Legal Update

Employment contracts: invaluable protection against costly severance claims

by Thomas Gorsky, LLB

EMPLOYERS ARE OFTEN CONFRONTED WITH DIFFICULT DECISIONS — BUT GENERALLY NONE SO DIFFICULT AS A DECISION TO TERMINATE EMPLOYMENT. OF THE TERMINATION-RELATED ISSUES WHICH COMMONLY ARISE, THE COST OF TERMINATING EMPLOYMENT IS AT THE FOREFRONT. EMPLOYERS WITHOUT EXPERIENCE IN SUCH MATTERS MAY BE SURPRISED TO LEARN HOW HIGH THE COST CAN BE. FORTUNATELY, THERE ARE EFFECTIVE STRATEGIES TO AVOID EXPOSURE TO LARGE CLAIMS.

Termination Obligations Include Statutory And Common Law

One obligation on termination — an obligation almost every doctor's office or medical clinic will be required to follow — is the statutory obligation under the Employment Standards Act to pay termination pay. Statutory termination pay is required in the vast majority of terminations. Exceptions to this requirement are rare, the most common being serious and intentional employee misconduct. Thankfully, the maximum liability which accrues for statutory termination pay is eight weeks' pay and continuation of benefit plan contributions, and that level of liability is not reached until an employee attains eight years of service.[1] The Employment Standards Act termination notice obligations cannot be circumvented.

Another termination obligation which may arise is the implied obligation to give "reasonable prior notice of termination," or alternatively, to make payment "in lieu of notice." That obligation arises at "common law" — judge-made law developed by courts through the tradition of following prior legal precedent.

When a judge decides how much to award at common law, a number of different factors are taken into account, the most significant being length of service. The amount of notice required to be given will increase as length of service increases. In the absence of a contract limiting the entitlement to common law notice (addressed below), the obligation to provide such notice (or pay in lieu) arises whenever a termination occurs without just cause.

Even when the workplace is closing down for a legitimate business reason — for example, as in the case of a doctor retiring and/or transferring his or her practice to another doctor who is not taking over the existing employees — the law requires the departing employees to receive their common law notice. In extreme cases, liability can be as high as 24 months' pay in lieu of notice.

There is a critically important distinction between the statutory obligation under the Employment Standards Act, and the obligation at common law. While courts do not permit employers to avoid the obligation to pay statutory termination pay, they do allow employers to regulate the common law obligation by contract.

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Employment Contracts Can Substantially Reduce Liability

A properly drafted employment contract can reduce or even eliminate a doctor's common law obligations. For example, a contract can validly limit an employer's obligations to the requirements of the Employment Standards Act. If an

employer wishes to be more generous, there are contractual formulas which can be used to accomplish this.

Although termination clauses are the principal reason for using employment contracts, they are not the only reason. Employment contracts serve an important role in clarifying obligations and entitlements during the course of the employment relationship. A well-prepared employment contract will set out remuneration, probationary period, duties of employment, hours of work, vacation, confidentiality obligations, etc.

The optimal opportunity for an employer to realize advantages from an employment contract is at the time of hiring. However, there are important technical rules which must be followed, or an otherwise valid contract can be invalidated. In order to take advantage of an employment contract, it should be presented before arriving at any form of agreement with the employee, and not afterward. Even a "handshake agreement" in which salary, position and start date are agreed upon, can mean that it will be too late to subsequently present a written agreement incorporating a termination clause. This is due to the legal requirement that employment contracts have "consideration" (i.e., in return for an employee giving up common law rights on termination, the employee must receive something of value in return). An offer of employment is considered valid consideration. However, if there is already a binding offer and acceptance of employment (a handshake can be legally binding), then it may be too late to insert an enforceable termination clause into a written contract.

Although it is preferable to use an employment contract with a termination clause at the time of hiring, all is not lost for doctors who may not appreciate their importance until after hiring has taken place. In situations where a valid termination clause has not been utilized at the time of hiring, opportunities may arise during the course of an employment relationship. Such mid-employment opportunities will involve an offer of fresh consideration, in exchange for an employee accepting revised terms of employment, including a termination clause. This can take place if a raise is being offered, or a benefits plan is being added, etc.

Human Rights Claims Cannot Be Avoided By Contract

Although employment contracts provide invaluable protection to employers, it should be appreciated that they do not protect an employer against claims arising out of violations of statutory obligations. For example, if employment is terminated due to unlawful discrimination, or there is a refusal to allow an employee to return to work after maternity leave, even the most well-drafted employment contract will not provide an employer with a defence to a claim.

Judges Have Strict Requirements

The benefits to an employer of a properly drafted employment contract are significant, and there are really few if any downsides. One mistake some employers make is to attempt to draft a contract on one's own, or use a document found on the Internet. This is to be discouraged, as there are many pitfalls which can lead to an invalid termination clause. Judges tend to be employee-friendly. They are not eager to find that an employee has been effectively prevented from pursuing a common law claim, and are receptive to technical arguments supporting invalidity of a contract. Therefore, an employer is well advised to ensure that any employment contract being entered into has been drafted or reviewed by a qualified lawyer. ■

Reference

1. In some cases an employer might be obliged to pay more than eight weeks, but for most employment by medical professionals, the maximum will be eight weeks' pay.

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