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employment contract amendments – a landmine for employers

In recent years, a number of our employer clients have faced difficult decisions regarding their businesses. More specifically, many businesses we advise have skilled employees who the employer wishes to retain, but economic circumstances do not justify continued employment on the same contract terms. As a result, many of the most challenging H.R. situations involve navigating the difficult topic of how an employer can implement less favourable employment terms without such changes automatically leading to a lawsuit.

The foundation for any employee contract changes is the concern about potential constructive dismissal claims. In very general terms, constructive dismissal involves situations where employees are "construed" as having been dismissed based on changes implemented by the employer. The legal analysis is focused on an objective test which assesses whether or not the employee is being subjected, when viewed objectively, to a fundamental change to the employment relationship. These changes ordinarily involve two main types: the first are changes to an employee's compensation; while the second relates to fundamental changes to the employee's duties, reporting relationship or responsibilities. In both situations, the risk for employers is that once such a fundamental change is implemented, there is the possibility that, despite the intention of retaining the employee with the company, the employee may be able to resign and claim damages on the same basis to which they would have been entitled had they been dismissed without cause.

The topic has been reviewed in a number of recent court decisions, with many practitioners now having some sense of strategies which may be adopted. In the Ontario Court of Appeals' decision in *Wronko v Western Inventory Service Ltd* (2008) ONCA 327, the employer was faced with the challenge of how to deal with a senior executive's employment agreement which had termination provisions more favourable than the colleague who was superior to him. When Darrell Wronko's boss learned of Wronko's entitlement to two years of compensation on termination of employment, various discussions ensued around what the company intended to do. Ultimately, Wronko was sent a document which asked him to agree to change his termination provision to a maximum of 30 weeks. Wronko refused and advised that he would be prepared to consider a "reasonable alternative" should the company wish to propose one. In response, Wronko was then sent a memo which purported to give him two years' notice of the intention of the company to amend the termination provision in his employment contract to a provision which was essentially the same as the document he refused to sign. Wronko objected over the next two years but continued to work in his same position. Then, two years and four days later, the company sent him a document which it claimed was then his employment contract. Wronko replied that he understood his job to be terminated and did not report to work. He sued for wrongful dismissal and claimed damages for breach of contract, as well as for bad faith, punitice and exemplary damages and unpaid vacation pay. The Ontario Court of Appeal ultimately held that Wronko had been constructively dismissed because the employer's memo with the new agreement indicated that if he was not prepared to accept the new contract, "then we do not have a job for you", which was effectively notice of termination.

The decision in *Wronko* confirms that there are essentially three options available to an employee when an employer attempts to make a unilateral amendment to a fundamental term for contracted employment. The options are as follows:

1. The employee accepts the change, either expressly or implicitly, in which case the employment would continue under the altered terms.

2. The employee may reject the change and sue for damages. In these instances, the rejection is essentially immediate and constructive dismissal ensues. An example of this is the leading case of *Farber v Royal Trustco* [1997] 1 SCR 46 where the employee was advised that he would be required to accept a demotion, but he refused and successfully claimed constructive dismissal.

3. The employee may make it clear to the employer that he or she is rejecting the new term. The employer is thus able to respond to this rejection by deciding whether or not to terminate the employee with proper notice. If the employer does not take this course and essentially permits the employee to continue to fulfill his or her job requirements, then the employee is entitled to essentially insist on adherence to the terms of the original contract.

Wronko found himself in the third situation, where his "steadfast opposition" to the revised terms was clear and not challenged by the employer. Thus, when they saw that he was not prepared to accept the revised agreement, the employer effectively had the choice to advise that the employment was going to be terminated (as opposed to amended) two years hence. The failure to do this in September 2002 when he was instead given the two years notice of the change meant that he was essentially continually employed on the same initial terms he had prior to the contract provision coming to the attention of the supervisor.

In a more recent decision which applied the framework above, Lorenzo Russo successfully sued his employer of 37 years, Kerr Bros. Limited, for damages which arose while he remained employed by the company. In other words, because the employer had unilaterally made contract changes to Russo's employment (decreases in compensation), he had a valid claim for constructive

dismissal. However, since he decided to remain employed at the reduced salary, the claim which Russo pursued successfully at trial was for the wage differential during the period of reasonable notice. In its decision in *Russo v Kerr Bros. Limited* (2010) ONSC 6053 (Ont. SCJ), the Court focused on the fact that there had been "a fundamental alteration in the terms and conditions of employment as a repudiation of the contract", or, to use the current terminology, it amounted to constructive dismissal.

Russo was prepared to accept the alterations to the terms and conditions of his employment as a repudiation or constructive dismissal, but had the right to remain in his employment under the new terms in order to mitigate his damages. As the Court noted, once the employer, Kerr, had been told that the plaintiff had accepted that a constructive dismissal had occurred and that he did not accept the new terms and conditions, Kerr could have told the plaintiff to leave the workplace, in which case, he would have been paid an amount on account of reasonable notice commencing at that moment.

These types of situations are arising with increasing frequency and can be very costly, particularly since the costs of training and orienting employees can be quite substantial. Further, many employers have cyclical businesses where they have a reasonable prospect that the amount of work will ultimately increase as economic conditions improve, but requires flexibility in the short term allowing them to adjust compensation levels given fluctuating conditions.

We offer the following recommendations to employers who are looking to minimize their exposure to damages for potential changes to employee contract terms:

1. Prepare contracts at the outset of employment which contain broad provisions which allow duties to be amended.

2. Document, in writing, the specific changes that will take effect on a certain future date.

3. Provide a significant period of working notice of amendments to employment contract changes, with employees signing back agreement to such changes, but avoiding language providing for termination for failure to sign.

4. If amended contract terms are not acceptable to the relevant employee, make a clear decision that the employee will either be retained on the old terms or terminated based on the refusal.

5. In appropriate circumstances, retain employees or contractors on defined term agreements (e.g, one year increments), which can then be amended as required when new terms are negotiated.

6. Provide employees with an appropriate form of compensation (such as a signing bonus, options or an increased vacation entitlement) in exchange for any required contract changes.

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a cautionary note