OMHRA Ontario Municipal Human Resources Association

BONUS ENTITLEMENT DURING THE PERIOD OF REASONABLE NOTICE – *YES, NO, MAYBE…*

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Employers recognize an employee dismissed without cause is entitled to notice of dismissal (or pay *in lieu* thereof). What many employers do not realize is that under statute and common law, the employee is entitled to any bonus during the applicable period of notice as if she had continued to work; the principle being the employee should be put in the same position she would have been had she continued to work to the end of the notice period. However, this principle can be modified through express contractual terms.

There are three kinds of potential bonus entitlement upon termination: 1. "Accrued" or "vested" relating to a period already concluded but not yet paid; 2. *Pro-rata* or stub relating to a period in which an employee is terminated part-way; and 3. Prospective entitlement in respect of a future employment period (*i.e.,* notice period).

Many employers spend hours drafting terms and conditions of a bonus plan, but are silent on what happens upon termination or resignation. Some employers import bonus plans from affiliates in other jurisdictions, such as the United States, which generally do not have the necessary language to limit entitlement in Canada. Others try to manage exposure by characterizing a bonus as "discretionary". Savvy employers may require the employee be "actively employed" at the time the bonus is paid out, or not include any notice period in the calculation of service for the purpose of the bonus plan.

While the language of the bonus provision is important, a court will be influenced by the perceived fairness of the result to the employee. Consider two recent decisions with very different outcomes. In ***Lin v Ontario Teachers' Pension Plan Board***[1] Justice Corbett awarded a dismissed investment professional a substantial bonus on account of a period prior to dismissal and also in respect of the reasonable notice period subsequent to dismissal.

The plaintiff, Mr. Lin, had worked for the Ontario Teachers' Pension Plan Board (the "OTPPB") for eight years and was 41 years old at the time of his dismissal, allegedly for cause. Justice Corbett determined the allegation of cause was not supported and, in the absence of a contractual termination provision, awarded Mr. Lin reasonable notice of fifteen (15) months.

During his employment, Mr. Lin was entitled to two types of bonus - a short term Annual Incentive Plan (AIP) and a Long-Term Incentive Plan (LTIP). The AIP comprised more than half of Mr. Lin's annual income. The fiscal year for the employer was the calendar year and bonus amounts were typically paid out in April after the end of the calendar year.

Mr. Lin was terminated in March of 2011, before the bonus for 2010 was paid out but after fiscal 2010 was completed. He sought an award in respect of the AIP and the LTIP for three distinct periods: January to December 2010; January to December 2011, which would have been paid in April 2012 (inside the 15 month notice period); and January 2012 to June 2012, a stub-period reflecting the balance of the notice period, to be paid out in April 2013 (outside the notice period).
A year prior to Mr. Lin's dismissal, the OTPPB implemented a change to the language of the bonus plans, introducing a requirement that to be eligible for payment an employee had to be actively employed at the time the bonus is paid out. This was a material change to Mr. Lin's employment agreement to which he refused to consent (together with other colleagues), and for which OTPPB did

[1] 2015 ONSC 3494

not continue to pursue its request for written agreement. Under the strict terms of the amended language Mr. Lin would not be entitled to a bonus for 2010 or any period thereafter.
Justice Corbett decided in favour of Mr. Lin on three grounds:

- First, he relied on a frequently followed case, *Schumacher,*[2] in which the court held, where a bonus is an integral part of an employee's remuneration[3] and the employee is terminated without cause, she is entitled to the bonus she would have earned during the period of reasonable notice, and any requirement to be 'actively employed' at the time of payout is unfair. To this end, Justice Corbett gave significant weight to the fact the AIP was more than 50% of Mr. Lin's annual income, and the employer's past practice of paying out the AIP amounts in other terminations.

- Second, Justice Corbett determined the limitation language was not valid in the first place because it was a significant change to the bonus plan to which Mr. Lin had refused to consent. Thus, while the revised AIP might have had the appropriate language to limit entitlement in line with previous decisions [4], without Mr. Lin's agreement, such a change could not be imposed unilaterally. Further, as OTPPB did not pursue its request for written agreement to the change, this "abandonment" was "reasonably interpreted by Mr. Lin as a decision by [OTPPB] not to pursue these changes."

