective ways) involved in this study shared several features:

¹ Based on Statistics New Zealand Quarterly Employment Survey data.

- They set up policies and procedures to deal with the most common or damaging employment issues ahead of time. They made clear to their employees what the boundaries of acceptable conduct were.
- They sought to address potential issues before they led to major conflict.
- They focussed on the major issues of concern and maintained good faith relationships.
- They knew about the full range of resolution methods available and could choose among them according to circumstances.

Future Research

The research leading up to this report has focused on the economic costs to employers and the social costs to employees as these have been the main areas of concern for the respective groups. Given time and a sufficient budget, DOL could usefully:

- survey employees to develop a fuller understanding of the economic costs they face;
- carry out more intensive research into the qualitative impacts of ERPs on employers and other staff;
- investigate the differences in experiences for small businesses in more detail, including why ERPs may arise earlier for small employers; and
- repeat this research at three year intervals to understand the changing patterns of ERPs and resolution methods over time.

INTRODUCTION

The Employment Relations Act was introduced in 2000 to provide the framework for regulating relationships between employers and employees. The Act recognises “that employment relationships must be built on good faith behaviour” (Section 3(a)(i)) and the “inherent inequality of bargaining power in employment relationships” (Section 3(a)(ii)).

This report examines some of the prevalent beliefs about the operation of these provisions of the Act, and determines the extent to which these beliefs are supported by the research evidence. It also provides information about how employment relationship problems develop, and the costs and benefits of employment relationship problems (ERPs). Finally, it gathers lessons from those case study employers who appeared most successful in minimising the costs and maximising the benefits of ERPs.

The Department of Labour has conducted research into the operation of the personal grievance provisions of the Act, including a long term and short term series of projects.

Long term research programme

- a survey of businesses, with 852 respondents, of which 130 had experienced disputes during the previous 12 months;
- a survey of public sector organisations, with 130 respondents of which 40 had experienced disputes during the previous 12 months;
- case studies of 15 disputes;

Short term research programme (previously reported)

- a survey of mediations carried out over a one month period,
- a review of Employment Relations Authority determinations over the same period; and
- a series of focus groups.

Results from the long term research programme provided the main source for the findings presented in this report, with additional information from the short term research programme used where pertinent.

Appendix I provides more information about the research methodology.

QUESTIONS ABOUT EMPLOYMENT RELATIONSHIP PROBLEMS UNDER THE EMPLOYMENT RELATIONS ACT

Employers, in particular, have raised a range of concerns about how the personal grievance provisions in the ERA operate. These concerns have been amplified by media reports that have focused on cases which have been particularly expensive for employers. This section discusses some of the key questions and concerns about the ERP and personal grievance provisions of the Act:

1. Do employment relationship problems present high costs for employers?
2. Is the incidence of employment relationship problems growing?
3. Is there a "grievance gravy train" led by a proliferation of no win no fee advocates?
4. What is the impact of stand-down requirements for Work and Income benefits on personal grievance claims?
5. Are there systematic biases in the employment relationship problem resolution system favouring employees/employers?
6. Do small businesses have a harder time dealing with employment relationship problems?

The research sheds light on the extent to which evidence supports these perceptions. In any case, perceptions can influence employer and employee behaviour and form part of the environment for ERPs, and thus need to be considered in policy deliberations.

Do employment relationship problems present high costs for employers?

Both focus groups carried out in the last half of 2006 and case study research carried out in 2007 indicated that there is a prevailing belief that employment issues that lead to personal grievance claims are expensive to settle. One estimate mentioned by some respondents was \$40,000 (including legal costs and settlement values) although the focus groups suggested that the amounts of payouts were expected to be closer to \$5000. Any perception of high costs from ERPs that are not settled internally is a powerful incentive for employers to either avoid addressing issues or seek quick resolution outside the frameworks provided by the Department of Labour.

The survey of private sector employers found that the median direct cost of all ERPs, including those proceeding to litigation, was about \$5000, of which \$2800 represented payouts to employees. The remainder included legal representation/advice, investigation costs and any replacement staff used to cover for participants in the ERP. The mean cost was \$10,850. The median cost is a measure of central values², and presents the best measure of "typical" values as the means were inflated by a small number of very high values.

Regardless of the actual cost, perceptions of high cost can have an impact on employer responses to performance or conduct issues among their employees. One of the case study employers provided three warnings over a period of several

² The median is the value where half of all values are above and half below.

months to an employee who had consumed alcohol on the premises and reported for work when impaired by drugs. The employer took this approach so that he could not be accused of unjustified dismissal. He estimated that the presence of this employee and his effect on workplace morale cost around \$10,000 per month in lost productivity – a cost which could have been forgone with a speedier resolution.

This belief that high payouts are likely may also influence the behaviour of some employees, leading them to hold out for unrealistic settlement amounts and unnecessarily protracting employment relationship problems. One advantage of mediation (where most settlements were below \$5000 and many below \$2000) may be the ability of mediators to inject a degree of realism into claims.

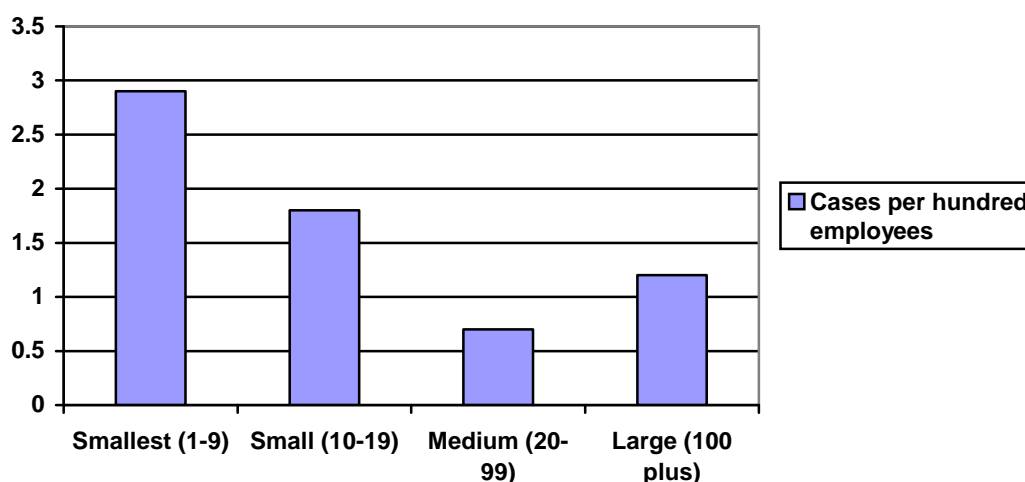
I think it can actually in some ways have a positive effect, because I think they can bring a reality check to the person... you hear people say "I'm gonna take them for thousands... but all of a sudden they do get into a mediation and they get into the reality check ... , what the average settlements are and what their chances are likely to be. (HR Manager)

More information on the costs and benefits of ERPs, and how these vary according to resolution methods is contained in sections 3 and 5.

Is the incidence of employment relationship problems growing?

The private sector survey found that for every hundred employees, businesses experienced 1.5 cases per year of ERPs sufficiently significant to come to the attention of business owners, senior management or HR departments (where these existed). The rate for small employers (1-9 employees) was 2.9 cases per 100 employees, while the rate for large employers (100+ employees) was 1.2 cases per 100 employees.

