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Changing bonus terms: Legal Q&A

James Green, solicitor, Burges Salmon 05 January 2010 12:20

There was much talk about the bankers' bonuses awarded near the end of 2009, followed by the chancellor's [Pre-Budget Report](#), which [outlined a 50% tax on the banks on large bonus payments](#).

Not many of us will be handing out six-figure bonuses this year, but for HR professionals who want to make changes to bonus terms, such as making the payment as part of a salary, the road could be rocky.

Q Do we really have to pay the bonuses?

A There are a number of ways to structure a bonus scheme, and the way in which this is done will fundamentally affect the freedom an employer has to reduce, defer or withhold a bonus. The key question is whether the bonus is contractual or discretionary.

The scheme may reserve full discretion to the employer, so the employer retains complete freedom as to when and how much to pay, or whether to pay at all. Alternatively, the scheme may be fully contractual, so that an employee has a contractual entitlement to a bonus at a particular level if he or she hits applicable targets. More commonly, the bonus scheme may be a mix of the two, with a discretionary element built into a contractual right to participate in a bonus scheme.

Q Nothing is set down in black and white. Are we off the hook?

A Not necessarily. Even where the scheme itself looks non-contractual, in some circumstances, a contractual entitlement to a bonus may have become implied through custom and practice. This is a particular problem where, having regularly paid annual bonuses, an employer then seeks to withdraw a bonus altogether and pay nothing. It is usually easier in those circumstances to pay a reduced rather than a nil bonus.

Q Should I reduce, defer or withhold bonuses?

A In cases where the bonus in question is a contractual obligation, seeking to withdraw or defer that bonus would, in most circumstances, require the employee's consent to vary that element of his or her contract. The contract itself may reserve a right to the employer to make amendments to the scheme, but that will generally only permit the employer a degree of wriggle room rather than the ability to make wholesale changes.

Where the scheme has a discretionary element, the employer should be able to rely on the exercise of that discretion to limit payments under the scheme or, in some circumstances, to defer or even withdraw them altogether. This does not mean, however, that an employer has a completely free hand. There are still some limits to the changes an employer can make, and the way in which you manage such changes to your bonus scheme can mean the difference between success and litigation.

Q Dealing with court or tribunal claims could quickly become more costly than the bonus itself. What is the risk of finding myself on the witness stand?

A Where an employer denies an employee a bonus to which he or she is contractually entitled, the employee may be able to bring a claim for breach of contract. The High Court has seen a number of high value banker bonus cases in recent years.

The employee may also have a claim for unlawful deduction from wages. However, this claim may only be brought where the employee can identify the precise sum that the employer has failed to pay and cannot, therefore, be used to challenge the employer's exercise of discretion.

Where an employer has behaved particularly poorly, an employee may seek to resign and claim constructive unfair dismissal.

Q Whose bonus should be the first to go?

A If, rather than reducing bonuses across the board, an employer seeks to pick and choose, the risk of challenges in the field of discrimination looms. If the decision to award a bonus is in part linked to, for example, length of service or a requirement for full-time working, then there may be grounds for complaint based on indirect sex discrimination. It is generally accepted by employment tribunals that women with childcare responsibilities are more likely to work part-time and have shorter periods of continuous employment with one employer.

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