

BAD LEAVER PROVISION WHERE SHARES AND LOAN NOTES WERE FORFEITED WAS FOUND NOT TO BE UNCONSCIONABLE OR A PENALTY

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BAD LEAVER PROVISION WHERE SHARES AND LOAN NOTES WERE FORFEITED WAS FOUND NOT TO BE UNCONSCIONABLE OR A PENALTY

The Claimant worked for a company that was acquired by way of a sale of shares. As a condition of the acquisition, the purchaser required that the seller provide equity to key employees to ensure continuity post-acquisition. The Claimant was therefore given a 2% shareholding.

The Claimant sold her shares to the new company pursuant to a share sale agreement which provided for both initial and deferred consideration. The deferred consideration included

staged cash payments and an entitlement to earn-out shares and loan notes, which were subject to good leaver/bad leaver provisions.

A bad leaver included an employee who voluntarily resigned so they would forfeit their loan notes in whatever way the Remuneration Committee may determine in good faith, and would be required to sell back their share at the lower of acquisition cost or fair value.

The Claimant subsequently resigned and sought to challenge the bad leaver provisions by arguing breach of contract and unauthorised deduction from wages. It was claimed that the bad leaver provisions were unenforceable as they were (1) unconscionable, (2) in breach of the rule against penalties and (3) amounted to a contravention of the Modern Slavery Act 2015 as the covenant not to become a bad leaver amounted to forced or compulsory labour.

The EAT ruled that the Claimant could not bring a claim under the unauthorised deductions from wages provisions. The Employment Rights Act 1996 excluded claims for any payment to the worker otherwise than in his capacity as a worker. The shares and loan notes were provided to the claimant in her capacity as seller of shares, not worker.

The EAT held that there is a three stage test for setting aside an unconscionable bargain: (1) one party must have been at a serious disadvantage whether through poverty, ignorance, lack of advice or otherwise; (2) the other party must have exploited that disadvantage in some morally culpable manner, and (3) the resulting transaction must be overreaching and oppressive. The EAT found that the Claimant did not meet even the first criterion – she had warranted in the share sale agreement that she had taken professional advice; further, the bad leaver provisions were, in fact, reasonable. In any event, setting aside the agreement would have put the Claimant in the position of never having received the shares, which was not

what she was seeking.

There was also no bad faith in treating the Claimant as a bad leaver even though the Remuneration Committee had discretion under the Articles to re-classify her as a good leaver. The bad leaver provisions, to which the Claimant had agreed, made it clear that an employee who gave notice to terminate employment was a bad leaver, and no exceptional circumstances had arisen such as to call into question the employer's decision to apply the default treatment of a voluntary resignation as making her a bad leaver.

Finally, in terms of the alleged penalty, the EAT held that the rule against penalty clauses was not relevant in this case because the consequences of being a bad leaver did not depend on the Claimant being in breach of contract/covenant. The company simply relied on the provisions of the Articles, which set out the conditions that needed to be satisfied to secure payment and these had not been met.

Nosworthy v Instinctif Partners Ltd [2019] UKEAT/0100/18

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