Figure 1: Incidence of Employment Relationship Problems



A 2000 survey of employers reported that 19% of employers (weighted by size) had experienced a "grievance dispute" during the previous 12 months. This is a slightly more restrictive definition than used in this survey of ERPs and compares

with 9% for this survey. A survey of employees in 2002 found that about 9 percent of employees had experienced “disputes” (using a slightly wider definition³) over the previous twelve months.

Given the different methods and definitions, the numbers are not strictly comparable, but do not suggest any increase in numbers of ERPs. If anything, they suggest a reduction.

Another method of gauging incidence of ERPs is through analysis of numbers of applications for mediation or for registration of dispute resolutions with the mediation service.

The Department of Labour publishes the number of applications for mediation in its annual report. With the exception of a slightly lower figure in 2001/2002 and higher figure in 2004/2005, this number has consistently been around 9200, with no evidence of a changing trend. This level is in line with the estimated rate of ERPs from the survey and the proportion of ERPs proceeding to mediation.

Is there a “grievance gravy train” led by a proliferation of no win no fee advocates?

In 2006 the Employers and Manufacturers Association (Northern) noted an increase in the number of employment issues going to the Employment Relations Authority and suggested that there was a “grievance gravy train”. They suggested that, encouraged by no win no fee advocates, “employees are trying their luck to see if their employer can be tripped up” over dismissals that were justified in substance, but flawed in process. There were even suggestions that some employees may be provoking confrontations in the hope of winning a financial settlement through such advocates.

Private sector employers surveyed stated that no win no fee representatives were involved in 16% of ERPs.⁴ There was no evidence that no win no fee advocates have dramatically changed the landscape or encourage meritless claims. One of the employers interviewed said that advocates were unlikely to put much effort into claims that lacked merit. Other parties interviewed in the case studies believed that no win no fee advocates played an important role in providing access to advice for low income employees. In any case, Department of Labour estimates suggest there are only a small number of no win no fee advocates in the market.

³ The 2002 definition included all disputes which involved a third person other than the employee and their immediate supervisor. Any ERPs settled with the involvement of a representative (such as a union rep) but not reaching the attention of the owner, HR or senior managers would be included in the 2002 sample but not the current study. Any ERPs included in the wider definition would be unlikely to present high direct costs, as high cost disputes would likely need involvement of more senior staff.

⁴ Some caution is needed in interpreting this figure as employers may make incorrect assumptions about how employee advocates are compensated (e.g. in one case study the employer reported the involvement of a “no win no fee” advocate, which the employee reported had been paid on a simple fee basis).

The one noticeable effect of no win no fee advocates on outcomes was to delay resolution somewhat compared to other ERPs involving third parties. ERPs where agents working on a no win no fee basis were involved took up to twice as long as those involving lawyers, but resulted in total cost levels comparable to those for other employee advocates (and lower than those where lawyers were involved).

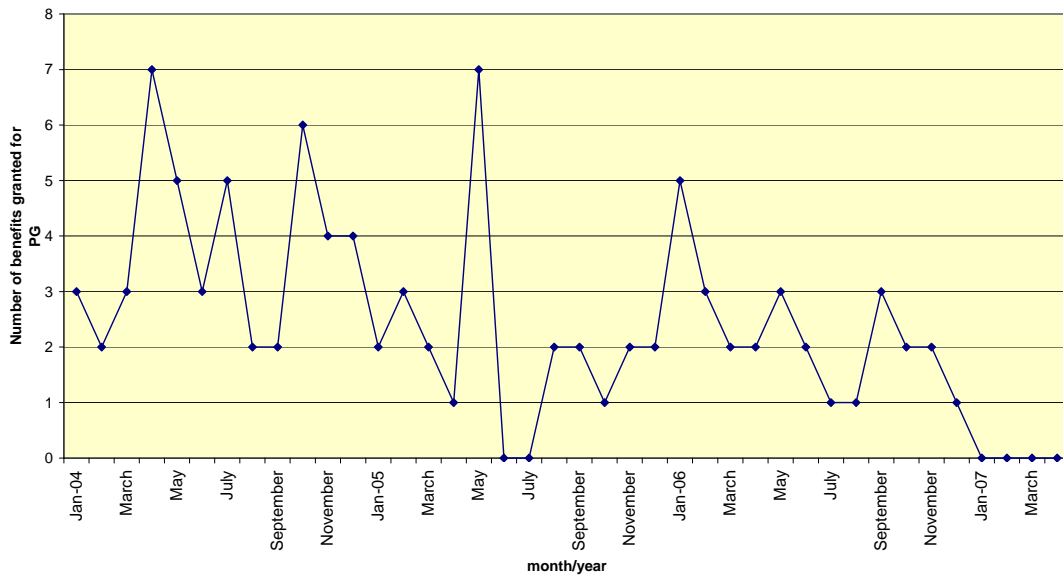
There was one case in the case studies suggesting that the employee may have attempted to manipulate the system. This employee did not use a no win no fee advocate. However, in almost all of the cases studied, ERPs were distressing for all parties. The level of distress reported by employees suggests that such attempts to manipulate are likely to be only a small minority of ERPs.

What is the impact of stand-down requirements for Work and Income benefits on personal grievance claims?

Some employers suggested that a proportion of personal grievances are taken mainly to receive income support. The Ministry of Social Development imposes stand down periods before people can claim unemployment benefits. If an employee is dismissed with cause or resigns voluntarily a 13 week stand down period applies before they become eligible for the unemployment benefit. However, if the employee challenges a dismissal or loss of employment by taking a personal grievance, this 13 week stand down period does not apply (though other stand down periods may apply depending on the employee's other personal circumstances). This provision was considered to provide an incentive for dismissed employees to take a personal grievance.

Ministry of Social Development figures show that the number of benefits granted under this provision have rarely exceeded 5 per month over the last three years with none at all being granted between January and April 2007. Since 2004, both the total number of benefits granted and the proportion of all benefits granted under this provision have exhibited a downward trend. This is illustrated in the graph below.

Figure 2: Unemployment Benefit Grant for Personal Grievance (total number/month)



The perception that unemployment benefit rules are a major contributor would, therefore, appear to be unfounded at present.

Are there systematic biases in the employment relationship problem resolution system favouring employees/employers?

The case studies and focus group research suggest that both employers and employees tend to focus on the obstacles they experience or expect in achieving their goals during ERP resolutions. Many employers feared that a judgement of inadequate processes would expose them to large liabilities. On the other hand employees saw the (presumed) greater experience and resources and inherent positional advantages of employers as tilting the balance the other way. Hence each believed that the system favoured the other party.

That's my really, really big concern about the employment contracts [sic]. I understand it's covering both parties, but I really feel that it's gone overboard the other way. It just makes it so hard for us... They know that ... they can go so far. They work the system to their advantage all the time. (Employer)

I think that the process as it stands at the moment is quite unfair on employees and that the employer has all of the cards in their favour... So, if they see somebody they perceive to be a problem employee, there's no problem to them just using inappropriate practices to bully a person out or get rid of them. (Employee)

Data from the case studies shows that ERPs were traumatic for both employers/managers and employees, which suggests that most employees would be unlikely to take grievances unless they felt it really necessary.

The mediation survey and study of Authority determinations indicated that employees initiate most of the formal procedures. This arises from the fact that it

is normally the employee who wants a change to the existing situation. Only if they or their representatives believe that they have a good chance of winning are they likely to advance to Employment Relations Authority. For this reason, the finding from the review of Authority determinations that more than half of all substantive Authority hearings find at least partially in favour of employees does not indicate that the Authority proceedings are unreasonably slanted.

