



Case No: A2 / 2009 / 2273

Neutral Citation Number: [2010] EWCA Civ 784
IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM QUEEN'S BENCH DIVISION
(HIS HONOUR JUDGE SHAUN SPENCER QC)

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: Wednesday 14th April 2010

Before:

LORD JUSTICE LAWS
LADY JUSTICE SMITH
and
LORD JUSTICE RIMER

Between:

GX NETWORKS LIMITED

Applicant

- and -

GREENLAND

Respondent

(DAR Transcript of
WordWave International Limited
A Merrill Communications Company
165 Fleet Street, London EC4A 2DY
Tel No: 020 7404 1400 Fax No: 020 7831 8838
Official Shorthand Writers to the Court)

Mr Michael Duggan (instructed by Halliwells LLP) appeared on behalf of the **Appellant**.

Mr Jonathan Davies (instructed by Webster Dixon Solicitors) appeared on behalf of the **Respondent**.

Approved Judgment
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Lady Justice Smith:

1. This is an appeal from the order of His Honour Judge Shaun Spencer QC sitting as a High Court judge on 5 October 2009. The judge awarded the claimant, Ms Deborah Jane Greenland, the sum of £139,569.60 and her costs but gave the defendant, GX Networks Limited, permission to appeal to this court. The claim arose out of Ms Greenland's contract of employment with GX Networks Ltd.
2. GX made and installed broadband hardware. Ms Greenland was employed as a sales account manager. Her contract of employment provided for remuneration by way of a basic salary and commission on sales. Her claim was that she had not been paid the commission due under the contract for the sales she had achieved during 2007. GX disputed the claim, contending that it had exercised a discretionary right to cap her commission.
3. It will be necessary to examine the terms of the contract insofar as they relate to the payment of commission.
4. In early 2007, GX introduced new commission arrangements which were incorporated into Ms Greenland's contract. The provisions were set out in a document entitled Pipe 2007 Sales Compensation Plan. The main change was that, whereas in the past commission had been paid on sales orders, from 2007 onwards it was to be paid on billed revenue. The new arrangements also introduced for the first time a graduated incentive scheme limited to new business. Under the new scheme the commission arrangements fell into two parts. First, commission was to be paid on the achievement of a target. This was called performance commission and could be up to 100% of the basic salary. I do not need to describe those arrangements in detail as they are not in contention in this appeal. The second element of the commission was known as "overperformance" commission. It was payable on new business which exceeded the employee's target. Targets were set by the company after negotiation with the employee. The company had the right to adjust the employee's target at the end of each quarter or shortly thereafter. To assist in the setting of targets the employee was required to submit a forecast of the sales likely to be achieved in the year. Such forecasts had to be kept up to date on a monthly basis. On the face of it, the overperformance commission provisions appeared to give a strong incentive to achieve sales over the target level because the rate of commission was three times that earned on sales within the target level.
5. The method of calculation is quite difficult to explain in the abstract but relatively simple to follow in relation to a specific example. The example I will take is that which formed the basis of Ms Greenland's claim. In 2007 Ms Greenland's basic salary was £37,980 per annum. At the beginning of that year her annual sales target was set at £317,000 but, in July 2007, it was increased to £450,000. She had a very good year for sales and the actual sales revenue achieved was £1,370,504. That was 305% of her target level. In other words she had exceeded her target by 205% or by a factor of 2.05. Under the overperformance provisions her commission was to be

calculated as three times that factor, viz a factor of 6.15. The multiplicand was to be 70% of the annual salary. Thus her commission entitlement for overperformance was $6.15 \times 0.7 \times \text{£}37,980 = \text{£}163,503$.

6. The employer did not dispute that as an arithmetical calculation. Its stance was that neither it nor any employee had ever contemplated that an employee could earn so large a sum as commission. Its contention was that there were two ways in which it could control the amount of commission actually earned under this provision. The first and most obvious was by adjusting the target. It was common ground that the employer was entitled to adjust the target at the end of every quarter and, in respect of the final quarter of 2007, the employer could have done so at any time up to the end of October. If her target had been adjusted upwards in October 2007 to say £1.4 million, Ms Greenland would have fallen just short of that target and would not have been entitled to any commission at the enhanced rate. The evidence was that, in October 2007, the employer considered raising Ms Greenland's target level but decided not to do so. The reason given to the judge was that this would have had a "demotivating" effect upon her. Having decided not to increase her target, the employer decided to deploy what it claimed was an alternative method of controlling commission, namely to apply a cap. The provision said to permit this is within paragraph 4 of the new scheme where it is provided as follows:

"Targets will be reviewed at the end of Q1, Q2 and Q3 [that is, the first, second and third quarters] to ensure that the target is challenging but achievable. The sales director has the discretion to cap an individual's Q4 bonus at 100% if required although such cases will be by exception only and require HR and Finance agreement."

