TERMINATION OF EMPLOYMENT:
A GUIDE TO COUNSEL FOR EMPLOYEES

by Nancy M. Shapiro, Koskie Minsky LLP

"Wrongful dismissal" refers to a termination where the employer has failed to provide adequate working notice or payment in lieu of notice. The fundamental question which you must offer an opinion is whether the employee has been wrongfully dismissed.

STEP 1 – INVESTIGATION & FACT FINDING:

First, one needs to gain the material information from one's client. This will include:

- age
- education
- work history
- position history with relevant employer
    - how they came to join the company including any inducement to leave secure employment
    - start date
    - reporting structure
    - position(s) held
    - responsibilities/position description
- compensation details
- copy of any Employment Agreement
- copy of any other potentially relevant documents including:
    - Non-Competition, Non-Solicitation Agreement
    - Stock Option Plan, Long term incentive plan
    - Bonus Plan
    - Shareholder's Agreement (if applicable)
    - Pension Statement (in particular if D.B.P.P.)
    - Commission Plan
- details of any performance issues
- details of any health issues
- details of any other relevant concerns
- why the employee was told they were being terminated
    - any belief the employee has as to why they were terminated

STEP 2 – OPINION & CLIENT REPORTING:

A) Legislation, Contracts, Common law

Your client then wants to hear your opinion as to their entitlement. Be sure to explain their entitlement in the context of the law so it is understandable and in plain English. For example, there is a strong chance your client has no idea what constitutes "severance pay".

The following are key points to communicate:

1. There are two regimes which govern employee rights and employer obligations with respect of termination in Canada.

2. The first is determined by the applicable provincial or federal employment standards legislation, which defines an employee's minimum rights with respect to many matters concerning their employment, including rights on termination. There are also mass termination provisions in all jurisdictions which may require additional notice to employees, notification and planning submission to provincial federal ministries of labour. The first thing is to ascertain and advise the employee of his/her statutory minimum entitlement. This involves ascertaining which piece of Employment Standards legislation applies and the rights and obligations arising from the legislation.

3. The second, and overlapping regime, is the common law.

4. Whereas the employment standards legislation prescribes minimal entitlements, much like minimum wage, it does not set out the actual amount of notice required to be provided to an employee upon termination. The common law needs to be considered to assess actual liability.

5. The actual obligation to be met is that of the common law obligation to provide reasonable notice.

6. However, the parties can have an employment contract by which they can agree as to what will constitute reasonable notice, subject to the applicable statutory minimums being met.[1] (refer to section B concerning contractual challenges).

7. In the absence of such a contract, the assessment of reasonable notice is dependent on consideration of the factors established by the court in *Bardal v. The Globe and Mail*[2] and expanded upon by the cases thereafter, namely:

    - age
    - length of service
    - nature of the position held
    - compensation
    - availability of other suitable alternate employment having consideration to the employee's training and experience
    - availability of other suitable alternate employment having consideration for economic matters, geography, and other "uniqueness" factors

---

[1] *Machtinger v. HOJ Industries Ltd.*, [1992] 1 S.C.R. 986 (S.C.C.); *Wood v. Industrial Accident Prevention Association*, [2000] O.T.C. 605 (Ont. S.C.J.).

[2] *Bardal v. The Globe & Mail Ltd.* (1960), 24 D.L.R. (2d) 140 (Ont.H.C.) and *Love v. Acuity Investment Management Inc.*, 2011 ONCA 130

- Reasonable notice may fall as low as the ESA minimum and generally will not exceed 24 months (though 28 months has been awarded in unusual circumstances).

8. Assessment of what will constitute reasonable notice requires knowledge of the case law or undertaking appropriate legal research. If you are providing an opinion to a client, you should have sufficient knowledge of the case law to provide this opinion when you meet with the client or undertake to obtain the information at the initial meeting and get back to them with the opinion shortly thereafter once you have had the opportunity to acquaint yourself with the relevant case law.