Employers often assert that process is more important than substance. However, in hearings on employment disputes, matters of substance and process are not always easy (or appropriate) to disentangle. For example, if an employee “wins” because the Authority finds that the employer failed to investigate alleged misconduct, the employer is likely to see this as “process trumping substance” while the employee may believe that their claim on the substance would have prevailed had an investigation taken place.

Although the Act does not explicitly distinguish between substantive and procedural unfairness, the Authority can and does modify awards according to its assessment of the merits. For example, the review of Authority determinations found two examples where the Authority found that dismissals were unacceptable in process terms, but awarded nothing to the employees because of their contributory behaviour. In around one quarter of all cases analysed the Authority reduced or rejected awards on the basis of contributory conduct.

Do small businesses have a harder time dealing with employment relationship problems?

Small businesses in the survey and case studies appeared to experience ERPs and personal grievance procedures quite differently from the larger employers.

Smaller businesses were less likely than larger businesses to experience a problem (6% of small businesses had experienced a problem during the survey period, as opposed to 53% of large businesses). This is not surprising, given that large businesses employ more staff. However, the incidence rate per 100 employees per year was higher for small businesses (2.9) than for large businesses (1.2), indicating that employees are more likely to experience an ERP if they work for a small business than a large one.

The median direct cost of ERPs for small businesses was between \$3,000 and \$3,900 (depending on the size of the business), compared to \$9,700 for the largest businesses – indicating that small businesses did not face higher absolute costs than their larger counterparts. Even so, costs in the range of \$3000-4000 could still have a large relative impact on a small business.

Small businesses had a markedly more negative view of the impact of ERP provisions than large ones. It is likely that small businesses will generally have fewer HR resources and expertise than larger businesses (who can afford to employ specialists). Small businesses are also unlikely to be experienced in dealing with ERPs as they may have one only every four or five years. As a result, their information about ERPs is more likely to come from media reports, or through business networks, which may amplify “horror stories”. Consequently,

small businesses may expect the costs of resolution to be high and fear that their processes would be found to be inadequate.

Interestingly, businesses employing between 10 and 19 full time equivalents were the least satisfied with resolution processes and outcomes and the most likely to provide negative comments about the Act in the "open" question of the survey. In fact, the profile of ERPs for employers of 10-19FTEs is closer to large businesses than it is to businesses employing 1-9FTEs, but it is likely that the financial and management resources available to large businesses to deal with these problems are not available to them. These (10-19FTEs) businesses therefore may be "squeezed" between much higher incidence of problems and higher cost than smaller businesses and a relative lack of resources to deal with them, which may explain their greater dissatisfaction with current employment problem resolution processes

Another difference between the experience of smaller businesses and larger businesses, which emerged from the mediation survey, was that ERPs emerged earlier in the employment relationship than was the case for larger businesses. We were not able to find the reasons for this difference from this research and this is an issue which could conceivably be addressed in future research.

THE DEVELOPMENT OF AN EMPLOYMENT RELATIONSHIP PROBLEM

In this section we explore the stages through which an employment relationship problem may develop, using a narrative example. This is used to provide a context for the findings on different resolution methods and to clarify how ERPs progress. For explanatory purposes, the ERP described here goes through almost all of the steps provided for in the Act. It should be noted that more than half of all employment relationship problems are settled informally without involvement of DoL institutions, **so this is not typical**. The narrative does, however, illustrate the range of issues and processes which may arise across the course of an employment relationship problem. This narrative is an indicative example, based on an amalgamation of several case studies. Sidebars draw on the full range of research to elucidate the incidence, causes, costs and benefits of each stage of the employment relationship problem as it might develop.

Figures quoted in this section come from the survey of private sector employers.⁵ The total response rate for this survey and the incidence rate for employment relationship problems were lower than expected. As a result the total numbers of ERPs resolved by some methods (mediation by non-DOL mediators, Employment Relations Authority hearings and the courts) were not large enough to provide reliable representative measures of their specific costs, time taken to resolve and satisfaction levels. Therefore, in the sections below that discuss specific resolution methods, analysis was conducted only for those methods with sufficient numbers to provide meaningful results.

Emergence of the problem

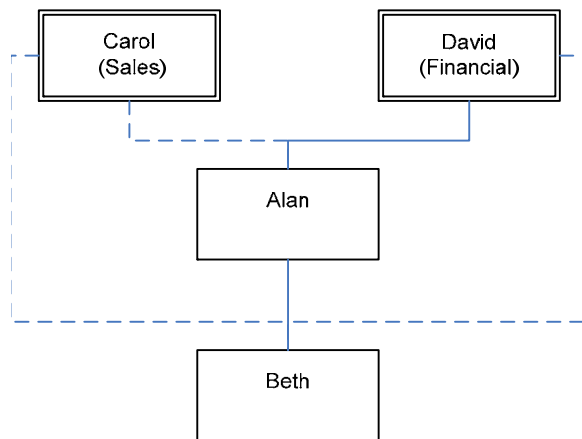
Alan⁶ worked in a moderate size company, where he had responsibility for aspects of the company's sales and finances. He supervised one staff member (Beth) and reported to two managers (Carol and David). At the time that the ERP arose Alan and the managers had been with the company for between 3 and 6 years and Beth for over 12 months.

Both the Mediation Survey and a survey of Authority hearings showed that the largest group of employees involved in hearings had been employed for between 1 and 4 years at the time the issue arose.

⁵ Findings from the survey of public sector employers are discussed in section 6.

⁶ All names have been invented for the purpose of this report, and the case study presented is a composite with elements from several cases.

Figure 3: Management structure for narrative



Several of the problems investigated in the case studies arose in workplaces with unclear or recently changed management structures.

Initially the relationships between the four were happy and productive. There were, however some tensions between Alan and Beth and lines of reporting were not always clear. Alan reported to Carol for sales functions and to David for other areas of work (Figure Three).

The initial issue arose when Beth complained to Carol about aspects of Alan's communication style. Carol notified Alan that Beth had made a complaint, but did not explain its specifics. Carol requested that Alan attend a meeting to discuss the issue. Alan declined involvement in a meeting unless he was notified of the complaint against him and the particulars of his alleged actions.

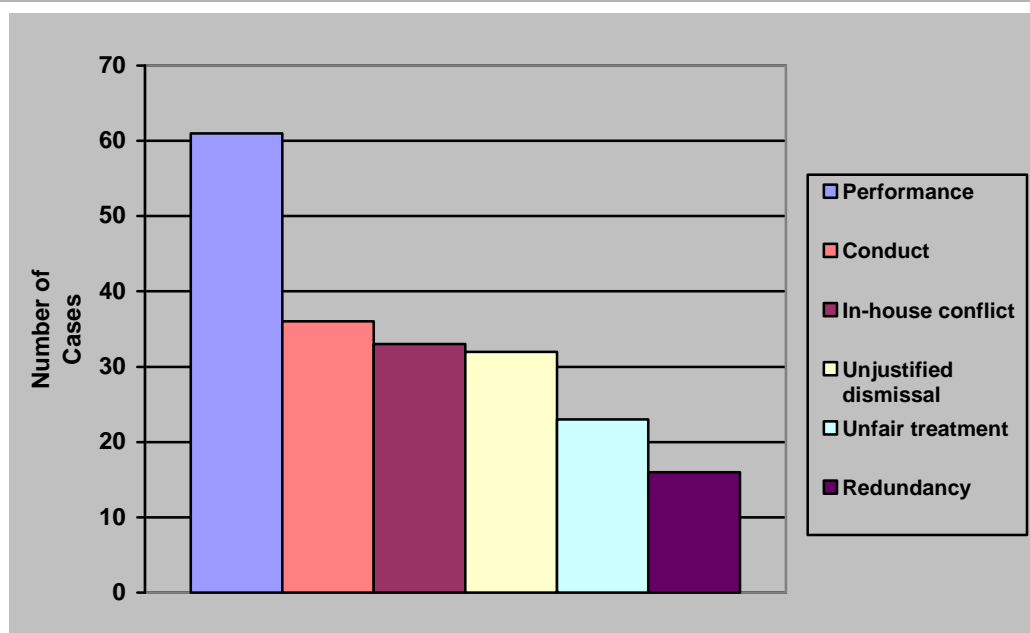
Types of employment relationship problem