7. It is the meaning of that capping provision which lies at the heart of this appeal. According to the employer this provision allowed the sales director, Ms Sandra Beaumont, to disallow all overperformance bonus. That is what was meant by capping at 100%. Overperformance bonus only applied once the 100% bonus had been earned by fulfilment of the target. Alternatively it was contended that Ms Beaumont could disallow part of the overperformance bonus as calculated and allow a lower level to be paid. That is what happened in Ms Greenland's case. The cap was applied at 130%. That means in practice that her overperformance commission was to be based on a factor of 0.3 and would be calculated as $3 \times 0.3 \times 0.7 \times \text{£}37,980$. The employer's case was that it was entitled to do this. It had done so because it had been in some difficulty operating the new scheme, from which the wrinkles had not yet been removed. It had been faced with the prospect of demotivating Ms Greenland by increasing her target, in which case she might have received no overperformance bonus at all. Rather than do that it had been deemed fairer to keep her target as it was and cap her potential bonus, so that she was at least guaranteed some overperformance commission. The cap had been exercised in good faith.
8. A similar step had been taken in connection with several other employees without complaint. However, it appears that in those other cases there had been discussion with the employee who had agreed to a cap being imposed in preference to the

imposition of an increased target. No such discussion had taken place with Ms Greenland.

9. Before the judge, the claimant accepted that there was a discretion to cap the bonus at 100%, wiping out all overperformance commission and also conceded that there was a discretion to apply the cap at a higher level so as to allow some overperformance commission. I will return to that concession later in this judgment.
10. The claimant's main argument was that her entitlement to overperformance commission was as provided by calculation and the discretion to cap it could only be exercised in exceptional circumstances. There were none such in the present case. The judge held that the employer had not been entitled to apply the cap to Ms Greenland. He held that this was not a discretionary commission scheme. The scheme provided an entitlement to commission as calculated. The discretion related only to when that entitlement could be taken away. The judge observed that Ms Beaumont had decided voluntarily not to increase Ms Greenland's target when she could have done. The employer, he said, was stuck with the effect of that decision and he thought that Ms Beaumont regretted it. The judge considered the meaning of the words "by exception only". The claimant had argued that they must mean that the cap could only be applied in exceptional circumstances. The employer contended that those words were not the same as "only in exceptional circumstances". The judge said that he could see that but that he was unable to discern what the words "by exception only" meant. That, I think, was unfortunate and I will return to the point later.
11. The judge's approach appears to have been to regard the discretion to cap as unfettered and then to consider whether it had been exercised reasonably. He considered the various factors which the sales director said she had taken into account when deciding to apply the cap to Ms Greenland. He quoted passages from Ms Beaumont's evidence in one of which she had explained that the company had set aside a pool of money for commission payments of a total sum of £616,000. She explained that if Ms Greenland were to be paid her full calculated entitlement it would make a very large hole in that sum, which was supposed to cover all the sales personnel. In the end, at paragraph 35 of his judgment, the judge said:

“It is not an appropriate exercise of discretion in those circumstances to say that we will impose the cap because the money, which the rules and regulations for commission indicate the claimant will get, amounts to a sum considerably more than we want to pay. I cannot myself accept that that is a relevant factor for the exercise of a discretion. The circumstances are that the target, it seems, was too low but they are responsible for their targets. The defendant company cannot use money which would otherwise be the claimant's to get themselves out of a hole which they have got themselves in.”

12. On this appeal, Mr Duggan for the appellant employer submitted that the judge went wrong in several respects. First, he pointed to the passage that I have just read where the judge speaks of the appellant getting itself out of a hole which it had got itself into. He submitted that the judge seemed to have thought that the decision to cap had been made at the end of the year when it was appreciated how large Ms Greenland's entitlement had turned out to be. In fact, he submitted, the decision to cap had been made in October 2007 shortly after Ms Beaumont had decided not to increase the target. The decision was taken not to get the employer out of a hole but as an alternative to the raising of the target level.
13. I am not sure that the judge did misunderstand the position and it seems to me that his reference to the employer being in a hole was not entirely inappropriate but in any event, for reasons which I will explain, this appeal does not in my view turn on whether the judge's understanding of that point was correct.
14. Mr Duggan's second point concerned the meanings of the words "by exception only". He submitted that they did not mean that the discretion could be exercised only in exceptional circumstances. The provision meant that the usual method of controlling overperformance commission was by adjusting the target level, but if for any reason that was not done the alternative or exceptional method was by applying a cap. I cannot accept that submission. If that were right, the structure of the whole scheme would be undermined. The scheme provides for the negotiation of target levels although if no agreement is reached the company can impose a target provided that it is challenging but achievable. The overperformance commission is based on that target level. If Mr Duggan's submission were right, the sales director would be able to avoid consultation about the target level and simply apply the cap at any level she thought fit. That would mean that the scheme was simply a discretionary bonus scheme. It would have been quite pointless in those circumstances to have provisions for the calculation of entitlement.
15. Mr Duggan realistically acknowledged that if his submission as to the meaning of those words were rejected he would have to accept that the cap could only be applied in exceptional circumstances. The judge, he said, had not decided the case on that basis.
16. Mr Davies for the respondent submitted in his Respondent's Notice that, although the judge had not articulated his reasoning by reference to exceptional circumstances, what he had done was to reject all the contentions which the appellant claimed amounted to exceptional circumstances. Thus, he said, the real basis of the judge's decision was that he had found no exceptional circumstances which could justify the application of the cap.
17. In my view the capping provision in paragraph 4 is poorly drafted and its meaning is far from clear. Left to myself I might have held it to be void for uncertainty. Alternatively I might well have held that it was intended to operate to wipe out completely rather than to adjust the employee's entitlement to overperformance commission and could be exercised only if required and only in exceptional circumstances. I have in mind, for example, that it might have been invoked where

