Termination Clause Enforceability: Ontario Court of Appeal Attempts to Clarify Enforceable Termination Clauses in Employment Contracts

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On February 23, 2017, the Ontario Court of Appeal released its anticipated decision Wood v. Fred Deeley 2017 ONCA 158, in which the Court held that contracting out of an employment standard under the Employment Standards Act, 2000 (the "ESA") and not substituting a greater benefit will render a termination clause void and unenforceable. The Court further stated that an employer's conduct upon termination, or during the notice period, cannot remedy an otherwise illegal and unenforceable termination clause. An employee will be entitled to reasonable notice of termination at common law in these circumstances.

The Facts

Fred Deeley Imports ("Deeley"), was the exclusive Canadian distributor for Harley-Davidson motorcycles, parts, apparel and accessories. In April 2007, Deeley hired Julia Wood, as a Sales & Event Planner. Approximately eight years later, Harley-Davidson Canada entered into an agreement with Deeley to buy all of its assets. As a result of the buyout, Deeley immediately informed all of its employees, including Wood, that their employment would be terminated on August 4, 2015.

Wood signed an employment agreement the day after she started working for Deeley in 2007. The agreement contained the following termination clause, which was the main issue in the dispute:

[The Company] is entitled to terminate your employment at any time without cause by providing you with 2 weeks' notice of termination or pay in lieu thereof for each completed or partial year of employment with the Company. If the Company terminates your employment without cause, the Company shall not be obliged to make any payments to you other than those provided for in this paragraph... The payments and notice provided for in this paragraph are inclusive of your entitlements to notice, pay in lieu of notice and severance pay pursuant to the Employment Standards Act, 2000 ("ESA").

Deeley paid Wood her salary and benefits for her 13 weeks of working notice. Deeley also paid her additional compensation, including a lump sum equivalent to eight weeks' pay. Wood commenced an action against Deeley and brought a motion for summary judgment. Her main contention was that the entire employment agreement was unenforceable, and, in the alternative, that the termination clause was unenforceable. She asked for damages equivalent to 12 months' notice of termination.

The Decisions

The motion judge dismissed Wood's motion and held that both the employment agreement and the termination clause were enforceable. However, he also stated that if he was wrong, Wood would be entitled to damages equal to her salary and benefits for a reasonable period of notice. In his view, reasonable notice was equal to nine months.

On appeal, Wood renewed the arguments made on her motion, and raised the following three issues:

1. Whether the employment agreement was unenforceable because it was signed after Wood began working, and she was not provided with fresh consideration;
2. If the termination clause contravened the ESA because it excluded Deeley's statutory obligation to make benefit contributions during the notice period, and did not satisfy Deeley's statutory obligation to pay severance pay; and
3. If the motion judge had erred by fixing the period of reasonable notice at nine months.

In answering the first question, the Court found that a written employment agreement is not unenforceable merely because the employee signs it after beginning to work. A written employment agreement might well be unenforceable if an employer includes in it a material term that was not part of the original employment relationship, but Deeley had not done so in this case.

On the second question, Wood argued that the termination clause improperly excluded Deeley's statutory obligation to make benefit contributions during the notice period (contrary to ss. 60 and 61 of the ESA) and pay severance pay (contrary to ss. 64 and 65 of the ESA). In its defence, Deeley argued that the 21 weeks of combined "notice" and "pay in lieu thereof" provided to Wood following her termination exceeded her entitlements under the ESA and that the termination clause was broad enough to include both wages and benefits.

The Court agreed that Deeley had improperly tried to contract out of the ESA. The Court found that the word "pay" was ambiguous, and that ambiguity in an employment contract had to be resolved in favour of the employee. The word "pay", in this context, referred only to salary or wages, and not benefits or other compensation. The termination clause was also unenforceable because it combined two employer obligations under the ESA, namely to provide notice and to pay severance pay. Under the ESA, Wood was entitled to eight weeks' notice or termination pay, and 8.3 weeks of severance pay. The termination clause provided that she would be entitled to two weeks per year of service, a figure that combined her severance and notice entitlements.

The Court stated that, had Deeley drafted the termination clause to provide separate entitlements to severance and to notice, it would have been enforceable. Instead, by combining them, it created the possibility of three different scenarios: one in compliance with the ESA, the second a violation of the ESA, and a third which could result in either a violation or compliance. From Wood's perspective, this meant that when signing her employment agreement she did not know whether she would receive her statutory entitlement to severance pay when her employment ended. As a result, the termination clause was void and unenforceable.

The Court also added that Deeley's actual compliance with the ESA did not cure the clause's deficiencies because "illegal" termination clauses cannot be remedied after the fact. Consequently, Deeley was ordered to pay damages equal to nine months of reasonable notice at common law.

With respect to the third issue raised by Wood, the Court found that in finding that the period of reasonable notice was nine months, the motion judge took into account the well-established factors: the character of Wood's employment, her length of service, her age, and the availability of similar employment in the light of her experience, training, and qualifications. The motion judge also noted Wood's submission that though her position was “clerical” – she had no managerial duties – her high income together with her age would make it more difficult for her to find a comparable job.

Key Takeaways for Employers

The decision comes as yet another caution in the saga of termination clause enforceability for employers. The three key takeaways can be summarized as follows:

First, any attempt to contract out of or waive a provision of the ESA will render a termination clause unenforceable, even if both parties freely agree to do so. Consideration of including a "saving provision" to ensure compliance with the ESA may help mitigate this result.

Secondly, employers can only contract out of their obligation to provide reasonable notice of termination if they have done so clearly and unambiguously. In this decision, the Court also reviewed the 2005 decision Roden v. Toronto Humane Society O.J. No. 3995 (C.A.). , where a similarly worded termination clause was upheld. The Court distinguished this situation noting that the termination clause in Roden was open-ended and did not close the door to the standards required under the ESA, whereas the all-inclusive language in Deeley's limited its obligation to the payments specified in the termination clause.

Finally, compliance with the ESA after-the-fact is not a remedy for deficient clauses. Although Deeley had provided Wood with the benefits she was entitled to during the notice period as well as a lump sum payment to arguably account for the lack of severance pay, this did not change the fact that the termination clause was deficient and unenforceable.

Employers should pay careful attention to the language of termination clauses in offer letters or agreements as courts continue to signal that they will be looking for ways around them.

By

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