For the purpose of the survey, we identified seven types of ERP:

- In-house conflict (personality and relationship issues)
- Performance issues
- Conduct issues
- Unfair treatment (including allegations of harassment or discrimination)
- Redundancy
- Alleged unjustified dismissal
- Others

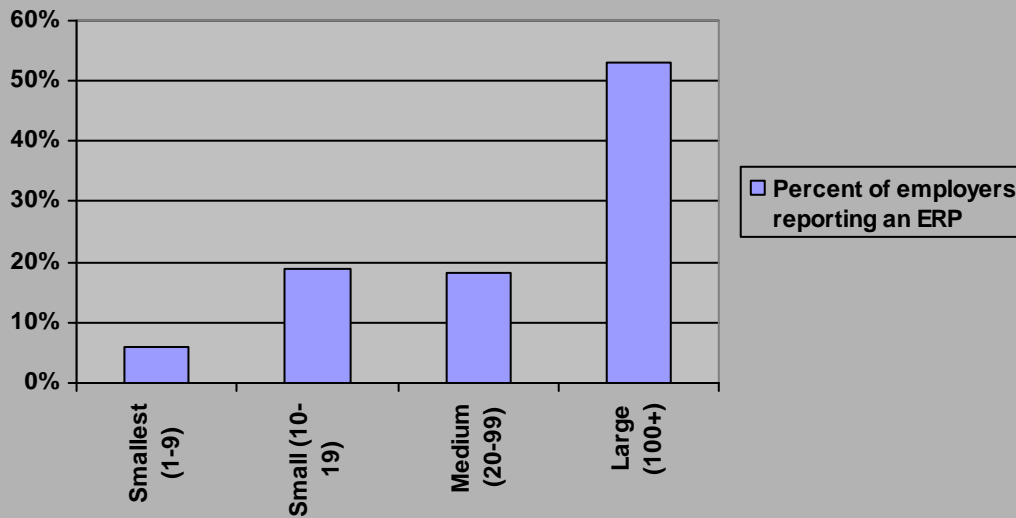
A single ERP might cover more than one of these categories. The graphic below shows the relative frequency of these.

Figure 4: Types of Employment relationship problem



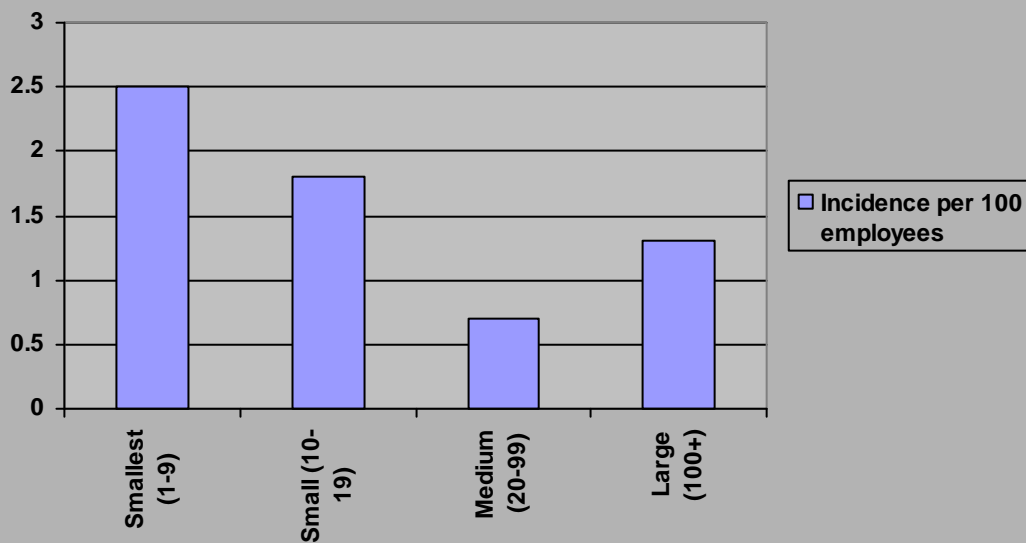
The likelihood of an employer facing an ERP over the course of a year varied according to the size of the employer. Although small employers reported more ERPs per employee, the higher number of employees meant that the largest employers were most likely to face an ERP in any given period.

Figure 5: Percent of employers facing ERPs in 12 month period



However, the incidence of disputes per hundred employees was highest for small firms. This is more important in determining the expected impact of ERPs on overall labour costs.

Figure 6: ERP incidence by employer size



Initial informal efforts at resolution

Alan requested a meeting with Beth to sort out whatever the issues were. Carol talked to Beth about this request, but Beth refused to meet. Alan once again asked Carol to explain the circumstances, but Carol said that she could not do so without Beth's permission. Carol and Alan both felt frustrated by the process, but Carol felt that she could not breach Beth's confidentiality.

The case studies suggest that many employers found conflict between employees particularly difficult to handle.

Carol began to investigate the complaint and found that some other colleagues had concerns about Alan's attitude. However she did not receive any specific examples. She again approached Alan to discuss the general thrust of the complaints. At this stage the issue was regarded as either a potential performance issue or a personality/relationship conflict, although the parties were unclear about the exact nature of the ERP.

It was common for in-house conflict issues, in particular, to be difficult to define initially. An employer raising a matter without providing specific examples of the behaviour that they are concerned about is taking high risks.

Resolution by negotiation

Employers responding to the survey were most likely to attempt resolution by direct negotiation in the first instance. Forty seven percent of the ERPs reaching the attention of respondents began with attempted individual resolution and 31% were resolved this way. Another 29% were settled in-house with external parties involved, making 60% settled by negotiation without mediation. Employers also favoured direct negotiation as a mechanism for future dispute resolution, with over 70% identifying it as their preferred option for future ERPs.

In-house resolutions were the quickest and lowest cost to settle. The median time for resolution was one month – the lowest for any of the methods of resolution – and the median direct cost was \$300, with a mean of \$3000.⁷

Introduction of external parties

Concerned about the development of issues, Alan decided that he needed help from a representative, and hired a lawyer to support him.

The introduction of external representatives was often a key moment in the development of an ERP. Once one party has brought in an external party, the other may feel constrained to do the same.

⁷ Mean costs for all types of dispute resolution were generally skewed by a small number of large settlements, making the means much higher than the typical cost levels.

