The U.S. tariff effect: Renegotiating terms of employment – Avoiding constructive dismissal risks

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A continuation in our U.S. tariff effect series, a national analysis of the impact of tariffs on Canadian employers. For more information, check out BLG's Tariffs and Trade Resource Centre.

In the face of the changing economic landscape, employers are confronted with difficult decisions. As the impact of the United States' tariffs are being felt across Canada, employers are having to take a hard look at their workforces, and search for ways to reduce their labour costs while maintaining their business activities. At the same time, employers are understandably loath to exit valued employees.

Employers may be considering aggressively downsizing their workforce. However, termination (and mass termination) liabilities can quickly balloon. By making a snap decision to downsize, employers may expose themselves to wrongful dismissal liabilities.

Tariff-related terminations and layoffs: What are your options?

A possible option for employers to avoid or limit terminations and layoffs is making changes to their employees' terms of employment, with the goal of reducing their overhead labour costs while still keeping as many employees on as possible. Employers can make salary and rate cuts, remove or reduce pay rate premiums, change bonus plans, reduce working hours, and stagger working hours. However, changing employees' terms of employment should be done under the advice of legal counsel, and to as limited an extent as possible.

The key concern for employers in making changes to terms of employment consists in avoiding, or limiting, constructive dismissal liability. If changes to an employee's employment result in their constructive dismissal, the employer may end up in the same place as if they outright terminated the employee — that is to say, suddenly on the hook

for common law reasonable notice of termination (or more likely, pay in lieu of the same), and any applicable statutory severance pay.

Constructive dismissal, in the context of a change to employment terms, arises where the employer either makes a fundamental change to a key term of employment, or where the employer's course of conduct demonstrates an intention to no longer be bound by the original terms of employment. The courts tend to be very reactive to changes to compensation, or to an employee's ability to work to earn compensation. Thus, changes to salary, wages, and hours of work are likely to lead to constructive dismissal unless the changes are very minor.

Fortunately, there are two key approaches that can diminish the risk of constructive dismissal claims when varying employment agreements. Employers can either 1) provide employees with consideration for the change, or 2) they can choose to provide notice of the change equal to a given employee's common law entitlement to notice of termination.

Option 1: Consideration for the change

Consideration, in the context of changes to employment agreements, works differently compared to the doctrine of consideration in other areas of the law. The courts are less concerned with the actual value or adequacy of the consideration, and more concerned with the actual presence of consideration in exchange for a change to an employment agreement. Provided that there is some consideration for the change to the employment agreement, the court leaves it to the parties to form their own judgment over its adequacy, and make their own bargain.

The courts have, however, identified what counts as valid consideration in the context of a change to an employment relationship. Consideration must be some kind of new benefit for the employee — merely continuing the employee's employment does not count. Typically speaking, cash, increased vacation entitlements, promotions, increased termination entitlements, and increased benefit coverage each count as valid consideration for a material change to an employment agreement. Salary increases and bonuses also count as valid consideration in this context, although these may be of little utility if the goal is to reduce labour cost overhead. Requested changes by employees may also count as consideration: in one Ontario case, the court found that granting an employee the right to work from home counted as valid consideration for placing the employee on a different employment agreement with new terms.

Option 2: Notice of a change

Alternatively, employers can provide notice of changes to employees, equal to the employees' individual common law notice entitlements. This option can be taken at first instance, or after negotiations for an exchange of consideration for changed employment entitlements if the negotiations are unsuccessful. By giving advance notice of a change, employers can limit their liability exposure to constructive dismissal claims by providing the employee the opportunity to reject the change, while also making it clear that the employee's employment will end at the end of the notice period. It is vitally important that counsel is involved in the determination of the notice period, as well as in the notification of the change.

Practically, notice of a change to terms of employment can be accomplished by providing the impacted employee with a letter outlining the changes, stating that the changes will come into effect at a specific date, and stipulating that if the employee rejects the changes, then their employment will terminate on the noted date. The letter should include a new written employment agreement with the new terms included. Despite an initial rejection, employees should be free to accept the new terms at any point during the notice period, as allowing delayed acceptance preserves the employer's ability to argue, in the event of a wrongful dismissal claim, that the employee failed to mitigate their damages, as it was always open to them to accept the new terms of employment.

At the end of the notice period, the employee's employment will terminate provided that they did not accept the new terms of employment. Any statutory severance pay will become payable at this time, if applicable, and any notice requirements will already be met by the notice the employee was given of the change to the terms of their employment.

Employers need to stick to the notice period in the notification letter. If an employer allows an employee to continue working on their previous terms past the change date, then the court will conclude that the employer has acquiesced to the employee's position, and the new or changed terms are of no impact for the employee's continued employment.

BLG can assist

Employers facing down American tariffs do have some options to reduce labour costs without engaging in layoffs or terminations. If you are considering altering your employees' terms of employment, or considering taking other measures in light of the current unprecedented economic circumstances, lawyers from BLG's Labour & Employment Group are ready to help you and your business navigate through these uncertain times.

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Expertise

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