9. It is important to remember that common law reasonable notice can generally be provided as either working notice or payment in lieu of notice. Counsel must explain to the client what that means, as well as the obligation to mitigate (i.e. seek new employment) and the impact of re-employment during the notice period on their claim. It is noteworthy that an employee has no duty to mitigate damages (unless the employment agreement stipulates such obligation) when the employment agreement fixes the notice period or termination pay in lieu of notice.[3]

B) Contract Challenges

If the employee has signed an Employment Agreement/Contract, which impacts in some fashion their rights, it will be necessary to assess whether or not the contract is enforceable.

There are a plethora of drafting errors which can be made and can lead to potentially devastating consequences. It is necessary to understand the treatment which contractual provisions typically receive by the court to advise the client whether what they contracted for will be enforced.

1) Circumstances of signing of Employment Contracts

The requirement of consideration, a first year law school principle, is surprisingly one which is frequently overlooked. Contracts must be signed prior to the commencement of employment; if they are signed during the course of employment, they must be accompanied by adequate consideration, which is conditional upon execution[4]. Continued employment will not constitute sufficient consideration. The Court of Appeal in *Techform Products Ltd. v. Wolda*[5] stated:

---

[3] *Bowes v.Goss Power Products Ltd.*, 2012 ONCA 425
[4] *Stott v. Merit Investment Corp.* (1988), 48 D.L.R. (4th) 288 (Ont. C.A.)
[5] 2001 CanLII 8604 (Ont. C.A.) at para 26.

> "Where there is no clear prior intention to terminate that the employer sets aside, and no promise to refrain from discharging for any period after signing the amendment, it is very difficult to see anything of value flowed to the employee in return for his signature. The employer cannot, out of the blue, simply present the employee with an amendment to the employment contract say, "sign or you'll be fired" and expect a binding contractual amendment to result without at least an implicit promise of reasonable forbearance for some period of time thereafter."

During the existence of an employment contract, some additional sufficient consideration will be required in order to affect a modification, or in exchange for the employee's agreement to non-competition or non-solicitation covenants.

Accordingly, inquiring as to the circumstances under which the contract was signed may evidence an unenforceable contract.

2) Compliance with Employment Standards Minimums

The second most common challenge is to attack termination provisions in contracts for failure to comply with the requirements of the applicable employment standards legislation.

It is well known that parties cannot contract out of the minimal standards prescribed by applicable employment standards legislation[6]. The importance of this should not be overlooked. For example, contract provisions requiring the employer to only pay two weeks' termination pay irrespective of the length of employment, or requiring non-managerial employees to work over-time without pay, for example will not be enforceable. Termination provisions which do not provide for benefit continuance and payment of only statutory minimums have been held to be unenforceable.[7] Recently in Ontario we have seen provisions requiring no payment on a "for cause termination" to invalidate entire termination provisions as failing to meet the statutory threshold of 'wilful

---

[6] *Supra* note 8, s. 5(1) provides:

> **5.** (1) subject to subsection (2) no employer or agent of an employer and no employee or agent of an employee shall contract out of or waive an employment standard and any such contracting out or waiver is void.
>
> (2) If one or more provisions in an employment contract or in another Act that directly relate to the same subject matter as an employment standard provide a greater benefit to an employee than the employment standard, the provision or provisions in the contract or Act apply and the employment standard does not apply.

See also *Machtinger v. HOJ Industries Ltd.* (1992), 91 D.L.R. (4th) 491 (S.C.C.).

[7] *Wright v. Young & Rubicam Group*, 2011 ONSC 4720; *Stevens v. Sifton Properties Ltd,* 2011 ONSC 4720 at paras 55-67

misconduct, disobedience or wilful neglect of duty that is not trivial and has not been condoned by the employer', being the ESA exception, and hence still requires payment.