When David heard that Alan had hired a lawyer he decided that the company also needed legal representation. The company hired a lawyer specialising in employment issues to assess the actions taking place so far. The specialist noted that managers had failed to make it clear to Alan what actions he needed to improve on and suggested that they continue to negotiate a solution. After a meeting of representatives, Alan, Beth and Carol agreed to try to improve working relationships, to be clearer about behavioural expectations and to use mediation in the event of future difficulties.

Legal representatives may enter at any point in the development of the ERP. There is no requirement to have a representative, even for hearings before the Authority. While both of the representatives here continued to support informal methods, other representatives favoured more confrontational or formal approaches.

Involvement of third parties

Negotiation involving third parties was the second most common starting point for resolving ERPs. Thirty two percent of ERPs involved third parties at the point they came to the attention of senior management or HR and 28% were resolved in-house but with the assistance of third parties.

The most common third parties were advocates or lawyers, with employees being slightly more likely to use an advocates or union representative and employers more likely to use lawyers. Not all advocates worked on a no win no fee basis.

The median time for resolution by negotiations involving third parties was two months and the median financial cost to employers was \$5,800, with a mean of \$13,100. No win no fee advocates were involved in 16% of ERPs (making up less than a quarter of the total employee representatives).

Mediation

After a few months it became apparent that the new arrangements were not working out. Beth was complaining of stress and Alan was getting conflicting messages from Carol and David about his performance. In accordance with their previous agreement, the team brought in an external mediator to help them work through the issues.

Alan supported sending the ERP to mediation, as he felt it gave him the first opportunity he had to explain his point of view. Up until that point he felt that Beth was the only one who had been able to explain her perspective (as the previous meeting had not included an opportunity for him to comment on specific

Stress was common for both the immediate participants and for others in the workplace (such as Beth).

The desire to be heard was a recurrent theme for employees in the case studies. "*Effectively I wanted to be heard, because in the first meeting the guys didn't hear me and ... trundled through.*" (Employee)

incidents).

The four of them met together with a private sector facilitator at a neutral venue. Under mediation, they agreed that Beth would continue to report to Alan and that Alan would attend a communication skills workshop. They also agreed to streamlined accountability arrangements, with David responsible for Alan's performance management.

The Department of Labour's Mediation Service provided mediators for most of the ERPs in the survey and case studies. However some employers said they would only use DOL mediators if the employment relationship had broken down irrevocably.

Mediation

Mediation was the next most common resolution mechanism. Mediation is a process where a neutral third party assists the parties to an ERP to find a mutually acceptable resolution.

Employees initiated most mediations but any party can call for mediation. Thirty percent of ERPs eventually settled in mediation (26% DOL mediators and 4% external mediators).

The median time for settling an ERP using DOL mediators was five months (this timeframe includes any earlier unsuccessful attempts at in-house resolution). The median direct cost to businesses of ERPs resolved in DOL mediation was \$7,275 and the mean was \$13,600.

The mediation survey carried out in 2006 reported on levels of settlement for ERPs resolved through DOL mediation. In this survey (covering a larger group of mediations) the median settlement cost was low in the range \$2000-5000,⁸ and a quarter of all mediations resulted in no payout to the employee.

Employment Relations Authority

Shortly after mediation, Beth went on sick leave. While Beth was on leave, Alan noticed that a sum of money had been incorrectly credited to his account. He told Carol about this, as she was in charge of that part of the system. She thanked him and said that she would look into it. She mentioned the discrepancy to David, who was concerned that the relationship between Alan and Beth may have contributed to Beth's illness. David then sent Alan a letter stating that the financial discrepancy was being treated as potential serious misconduct and requesting his attendance at an investigation meeting. At this meeting, Alan was dismissed.

⁸ As the settlement amounts were entered as ranges, it is not possible to give precise figures. However 44% of settlements cost less than \$2000 and 79% were less than \$5000.

Alan consulted his lawyer who recommended that they approach the Employment Relations Authority with a personal grievance claim. The Authority referred the complaint to the DOL Mediation Service. The company offered Alan a substantial sum of money to settle the case but would not agree to publicly withdraw the accusation of financial irregularities. Alan declined the offer, because he felt that the accusation of dishonesty was unjustified, and would prevent him from finding future work in his field. The company made other, similar, offers in the lead up to the Authority hearing, with the same results.

The Authority hearing took place four months later, and the determination was released three months after that. The determination was in favour of the employer, but Alan's lawyer was convinced that a challenge would be sustained.

In using Alan's discovery of a financial discrepancy as they did, the managers lost his trust and belief that they were acting in good faith. This happened in several ERPs in the case studies.

This "fishing" for excuses to dismiss the employee led to escalation and loss of trust in each case where it occurred.

Similar effects could be found where employees seemed to focus excessively on the process followed by the employer rather than the substantive issues.

The Authority must consider whether mediation will be helpful in resolving the problem.

Of the ERPs covered by the survey, only five percent (six ERPs) were resolved at the Authority. Taking an ERP through to the Authority was a time consuming process and generally appeared to be more expensive than negotiated or mediated resolutions.

Administrative data shows that the average time from an application to the Authority to the actual hearing, including time for unsuccessful mediations, where appropriate (where mediation was successful there was no need for a hearing) was 148 calendar days. The time from the Authority hearing to the issuing of a determination was 43 days.

Employment Court

The final stage of the ERP was a hearing before the Employment Court. It was still important to Alan to clear his name, and he saw the Court as his last opportunity to do so.

Both Alan and the company presented their cases to the Court. Taking into account the fact that Alan had volunteered the information about the overpayment (and therefore could not be assumed to have engaged in misconduct) and the poor processes used in leading up to the dismissal (fishing for reasons for dismissal and a failure to allow Alan to explain the discrepancy), the Court found in favour of all of Alan's claims and ordered compensation accordingly.

The company did not appeal the case to a higher court.

Court proceedings are the least common, but most expensive, way of settling ERPs. In the survey, only two cases were resolved at the Employment Court and one each at the High Court⁹ and Court of Appeal.

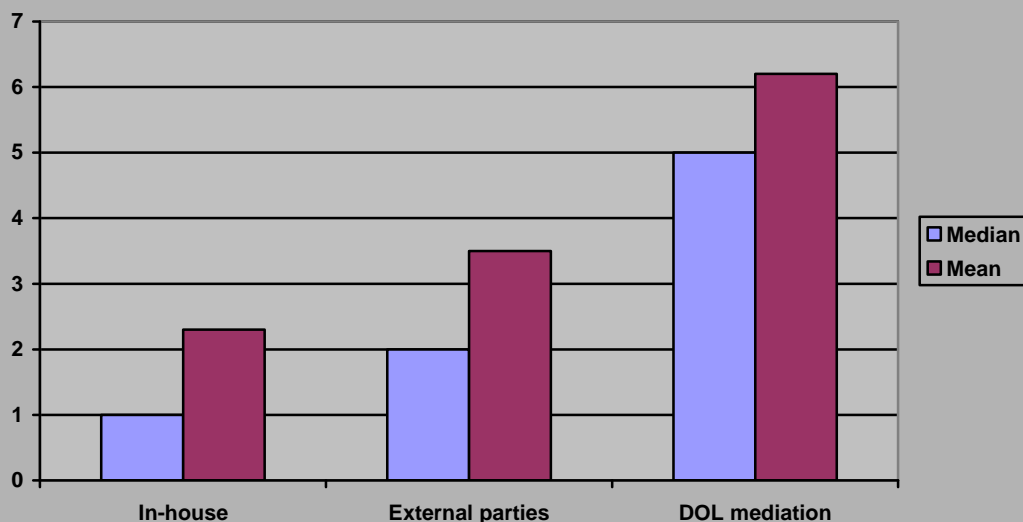
Because these cases were so rare, it is difficult to provide definite figures from the survey on the costs of ERPs that reach the court system. As an indication, however, the time and costs were higher again than those for the Authority.