there had been some sort of misconduct by the employee such as would justify the wiping out of earned entitlement to commission. In such a case the human resources department would have a legitimate interest in the decision. It might also be invoked if the company were in dire financial straits, in which case the finance department would have a legitimate interest. No doubt there are other circumstances which might properly be categorised as exceptional.

18. I recognise, however, that the case was not argued on that basis before the judge; nor have we heard argument to that effect today. It was accepted on both sides that the power to cap could be used to adjust the amount of overperformance commission paid as well as wiping it out. I must therefore make my decision on that basis, which means that I must accept that the provision is of wider potential application than I might have held. However, I am firmly of the view that the capping provision does not provide an unfettered discretion. As I have said, if the employer had an unfettered discretion to take away or to reduce the overperformance commission, a major plank of the agreement would be completely undermined. Any provision which seeks to restrict liability must be strictly construed. In my view the provision can only be applied in exceptional circumstances. I cannot think of any other meaning which could sensibly be given to the words "by exception only".
19. I said earlier that I thought it was unfortunate that the judge did not reach any conclusion as to the meaning of the words "by exception only". If he had done, he would have necessarily considered the various factors and circumstances and decided whether or not they were exceptional. He did not do so, although I agree with Mr Davies's submission that he considered and commented adversely upon the various circumstances which the appellant contended were exceptional. However, I cannot accept that the judge effectively decided the case on the basis that there were no exceptional circumstances to justify the imposition of the cap. It follows that this court must make that assessment for itself.
20. Mr Duggan's submissions on this topic faced him with an uphill task. He submitted that the appellant had been in difficulties in setting targets. The scheme was new. Its difficulties had been increased because the respondent had submitted hopelessly inaccurate forecasts of her likely sales. That was true. Her forecasts had been made on the mistaken assumption that she had to include old recurring business as well as new business. In fact she was supposed to forecast only the level of new business. However, it is clear to me that that situation could not and did not in fact create any particular difficulty for the appellant in setting a target. Ms Beaumont's statement, as quoted by the judge, made it plain that, by October 2007, when she was considering whether to raise Ms Greenland's target to a higher level, she was aware that the forecasts had been wrong and why that was so. She was also aware that Ms Greenland had already exceeded her existing target of £450,000 and was likely in the rest of the year to exceed it by a large margin. That was because Tesco's stores were about to take substantial deliveries in the last two months of the year. Thus, any inaccuracy in the forecasting was in my view clearly irrelevant and did not cause any difficulties to the appellant.
21. Mr Duggan submitted that the circumstances were exceptional because Ms Greenland's target had not been raised as it could have been. It is common ground

that the target could have been raised so as to ensure that she received little or no overperformance commission. Under the scheme, targets were supposed to be reviewed at the end of every quarter and consultation was an essential part of the process. Ms Beaumont chose not to review Ms Greenland's target for reasons which seemed good to her at the time. She thought that to raise the target unilaterally would be demotivating. She did not consult with Ms Greenland about her target. There is no evidence as to why she did not. It may be that she wished to avoid confrontation which would not have been conducive to the continuance of Ms Greenland's efforts. Whatever her exact reasoning, she took a decision for what appeared to her to be good management reasons. She did so in full knowledge of the facts. I cannot see how it can be said that those amounted to exceptional circumstances.

22. It seems to me that the only factor which could possibly be described as exceptional was that Ms Greenland achieved unusually good sales in the later part of 2007. Within a scheme which is designed to encourage and reward effort and success it cannot be envisaged that an unusual degree of success should be treated as an exceptional circumstances justifying the capping of the very reward which was being offered. To be fair Mr Duggan did not suggest that it could be.

23. I am quite satisfied that at the time of the decision to cap Ms Greenland's commission there were in existence no exceptional circumstances which could justify the exercise of that power. The decision to cap was therefore not in accordance with the contract of employment and Ms Greenland was entitled to receive the full commission which she had earned. That was what the judge decided, so, although by different reasoning, I would uphold the judge's decision and dismiss the appeal.

Lord Justice Laws:

24. I agree.

Lord Justice Rimer:

25. And so do I.

Order: Appeal dismissed