Accordingly, careful review of the language and knowledge of case law in this area is necessary to assess whether the employee's contract is enforceable

3) Continuity – Material Change to Substratum

Changes in an employee's position at the company can operate to nullify the enforceability of an employment contract[8] if it can be argued that there has been a material change to the substratum (generally a fundamental change in position, compensation and/or passage of significant time) on which the contract was based. While most employers over the years have begun to include a "survival" type of clause which expressly states that the contract will continue in force irrespective of passage of time and change to positions, that is not always the case and whether there is arguably a material change to the substratum of the contract such as to render it unenforceable should also be considered.

4) Fixed-Term Contracts

If the employee presents you with what appears to be a fixed term contract, consideration must be given as to whether or not an agreement is one of a series of employment contracts. Such a series may be deemed to be a hiring of indefinite duration notwithstanding the parties characterization to the contrary[9]. Accordingly, when faced with a fixed-term employment contract it will be important to consider whether this one in a series to determine but whether the terms are enforceable in the case of an employee working pursuant to a prior fixed-term contract. If the contract is one of indefinite hire, the stated termination provision may not be enforceable as typically such provisions will not comply with the employment standards legislation.

5) Employment v. Independent Contractor Relationship

If the agreement signed by your client is in substance an employment agreement and not an "independent contractor" relationship, you may have the ability to negotiate an improved termination package for your client provided the statutory and common law rights as an employee exceeds the contractual entitlement delineated pursuant to the independent contractor relationship. The Courts[10] have applied the following test to ascertain whether the individual is operating as an employee or independent contractor:

Step 1: Determine the *subjective intention* of the parties by written agreement or conduct (i.e. invoices for services rendered, registration for HST purposes, income tax filings);

---

[8] *Wallace v. Toronto-Dominion Bank* (1983), 41 O.R. (2d) 161 (C.A.).

[9] *Ceccol v. Ontario Gymnastic Federation* (2001), 55 O.R. (3d) 614 (C.A.) and *Congregation Beth-Elv. Commission des Relations du Travail*, [2003] J.Q. no 20718 (S.C.).

[10] 1392644 Ontario Inc. (Connor Homes) v. The Minister of National Revenue , 2013 FCA 85 (CanLII)

Step 2: Ascertain the *objective reality* by evaluating whether the facts are consistent with the parties' stated intentions. In essence, the form (the characterization of the relationship) cannot trump the substance.

Where the parties have a subjective mutual intention (by contract or conduct) to characterize a relationship as independent contractor, the Court will then evaluate the factual reality including the following *non-exhaustive* factors:

- level of control over worker's activities (i.e. work procedures and scheduling)
- management and assumption of risk (i.e. any worker loans, investment in capital assets, specialized equipment, operating line of credit)
- opportunity to profit.

(6) Covenants of Non-competition and Non-solicitation

Other than termination provisions, employees require opinions on common law duties and contractual covenants which apply and may confine their activities following the termination or resignation of employment.

Employees in the upper echelons of management owe common law fiduciary duties to their employers both during the course of employment and for a reasonable period of time after the termination of that relationship (this is a common law duty in all provinces except Quebec where it is embodied in the Civil Code).[11] In the employment relationship, this duty, if applicable, includes the duties of fidelity, loyalty, avoidance of conflicts of interests, non-solicitation of staff and clients/customers and following termination, not to unfairly compete with the company. This duty is somewhat limited and dependent upon the context of the employment relationship, the degree of control/influence the employee had over the operation, access to confidential information, participation in strategic planning and so forth. Also, the duration of the duty post termination varies greatly and a large variable is how long the employee was employed by the company. If the employee owes this duty, you must explain the nature and scope of these obligations and provide an opinion regarding permissible and prohibited activities following the cessation of employment.

Many employers seek to protect their interests through various forms of restrictive covenants embodied in employment agreements. The most common varieties are: 1) non-solicitation of employees; 2) non-solicitation of customers/clients; 3) non-competition; and 4) confidentiality. One should review what exists, explain it to the client and ascertain what may require renegotiation or a position that it is not enforceable, in which case some of the same considerations discussed above with respect to termination provisions will also apply.