Outcomes

Alan ended up winning his case at the Employment Court and his employer decided against further appeals. Although Alan received a substantial payout and cleared his name, he ended up out of pocket overall. For both him and his employers the process was also highly stressful and time-consuming. For the employer in this case the financial costs were higher than those Alan faced, as they had to make a payout and cover legal costs as well as the time devoted by company management to pursuing the case and staffing costs to replace Alan and Beth during the period of ERP.

Unsurprisingly, the type of mechanism used to resolve ERPs had a significant impact on the amount of time it took to reach resolution. ERPs that were settled in-house were the fastest, while cases that led to Employment Relations Authority or Court hearings took much longer.

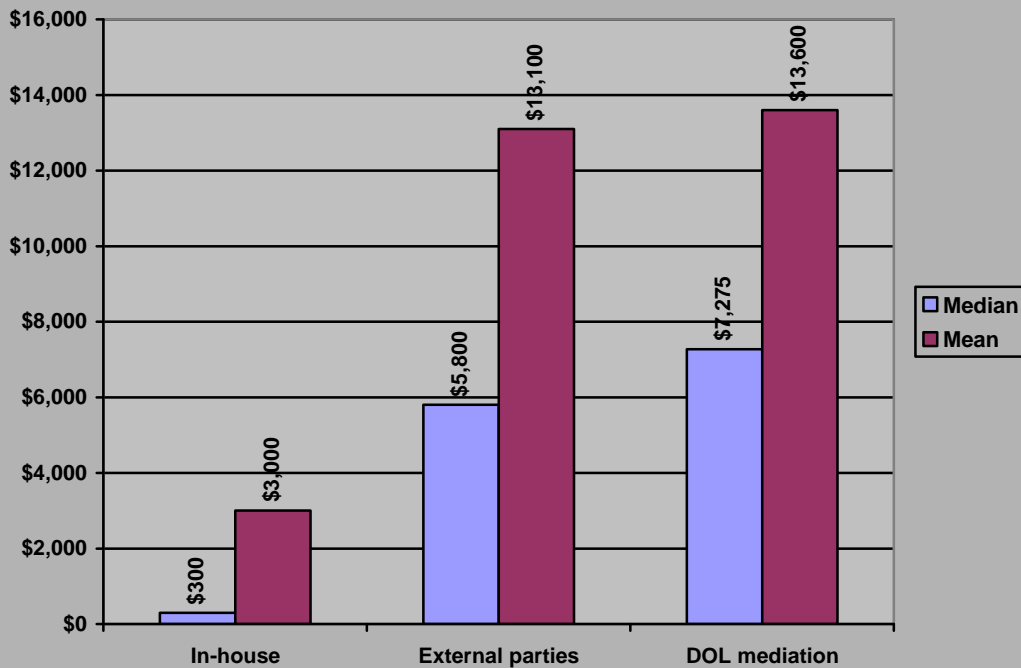
Figure 7: Duration by settlement type (months)



The relative costs to employers of ERPs according to the method of resolution are indicated below.

⁹ The Employment Court has exclusive jurisdiction for ERP issues. It is possible that related issues were taken to the High Court, leading to a resolution of the ERP in this case.

Figure 8: Costs by resolution type



The time taken and costs involved with problem resolution were lowest for the ERPs resolved through direct negotiations between the parties (the pathway most favoured by employers). The median costs for resolutions reached through mediation or negotiations involving third parties were between \$3,000 and \$7,300. There were insufficient numbers to provide significant figures for cases reaching the Authority or courts, although indicative figures showed that these cases were more expensive. The findings support the preference in the Act for informal resolutions, while showing that the costs can become a significant issue for employers.

It is probable that one of the reasons for the lower costs of internal resolutions is that they are dealing with less severe or complex ERPs than those settled by other means.

Satisfaction

We asked employers how satisfied they were with the process and outcomes of the most recent employment relationship problem they had resolved in their organisation. Overall, employers were satisfied with both the process and outcome of the resolution method they had used. Results are shown the table below. Other resolution methods (other mediation, Employment Relations Authority, and court system) are not reported because only small numbers of cases were involved, but responses indicated that satisfaction with the other methods was lower.

Large employers were the most satisfied, and employers with 10-19 employees the least satisfied, with both process and outcome. Employers found in-house resolution the most satisfying in terms of both process and outcome. The next

most satisfying process was Department of Labour mediation, followed by in-house resolution involving external parties (e.g. lawyers, advocates), though the satisfaction with the outcomes from these methods was about the same.

Employers	Process	Outcome
Overall employer satisfaction with the resolution method used	63%	66%
Most satisfied employers	100+ employees 79%	100+ employees 78%
Least satisfied employers	10-19 employees 57%	10-19 employees 62%
Satisfaction with resolution process	Process	Outcome
In-house	79%	100%
Department of Labour mediation	70%	55%
External parties	40%	56%

FACTORS INFLUENCING DECISIONS ON HOW EMPLOYMENT RELATIONSHIP PROBLEMS PROGRESS

Nearly every case study started with an attempt at internal resolution. The survey found that problems were most likely to be dealt with in-house, both initially (47 percent) and as a final resolution method (31 percent). If respondents had the chance to resolve the problem again, they would generally prefer to do so in-house, without external parties (71 percent).

However, a formal, external resolution pathway can be initiated by either party. Once an employee or employer applied for mediation or an Employment Relations Authority hearing, there was little chance for the problem resolution to continue down an informal path.

In the case studies, pure misconduct cases tended to follow a more predictable path – an internal disciplinary meeting, attended by the employee with a representative, followed by a warning, dismissal, or resignation. In contrast, performance and relationship issues (in particular) tended to be more complicated. Employers seemed to be less clear about how to resolve these issues. As a result, the problem often continued for a longer time. This was aggravated where employers or employees went “fishing” for additional issues, which increased the level of tension and made the problem more difficult to resolve.

For both employers and employees, the stakes involved impacted on their choices regarding the path of the employment relationship problem. For employees, the stakes included whether the employee had found a new job, the impact on their families, or the desire to clear their name. For employers, the stakes included their assessment of the costs of the resolution pathway, the effect of publicity on their reputation, or whether the problem would create a precedent within their organisation.

OVERALL IMPACT OF EMPLOYMENT RELATIONSHIP PROBLEMS ON THE ECONOMY

Financial costs and benefits of employment relationship problems

There are several ways of measuring the overall cost and benefit of employment relationship problems to the economy and society as a whole. None of these methods are perfect and many costs and benefits can only be estimated.

The net direct financial costs of ERPs can be defined as the total amount that employers and employees or their representatives spend on investigating, negotiating and resolving problems, including:

- Legal or similar costs,
- Meeting costs,
- Replacement staff to carry out the duties of staff under suspension or stress/sick leave during the course of an ERP.

The median net direct cost to immediately affected parties (that is employer and employee payments other than transfers) was around \$2200. The total direct costs for all employers (that is multiplying the average costs found in the survey by the number of ERPs estimated for the whole economy) would be around \$146 million for the 12 month period. This amounts to around 0.4% of private sector wages and salaries for the year.¹⁰ Adding in lost management and staff time and productivity during the course of the ERP would increase the total cost to employers of ERPs to \$214 million (0.6% of private sector wages and salaries for the year).

