MAYER·BROWN JSM

Employment & Benefits
Legal Update
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Must an Employer Complete Disciplinary Proceedings before Termination?

Summary

On 2 March 2009, the Court of First Instance held in *Warham & Ors v. Cathay Pacific Airways Limited* & Anor (the "**CPA Case**") that Cathay Pacific Airways Limited ("**CPA**") was obliged to follow its disciplinary procedure before terminating the employment of a pilot where the underlying reason for the dismissal is CPA's belief that the pilot is guilty of misconduct. This decision runs contrary to the decision of Deputy High Court Judge To in *Cheung Chi Keung v. The Hospital Authority* (the "**HA Case**") handed down on 15 February 2006 which held that the Hospital Authority could elect to terminate the employment of an employee by giving the relevant notice and without having to complete a disciplinary process which was in progress at the time of termination of employment.

This article considers the CPA Case and how it can be reconciled with the earlier HA Case.

Full Update

Before considering the CPA Case it is instructive to look at the earlier HA Case.

(A) THE HA CASE

Mr Cheung was employed as a general manager with the Hospital Authority ("**HA**") from March 1994. His employment contract stipulated that termination could be by giving two months' notice or making payment of wages in lieu. In March 2002, the HA issued a written warning to Mr Cheung for providing misleading information to its finance sub-committee. This warning made it clear that he would be liable to disciplinary action if he failed to achieve a satisfactory standard of conduct and performance.

Subsequently, in January 2003, the HA decided to initiate disciplinary proceedings for unsatisfactory performance at work. However, before the proceedings were completed, Mr Cheung's contract was terminated, with the HA paying two months' wages in lieu of notice.

Mr Cheung began proceedings in the Court of First Instance, claiming wrongful dismissal and that the HA could not terminate his contract of employment while disciplinary proceedings were taking place.

The basis of Mr Cheung's action was the UK case of *Gunton v Richmond-upon-Thames LBC*. The plaintiff in *Gunton's* case was appointed by the defendant Council as a college registrar under an employment contract terminable by one month's notice. The employment contract incorporated a procedure for dismissal of the employee on disciplinary grounds. The plaintiff's superior recommended his dismissal from the Council's service and commenced disciplinary proceedings under the disciplinary procedure. Before the procedures had been fully complied with, the Council gave him one month's notice of termination. The plaintiff brought an action for a declaration that the Council's purported termination was void. The court granted the declaration and ordered an assessment of damages. The court said that the effect of the incorporation of the disciplinary procedures into the plaintiff's employment contract was that the plaintiff could not lawfully be dismissed on a disciplinary ground until the procedure had been carried out.

While Mr Cheung's contract incorporated a disciplinary procedure, the court was of the opinion that the procedure only applied if the HA sought to terminate his employment for cause. If the HA chose to terminate Mr Cheung's employment for cause it would need to allow the disciplinary procedures, including the appeal procedures, to run their full course before terminating his employment for cause.

There was no obligation requiring compliance with the disciplinary procedure if the HA chose to terminate his employment by notice, even if the disciplinary procedure had commenced but had not been completed.

Accordingly, the Court found that if the HA chose to terminate Mr Cheung's contract by way of notice or payment of wages in lieu, it did not need to complete any disciplinary procedures beforehand. The Court held that termination of employment in accordance with the notice provision is not wrongful and is consistent with the decision of *Gunton's* case.

It was the HA's prerogative to determine whether to terminate for cause or by giving the required notice or payment.

(B) BACKGROUND TO THE CPA CASE

On 9 July 2001, CPA terminated the plaintiffs' (each of whom was a pilot) employment under clause 35.3 of their conditions of service ("**COS**") by paying three months' wages in lieu of notice. The plaintiffs claimed that CPA took action against them because their staff association took industrial action in July 2001.

Clause 35.3 of COS provided that CPA could terminate the plaintiffs' employment by giving three months' notice or payment of wages in lieu of notice. The COS included "Disciplinary and Grievance Procedures" (the "**D&G Procedure**") which sets out a disciplinary procedure to be followed where CPA alleges misconduct on the part of a pilot.

The Court was asked to determine two preliminary issues, namely:

i. Whether CPA had an unfettered contractual right to terminate the plaintiffs' contracts of employment by giving the relevant notice without first applying the D&G Procedure, and
ii. If the answer to (i) is "no", whether CPA had an unfettered contractual right to terminate the plaintiffs' contracts of employment without cause by giving the relevant notice or making a payment of wages in lieu once the D&G Procedure had been carried out, irrespective of the outcome arising from those procedures.

For the purpose of determining the two preliminary issues, the Court proceeded on the "**working assumption**" that the underlying reason for the pilots' dismissal was CPA's belief that the pilots were guilty of misconduct. The Court stressed that this was **merely a working assumption** and it remained an unresolved factual issue whether CPA actually had such underlying motivation.