Confidentiality is a duty generally upheld by courts across Canada without limitation in terms of duration. Confidential information of the employer is considered to be the

---

[11] *Canadian Aero Service Ltd. v. O'Malley*, [1974] S.C.R. 592 (S.C.C.).

property of the employer, and until such information ceases to be confidential, if ever, employees are not permitted to use, disclose or possess this information. It is not their property. This one should be left alone.

Conversely, non-competition covenants are *prima facie* a restraint of trade, contrary to public policy, and therefore void[12]. There is generally a presumption that these covenants are not enforceable. They are considered *prima facie* void as being in restraint of trade. The onus will fall on the employer to show that the protection of a non-competition covenant is required owing to the specific role the individual played with the organization and the knowledge they have such that the needs of the employer could not be protected by a non-solicitation provision.[13] Further, the scope of the covenants needs to be not overly broad in terms of geography, duration and scope. [14] A competitor must be defined as narrowly as possible to reasonably protect the needs of the company. The duration must be reflective of the operational needs and strategic planning of the company and must be proportionate to the duration of the employee's employment, and not extend past two years. The geographic scope is also very important and covenants which operate to prevent employment of the employee in their field of work anywhere in the globe will almost never be enforced. The court may also consider the fairness of the provision generally and refuse enforcement where it is not in the public interest.

In order to be enforced, it is necessary that the non-competition provision(s) be reasonable[15]. Assessing what is reasonable will require counsel to become familiar with the types of classes of employees, the typical restrictions which are sustainable and those which the courts will decline to enforce. A covenant which is broader in geographic scope, longer in duration, or more restrictive in prescribed activities than can reasonably be justified in the particular circumstances of the case will not be enforced. While a detailed review of the case law in this area is beyond the scope of this paper, the Supreme Court of Canada in *Elsley v. J.G. Collins Insurance Agencies Ltd.*[16] set out three general requirements in order to consider enforcement which merit inclusion here:

(1) where the employer has a legitimate propriety interest entitled to protection;
(2) where the duration, breadth of activities and geographic scope of the restraint are not too broad; and,
(3) where the covenant does not create a general prohibition against competition.

---

[12] *Canadian Encyclopedic Digest* (Calgary: Carswell, 1973) Employment Law (Ontario), IV – Written Employment Contracts, 7 – Restrictive Covenants, (a) – General, s. 662.
[13] *Lyons v. Multari*, (2000), 50 O.R. (3d) 526 (Ont. C.A.).
[14] *947535 Ontario Ltd. v. Jex* (2003), 37 B.L.R. (3d) 152 (Ont. S.C.J.).
[15] *Canadian Encyclopedic Digest, ibid.*, Employment Law (Ontario), IV – Written Employment Contracts, 7 – Restrictive Covenants, (b) – Justification for Restrictive Covenant, s. 665; and *American Building Maintenance Co. v. Shadley* (1966), 58 D.L.R. (2d) 525 (B.C.C.A.).
[16] [1978] 2 S.C.R. 916 at para. 19.

In general terms, the covenant should be only as restrictive as is necessary to accomplish the legitimate business objectives of the employer. This will require an individualized assessment based upon the nature of the business, the type of position held and the potential harm which the employee is capable of inflicting by virtue of any breach.

The non-solicitation of clients/customers is one which is more often enforceable. Again, the character of the employee will be relevant and the provision will need to be considered by the court to be reasonable when taking into account the role of the employee with the company and the reasonable needs of the employer. It must also be proportionate in terms of subject matter, duration and geography. For example, it should not extend to the non-solicitation of thousands of clients when the employee serviced only a dozen.

Non-solicitation of a fellow employee is generally considered to be reasonable provided that the duration of the request is reasonable given the context of the employment relationship. The need of an employer to protect against a mass attrition of staff is recognized to be reasonable as it does not operate as an impediment to re-employment by the departing employee. As a result, there is little reason usually for a court to refuse enforcement.

All of this being said, the above are very general propositions only and the context and needs of the individual employer and the role of the particular employee require consideration in each case as to what may warrant negotiation to avoid later dispute and potentially secure a huge advantage for your client in his/her job search.