In addition to these direct financial costs, there were several other costs and benefits identified. ERPs were stressful for both employers and employees. Several of the employees interviewed for the case studies spent periods of time, varying from a week to months, on sick leave, and managers or employers also commented on the levels of stress. This stress could also spill over into poor morale for other employees, especially where the ERP included elements of in-house conflict or parties not acting in good faith. On the other hand, facing up to issues and addressing them can have significant benefits.

While ERPs may cause morale problems while they are being addressed, these may be made up for in improved morale if staff see a fair result, and particularly if management are seen to be addressing disruptive actions by other employees (for example, workplace bullying). In the survey, more of the employers who experienced ERPs during the previous twelve months reported increases in productivity than those who did not. Several employers in the case studies also put in place more robust processes and procedures to prevent recurrence of issues. For example, a case study employer put in place policies on alcohol and drug induced impairments in the workplace in response to dealing with a specific ERP related to these factors.

¹⁰ Based on Statistics New Zealand Quarterly Employment Survey data.

Around 17% of employers said their ERP resulted in a gain in productivity, about 8% said there was a loss in productivity and the remaining 75% said there was no change.

Social and personal costs and benefits

Findings from the case studies suggest that ERPs also presented both employees and their managers with a range of social costs and, in some cases, benefits.

Costs

The largest and most commonly mentioned costs were psychological. Both employees and employers found ERPs to be stressful, unpleasant and even distressing. Employees spoke of depression, anxiety and low self-esteem. Others commented on the amount of time and energy that fighting the ERPs cost them. Some said that they had reduced social contacts and energy for their families.

It was probably the most debilitating three years of my life... You'd get one letter and then you'd spend weeks analysing it, going over it ... My young fella he went from about form one to form three. ... And we lost those years with him. (Employee's husband)

The emotional effects themselves affected the employees' sleep and general health, in some cases exacerbating pre-existing conditions such as high blood pressure. This impact on employee health was reflected in increased use of sick leave entitlements during the ERP.

Employees felt their job and career had suffered as a result of the ERP. Some lost a job they wanted to do and got satisfaction from. Some noted the difficulties of not being able to use their employer as a referee for future job applications. During the ERP, employees also had reduced productivity at work because of the stress of the ERP, time spent on it during working hours, and/or personality conflict with colleagues.

During an ERP, employers, management and other employees, even if they were not directly involved in the ERP, also felt stressed from the unfolding ERP and sometimes from having to give evidence. Both employers and employees were also worried about the impacts of ERPs upon their reputations and the morale of those around them.

ERPs affected the stress levels, health, financial situation and productivity of both, employers and employees, and led to consequences for the families of both. All the interviewees indicated that the process had been unpleasant to be involved in, even extremely distressing. Most of them wanted the ERP to be resolved so they could put it behind them and carry on with their lives.

The extent and magnitude of the social costs varied a lot. To some extent, but not always, the severity of the consequences depended on:

- The length of time for which the case lingered. This in turn depended on the extent to which the case had escalated, and the length the parties were prepared to go resolve the case.

- Personal circumstances of the employee and employer. If the involved parties had family, often the party resolved the case just to be finished with it regardless of the outcome, because of the effects on their family. In contrast, an employee with no immediate family and in secure financial circumstances could pursue his case until it was resolved to his satisfaction.

Benefits

Some employees had discovered an inner strength in going through the case and thought they had come out a tougher person.

But ... I believed in what I was doing – believed that I was doing the right thing and that gave me strength to be able to carry on and work through it. (Employee)

Some employees had looked back on the job they had left and realised that they actually did not want to continue in it, so they were pleased to have left it. Following an ERP, a few employees had gone on to get better jobs. In addition, some others mentioned specific, one off, benefits, such as improved problem solving skills.

Where an employee left as a result of an ERP being resolved, remaining employees often experienced a better work atmosphere and a more functional team. This outcome was usually a result of the ERP being resolved, rather than the ERP itself; however it was a benefit. One employer also received positive publicity for pursuing a case against a workplace bully.

Following an ERP, some employers introduced better, more consistent, up-to-date and often formal procedures or processes such as human resources management, recruitment, and employment agreements. One employer now attended employment information/training seminars to ensure they were fully aware of their employment obligations. While instituting such improvements would incur a financial and time cost at the time, their payoffs should outweigh the costs in the long run.

Generally, both employers and employees in the case studies indicated that the costs, both financial and personal, far outweighed the benefits. Both employees and employers could readily list the costs of the ERP, but most identified few, if any, real benefits. Even employees who received relatively large financial settlements indicated that this did not make up for the costs they had incurred as a result of being involved in an ERP. Employers who noticed improvements in productivity or work atmosphere following the departure of a 'problem' employee had incurred reduced productivity and an unhealthy work atmosphere with reduced morale during the ERP.

Access to justice issues

Employment relationship problems of some type or another are inevitable. There will always be some underperforming staff, dishonest employees or bullying managers. The Employment Relations Act recognises this inevitability and provides a mechanism for resolution of these issues. In the absence of such a

system, the most likely consequence is that aggrieved employees would seek common law damages. Certainly this has been the experience in the USA, where courts have found a variety of grounds for challenging unjust dismissals. The Act's emphasis on "good faith" would be likely to encourage such developments in New Zealand. Such a common law approach would be likely to result in greater uncertainty for both employers and employees until sufficient case law had developed and less likelihood of some parties, in particular low income employees, to be able to fund the costs of litigating unfair treatment.

EMPLOYMENT RELATIONSHIP PROBLEMS IN THE PUBLIC SECTOR

Figures quoted in the report so far have been drawn from the survey of private sector employers. A similar survey of public sector employers was also conducted covering the following sectors:

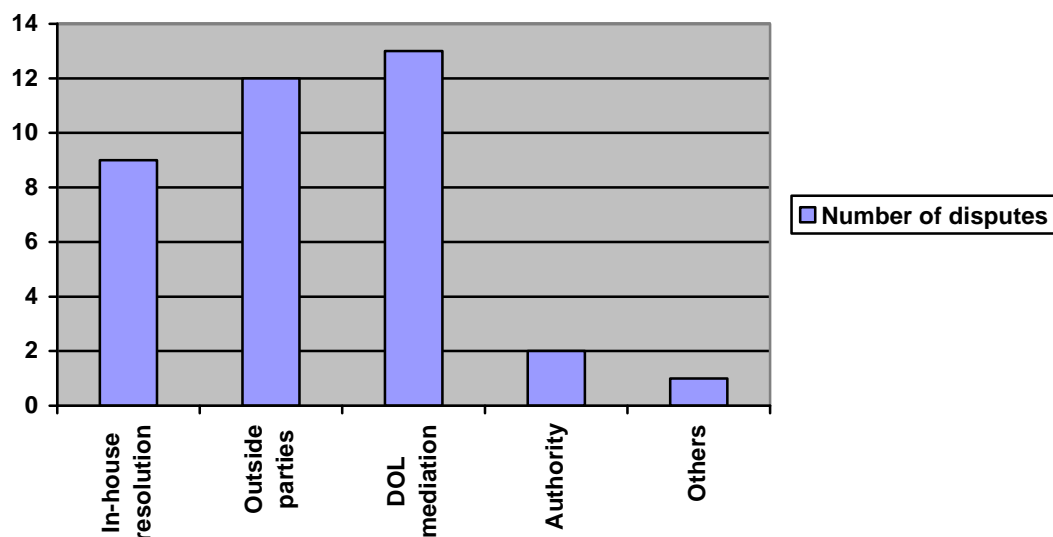
- government departments
- Crown entities
- Crown research institutes
- schools
- universities and polytechnics
- local authorities
- district health boards.