- Third, Justice Corbett held that even if he was wrong in respect of the above, he considered the limiting language to be an unenforceable "penalty clause". A court may grant relief from a penalty clause when it functions more like a punishment than a genuine estimate of damages suffered. Because an employee is entitled to compensation for work done, enforcing the limitation language would unjustly enrich an employer at the expense of an employee.

It is significant to note there is no explanation from Justice Corbett as to why the concept of unjust enrichment should apply to the period during which no work is performed. It will be interesting to see whether the penalty clause analysis is followed in future wrongful dismissal decisions.
Another recent decision, released less than two weeks after *Lin*, is ***Kielb v National Money Mart Company***[5].

Mr. Kielb was a lawyer working in-house for National Money Mart Company. He had been employed for roughly 18 months when his employment was terminated without cause. An issue was Mr. Kielb's entitlement to a Key Management Bonus ("KMB"). The fiscal year for Money Mart was July 1st through June 30th and Mr. Kielb was terminated in April 2010. Money Mart's KMB had clear language stating the bonus was "discretionary", "did not accrue" and "is only earned and payable at the time it is provided to you by the Company". The language also included examples of timing to illustrate an employee was not entitled to any bonus amount if she was not employed at the time of payment, even if she had been employed at the end of the relevant period.

The KMB for 2010 (July 1, 2009 to June 30, 2010) would have been paid in September 2010 at 59.4% of salary. Mr. Kielb was terminated in April 2010, before the end of the fiscal year and before the time of payment. Even considering Mr. Kielb's contractual notice entitlement of eight weeks, he would not have reached the end of the fiscal year or the time of payment.
Despite concluding the KMB *was* an integral component of Mr. Keilb's compensation, and a key negotiating point prior to his accepting the position, Justice Akhtar upheld the limiting language and

[2] *Schumacher v Toronto Dominion Bank* (1997), 147 DLR (4th) 128 (Ont Gen Div), aff'm [1999] 120 OAC 303
[3] In *Schumacher*, *supra* note 2, the bonus varied, but was generally two or three times Mr. Schumacher's base salary.
[4] See *e.g., Duynstee v Sobeys Inc.* 2013 ONSC 2050; *Love v Acuity Investment Management Inc.*, 2011 ONCA 130; *Kieran v Ingram Micro Inc.* (2004), 189 OAC
[5] *Kielb v National Money Mart Company,* 2015 ONSC 3790

did not award Mr. Kielb any damages for the KMB. To this end, Justice Akhtar considered the following factors to be significant:

- The limiting language in *Kielb* was far more clear than the language from cases such as *Schumacher*.
- Mr. Kielb's contractual termination entitlement still would not have taken him to the end of the fiscal period or the qualifying date.
- Mr. Kielb was a lawyer and the employment contract had been negotiated back and forth on several items.
- Mr. Kielb knew the impact of the limiting language and nevertheless signed the contract.
- There was no public policy reason to disregard the clear wording of the limitation language.

The decision can be seen as a positive decision for employers. The court upheld clear language requiring active employment on the relevant payment date as a valid requirement to receive a bonus. Mr. Kielb fell short of the relevant date thus the necessary condition was not achieved. However, the significance of Mr. Kielb's status as a lawyer and the fact the contract was bilaterally negotiated are key factors that cannot be ignored.

Lessons for Employers

Kielb affirms the principle that an employer can limit bonus entitlement on termination by using clear, unambiguous contractual language (perhaps with examples), even when the amount is a significant component of compensation. However, when read with *Lin*, the caution is clear - the language must be contractual, not aspirational.

An employer utilizing a bonus program as a component of compensation, particularly where the bonus is a significant portion of the overall package, is well advised to consult with experienced employment counsel on the impact of a termination or resignation on entitlement, and the drafting of the contract itself.

To learn more and for assistance drafting bonus and other contractual language to protect your organization, contact a member of Sherrard Kuzz LLP.

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