Employers seeking to employ executives commonly will request the potential employee advise as to whether they are contractually bound by any non-competition or non-solicitation obligations which would impede their ability to accept an offer of employment. If answered in the affirmative, copies of the contracts are commonly requested (or of only the applicable provisions) and legal opinions are often sought by both the prospective hire and the employer at this preliminary stage to determine whether there is a potential problem if the employee is hired. Accordingly, the existence of such a provision may operate as a disincentive to hire someone potentially in violation of the contract even if the courts are unlikely to offer any immediate relief if the employee is hired. Consider the opportunity to negotiate agreement that the provision will not be enforced, or of less onerous terms; it may prove very valuable.

Understanding and explaining to the client what the document requires of them and what your opinion is as to whether or not those provisions are likely enforceable should always be undertaken. However, the client should be warned that even if not enforceable, that does not mean that they could not be wrapped up in long and expensive litigation if the company alleges violation.

STEP 3 – PLANNING OPTIONS

After you have reviewed the relevant facts, assessed the contract as required and provided an opinion to your client, you then need to consider the offer, if any, and what changes you recommend. You should discuss with your client the possible options:

1. acceptance
2. negotiation of possible changes themselves
3. negotiation of possible changes through counsel
4. commencement legal proceedings within the applicable limitation period. You should consider the appropriate forum/venue by ascertaining if the relief sought can be granted by an Employment Standards Officer or if a formal Superior Court proceeding is appropriate

One important element to discuss will be the structure of the proposed settlement and how that will meet or not meet with the employee's plans and needs. Based on that, you will need to provide some further advice as to possible things to consider.

a) New Elements

Consideration should be given not only to the notice period or amount of payment in lieu of notice but to other items that can be added to the negotiation. Frequent additional requests are:

- elements of compensation not provided in the existing package
- pension bridging
- letters of reference[17]
- legal fees
- changes to the terms of non-competition / non-solicitation
- modifications to the release

When discussing settlement of any termination payment, there are also considerations about payment which require consideration beyond whether the monies are lump sum or salary continuance and you should be prepared to deal with other frequent questions and provide appropriate advice.

---

[17] There has not been a single case of liability for the provision of a letter of reference. There has however been liability for the failure to provide one (*Ditchburn v. Landis & Gyr Powers Ltd*., [1997] O.J. No. 2401 (Ont. C.A.)). The lesson – if your client wants one, do not be afraid to ask. There is something positive that can be said about most employees, even those with whom an employer has experienced issues. An employer should focus on the employee's strengths in the letter of reference and the employee requesting the draft reference should stay realistic about the content. It is a good policy that verbal references be given only in accordance with and limited to the content of the written reference.

b) Tax Structuring

This is frequently asked; however, there are few means of reducing the tax which is payable on termination settlements. The employer is required to withhold taxes on all amounts paid as termination and severance pay under applicable legislation or any other amounts payable in that respect as damages for wrongful dismissal paid as a result of common law entitlements. On the one hand, where a lump sum (or installments of a lump sum) is paid by the employer, it may be classified as a "retiring allowance"[18] and subject to flat tax withholdings as follows:

- 10 percent on amounts less than $5,000;
- 20 percent on amounts greater than $5,000 and less than $15,000;
- 30 percent on amounts greater than $15,000.

Such classification will only be permitted, however, if it considered "reasonable" by the Canada Revenue Agency ("CRA") .Therefore, counsel should be wary against providing bold assurances as to how the payment will be treated by the CRA, unless an express opinion on the issue is first sought from the CRA.

On the other hand, salary continuance, with associated benefits and often pension participation, is considered as income from employment and is subject to ordinary withholding rates and subject to all other statutory withholdings such as Canada Pension and EI.

Clients need to understand that amounts classified as a retiring allowance may be subject to further taxation later and are included as income attributed to the employee in the year received. However, receipt of a retiring allowance makes available transfer options to RSP/RRSP as set out below.