(C) FINDING OF THE COURT IN THE CPA CASE

The Court looked at the D&G Procedure and noted that it identified five types of disciplinary action which ranged from admonishment to "dismissal" and "summary dismissal". According to the D&G Procedure, dismissal is to "take place after the appropriate notice has been given or payment made in lieu of notice". The Court held that this must be a reference to the giving of three months' notice of termination or payment in lieu under clause 35.3 of the COS.

The Court asked (rhetorically) whether it is a sufficient answer to say that, whatever the underlying motive, officially the plaintiffs' employment were terminated without cause pursuant to clause 35.3. The Court answered in the negative, for the following reasons:

- The nature of an employment contract has been transformed over the past 30 years or so. It has been recognised that a person's employment is usually one of the most important things in his or her life. It is "an important source of one's identity, self-esteem and well-being". Therefore, "absent clear indications to the contrary, the Court must assume that in entering into an employment contract an employee would not have intended provisions protecting the security of his livelihood to be readily by-passed."
- Given the assumed underlying reason for the dismissals, the Court did not think that the fact that the termination letters were silent on CPA's motive makes a substantive difference and clause 35.3 must be read as modified or constrained by the D&G Procedure.
- CPA submitted that it had a choice to dismiss with cause pursuant to the D&G Procedure or to dismiss without cause pursuant to clause 35.3, and it was CPA's prerogative which way it wished to proceed. The Court rejected this submission saying that construing the relevant contracts as a whole and in light of the social reality referred to above, the D&G Procedure imposed a fetter on clause 35.3. The Court said that if CPA's submission was accepted, the D&G Procedure could always be by-passed by CPA not giving the officer any reason for termination. An officer would

then not be afforded any opportunity to refute unjustified allegations of misconduct and protect his source of livelihood. The officer would simply have to accept dismissal without cause. That could have a devastating effect on the officer's reputation and the Court said that far clearer words would have to be inserted in the COS if they are to be construed as submitted by CPA.

- CPA submitted that construing clause 35.3 as being fettered by the D&G Procedure would produce an "unreal" outcome. If CPA were obliged to follow the D&G Procedure, it could simply offer no evidence of misconduct in the disciplinary proceedings. This would cause any preliminary investigation under the D&G Procedures to conclude that there is no case for an officer to answer. In that event, CPA could then promptly give notice or payment in lieu without cause under clause 35.3. The Court said that such approach by CPA would come close to positing bad faith on CPA's part and that while CPA may attempt to get around the obligations in the D&G Procedure, the underlying reason would remain the underlying reason and the obligation to give a fair hearing and appeal would still remain.
- CPA submitted that if clause 35.3 is read subject to the D&G Procedure it would lead to an absurd result. It would mean that an employee who misconducts himself is more secure in his employment than one who does not. That is, the D&G Procedure could take longer than three months (the period of notice in clause 35.3) to complete. That would mean that the "model employee" can be dismissed without cause within three months, while the "rogue employee" must be retained pending completion of the D&G Procedure. The Court rejected this argument saying that on the one hand, an employee may be a rogue, but still be dismissed for reasons unrelated to any misconduct on his part. In that case, he would still be subject to clause 35.3 as is the model employee.

The Court considered both Gunton's case and the HA Case.

The Court discerned three principles from Gunton's case, namely:

a. If the employer's intention is to dismiss on disciplinary grounds, on a true construction of the relevant contract the disciplinary procedures of the Council (set out in Regulations) had to be completed before dismissal could be effected,
b. The fact that following the procedures in the Regulations might take longer than the one month's notice period was not pertinent. Otherwise, to allow the employer to rely on the one month's notice provision would make a "nonsense" of the protection afforded by the Regulations,
c. Whatever the outcome of the procedures, the employer would thereafter be able to give one month's notice to dismiss the plaintiff.

The Court did not follow the HA Case. The Court relied (again) on the importance of employment in a person's life and said it "seems odd to me that the validity or otherwise of its termination should fall to be determined on the basis of mere 'form' or 'artificiality'".

The Court was unable to see any distinction between the HA Case and Gunton's case. However, the Court did note that it may be that on the facts of the HA Case the contractual provision allowing two months' notice was not qualified by the requirements of the Manual (which contained the disciplinary procedures). In this case, the HA would have two independent options from which it could choose.

The Court held in response to the two issues, that the right to terminate without cause under clause 35.3 of the COS is not unfettered and cannot be used to bypass the D&G Procedures where the underlying reason behind a dismissal is alleged misconduct. As for the second issue, the Court held (following Gunton's case) that once the D&G Procedures had been completed and a final outcome is announced, the right to terminate without cause under clause 35.3 may be exercised.

(D) COMMENTS

Whether an employer is obliged to complete disciplinary procedures before exercising any right to terminate by notice (or payment of wages in lieu) will turn on the contract of employment.

If the contract of employment incorporates contractual disciplinary procedures then the employer must comply with such procedures, where the underlying reason for termination falls within the scope of the procedures, prior to terminating the employment of the employee.

While each case will turn on the contractual terms regulating the employment relationship, what may be gleaned from the CPA Case is that where there may be any doubt in interpreting those contractual terms, a court is likely to err in favour of the employee.

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