The response rate for the public sector survey was very low, making it difficult to make definitive conclusions about the impacts and progress of ERPs within that sector. Response rates for government departments and district health boards were particularly low. This uneven response makes any conclusions from this data tentative at best.

The incidence rate of ERPs for the public sector organisations responding to the survey was 0.8 ERPs per 100 employees, with the rate slightly higher in the smaller organisations (under 100 employees) and lower in the largest respondents.

The patterns of resolution were similar to those for the private sector, except for the fact that the proportion of in-house resolutions was somewhat lower, with the proportions of DOL mediations and external parties being accordingly higher. As expected with this mix of resolution mechanisms, the median time frames and costs of resolution were slightly higher than the private sector experience.

Figure 9: Resolution methods in the Private Sector



As can be seen from the chart, the total numbers of ERP resolutions of any type were low. Accordingly it is very difficult to provide reliable figures on the relative costs and benefits of different resolution methods for ERPs in the public sector. Generally, however, the trends were in line with those for the private sector, with internal resolution having the lowest direct costs and quickest resolutions.

GOOD PRACTICE AND KEY LESSONS

The most effective employers involved in the case studies (those who had few employment relationship problems and dealt with them in cost effective ways) shared several features:

- They set up policies and procedures to deal with the most common or damaging employment issues ahead of time. They made clear to their employees what the boundaries of acceptable conduct were.
- They sought to address potential issues before they led to major conflict.
- They focussed on the major issues of concern and maintained good faith relationships.
- They knew about the full range of resolution methods available and could choose among them according to circumstances.

All of these features are easier to achieve for large organisations. Both of the most effective employers in our case studies were large employers.

Putting policies and procedures into place ahead of time

Having clear policies and procedures was a major factor in the effectiveness of two of the case study employers. They provided employees with clear guidelines on what forms of behaviour were acceptable and managers with procedures to implement when an ERP arose. These policies and procedures meant that they were able to deal with alleged misconduct and other ERPs quickly and fairly. The procedures also meant that the employers could have confidence that any decisions they made would be upheld should the employee take a personal grievance.

We had, in terms of the policy documentation, very strong policy documentation ... had a code of conduct - and that code of conduct afforded us to cover performance issues and disciplinary issues, so it was very easy as a practitioner to work with that document and tie it all together when you're doing an investigation. (HR Manager)

For these employers, it was only on the rare occasions that their procedures were not followed that they felt at risk in taking ERPs through to formal hearings.

This contrasted with the employer who faced what he considered to be serious misconduct but felt that he needed to give the employee three warnings before dismissing him because of a lack of clear policies.

From other evidence, small employers appear less likely to have such policies and procedures in place, a finding that is not surprising given the smaller resources available to them and the lower probability that they will have faced ERPs in the past.

Effective employers also made sure that they had in place clear expectations for employees, which enabled employers to quickly isolate issues.

Settling employment relationship problems quickly

Both the social and financial costs of ERPs rise the longer it takes to reach resolution. The most effective employers in our case studies sought to identify potential problems early and come up with resolutions before relationships deteriorated.

Maintaining “Good Faith” relationships during employment relationship problems

It's a huge waste of time, completely soured my relationship with management, completely changed my view of management. ... I've lost all trust with them ... I've lost ... respect for them in terms of ... in terms of their position and it's changed my view to being – I'm just doing the job. (Employee)

Trust is a precious commodity which can make it easier to reach a resolution of an employment issue.

Good faith requires all parties to an employment relationship to (among other things):

- be active in maintaining positive relationships;
- avoid prejudging the facts of any case;
- give all parties the opportunity to be heard including commenting on any proposal that might be detrimental to their interests;
- maintain appropriate confidentiality and privacy; and
- be open and honest about all dealings.

Where an ERP arises from a relatively nebulous issue, such as conflict between employees or poor fit with the workplace, there is a temptation for employers to find something more objective to use as a reason for removing the person from the workplace. For example, one of the case study employers tried to make over-use of the internet an excuse to dismiss the employee. Another example (in two case studies) was a change in job descriptions which the employees saw as an effort to make them redundant.

These approaches are likely to be destructive of trust and be regarded by employees as showing a lack of good faith. Consequently, anything resembling a “fishing expedition” is likely to escalate the issue into a major dispute. Where the employees had not already brought in legal representation, such tactics led to their bringing representatives in, and representatives took a harder line on experiencing such tactics. It is therefore likely that fishing will extend the process, and therefore the costs.

Flexibility

The most effective employers recognised that there was not one single approach ideal for all ERPs, and tailored their responses to the circumstances. They used informal processes where appropriate, but were not afraid to dismiss an employee where they could demonstrate serious misconduct.

FUTURE RESEARCH

The research leading up to this report has focused on the economic costs to employers and the social costs to employees as these were the main areas of concern expressed in focus group research. Given time and a sufficient budget, there are a number of areas of future research that could be usefully undertaken by the Department of Labour:

- A survey of employees, to develop a fuller understanding of the economic costs they face.
- More intensive research into the qualitative impacts of ERPs on employers and other staff.
- Research on the impacts of unions on ERP costs and benefits.
- Repeated surveys of employers and employees at regular intervals (approximately every 3 years) to understand the changing patterns of ERPs and resolution methods over time (using a larger sample, if possible, to allow greater differentiation between the costs and benefits derived from different resolution techniques).
- More focussed research on the experiences of small businesses, as they appear to have greater difficulties in resolving ERPs.
- In depth investigation into ERA and Employment Court determinations.

The Department of Labour will consider all of these in setting priorities for future research.

APPENDIX I: METHODOLOGY

There were three main aspects to the long term research: a series of case studies and surveys of private and public sector employers. Full details of the methodology are provided in the technical research report (available upon request from the Department of Labour).

Case Studies

For the case studies, we identified parties to 15 ERPs and interviewed them to learn about the process of their issues, why they took the approaches they did, and the ultimate costs and benefits of the ERP. In most cases we only interviewed one party to the ERP (either the employer or employee), but we found many of the comments from participants were convergent.

Surveys

The surveys of the private and public sectors were conducted online, and participants were recruited via e-mails sent to senior managers/owners of businesses, or HR managers of businesses with separate HR functions. The survey requested detailed information about the ERP most recently settled and general information about the numbers of ERPs faced over the past 12 months and their costs and benefits.

Limitations

The total response rate for the private sector survey (11.5%) and the incidence rate for employment relationship problems were lower than expected. As a result the total numbers of ERPs resolved by some methods (mediation by non-DOL mediators, Employment Relations Authority hearings and the courts) were not large enough to provide reliable representative measures of their specific costs, time taken to resolve and satisfaction levels. Therefore, in sections of the report discussing specific resolution methods, analysis was conducted only for those methods with sufficient numbers to provide meaningful results.

The very low response rate for the public sector (4%), and particularly for district health boards and core government departments, have limited our ability to comment on costs and benefits of ERPs in the public sector.