Reimbursement for legal fees is permitted and such amounts are not taxable in the hands of the employee; however, the employee will not be permitted to also deduct the legal fees themselves.

---

[18] "Retiring allowance" is defined by the *Income Tax Act,* R.S.C. 1985 (5th Supp.), c. 1, s. 248(1) as:

> **248.** (1) an amount (other than a superannuation or pension benefit) received as a consequence of the death of an employee or a benefit described in subparagraph 6(1)(a)(iv) received:
>
> (a) on or after retirement of a taxpayer from an office or employment in recognition of the taxpayer's long service, or
>
> (b) in respect of a loss of an office or employment of a taxpayer, whether or not received as, on account or in lieu of payment of, damages or pursuant to an order or judgment of a competent tribunal, by the taxpayer or, after the taxpayer's death, by a dependant or relation of the taxpayer or by the legal representative of the taxpayer.

See also Canada Revenue Agency, Interpretation Bulletin IT-337R4, "Retiring Allowance" (1 February 2006).

Attribution of monies to other types of damages should be permitted with great caution. Only when the claim or facts support an independent actionable wrong such as personal injury and human rights damages, compensation for defamation or so forth, should general damages be included in the settlement of an employment matter. To pay general damages which are re-assessed as taxable income unnecessarily exposes the parties to tax liability (the employee for additional income and the employer for failure to withhold).

c) Transfer to RSP or RRSP

Be prepared to advise your client on potential tax sheltering. The only means to protect funds from taxation is for the employee to utilize available contributions in a registered pension plan ("RSP") or a registered retirement saving plan ("RRSP"). Allowable contribution space will be shown on the employee's notice of assessment from the prior tax year. Additional contribution room may be available if the employee was employed with the employer prior to 1996. In that case, additional contributions are permitted within sixty days of the year in which the money is received as income, as follows:

> (a) $2,000 multiplied by the number of years, or partial years, before 1996 which the employee or former employee in respect of whom the payment was made was employed by the employer or person related to the employer; and,
>
> (b) $1,500 multiplied by the number of years, or partial years, before 1989 in respect of which the employer, or a person related to the employer, was making contributions to a registered pension plan or deferred profit sharing plan which has not vested for the employee.

Consideration should be given to these matters and, when appropriate, the client referred to an investment advisor or accountant for determination as to the appropriateness of such a contribution. An appropriate direction will be required to be signed if the client is using such a transfer of retiring allowance monies.

d) Repayment of EI Benefits

Clients frequently ask about when and if they can qualify for EI. If received while a settlement is not yet finalized, EI benefits may trigger repayment obligations. The number of weeks of EI entitlement starts following the time settlement funds from the employer lapse or are exhausted. This happens whether there is salary continuance or lump sum and applies to monies received by the employee, or monies which go into the employee's RRSP/RSP.

As liability for repayment potentially lies with the employer, appropriate inquiries are to be made with Human Resources Development Canada ("HRDC") and repayment made as required by HRDC. Where the employee has in fact received such benefits, the employer will typically require that HRDC be contacted, the particulars of the settlement provided, and the amount of the required repayment determined. This repayment should be made when settling the settlement proceeds.

STEP 4 – OBTAIN INSTRUCTIONS

After you have provided a comprehensive opinion, only then can your client consider the options and instruct you as to what, if anything, he or she then wishes you to do. Employment matters often contain large emotional elements and are also often governed by the practical need for constant and uninterrupted income flow. You need to ensure your client is comfortable with their decision and that you are realistic in all aspects of your opinion and what they can expect. From there you will have a happy client who will refer others in the weeks, months and years ahead.

Nancy Shapiro
Koskie Minsky LLP
900 – 20 Queen Street West
Toronto, ON M5H 3R3

Tel: 416-595-2108
Fax: 416-204-2884
nshapiro@kmlaw.ca

With special thanks to David Silver an associate at Koskie Minsky LLP for his assistance as editor of this paper.