Employment Contracts: Good Idea? Bad Idea?

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In our practice we have seen a sharp increase in the number of employers who are asking new and sometimes existing employees to sign employment contracts, usually drafted by the employer or someone on their behalf. Often the contracts are 'generic' - by which I mean they are intended to be used with respect to a number of different types of employees, with different positions and responsibilities.

Employers often want to have employment contracts in place in order to limit the notice to be provided to employees on termination to the minimums set out in employment standards legislation or to otherwise establish a pre-determined amount of notice or pay in lieu of notice that will be provided upon termination.

The Common Law Obligations

If there is no written contract and the employees in question are not unionized, the employment arrangement in Canada is governed by two main factors. The first are whatever statutory conditions apply in the particular jurisdiction. The second, except for employees in Quebec, is the common law. All jurisdictions in Canada have employment standards statutes.

The provisions of these statutes apply to all employees and set minimum standards that must be met in both individual contacts of employment and in collective agreements. Parties are free to negotiate and implement better terms and conditions, but cannot contractually provide for terms and conditions that are less than the applicable minimum standards.

The common law in all jurisdictions, except Quebec, sets default conditions that are deemed to be in every contract of employment where there is no other contract in place.

In the not too distant past it was unusual for employees other than senior executives to have written employment contracts. However, over the last twenty years or so, the common law 'default' or implied terms have become more widely known and many employers have sought to

quantify and/or reduce the rights employees have at common law when terminated and in so doing to provide certainty to employer and employee alike.

At common law, an employee can only be terminated 'for cause' if he/she breaches a fundamental term of the employment contract in a material way. It is often very difficult to assess whether a particular act or omission will constitute cause at law. Many cases before the courts deal with just this issue.

A termination for reasons of lack of business or financial hardship of the employer is not just cause. A termination for other than just cause requires the employer to give the employee to be dismissed 'reasonable notice' or pay in lieu thereof. For long term employees, 'reasonable notice' can be many months - or in the case of very long employees - two years or more. By contrast, the minimum notice required in Ontario for employees with long service is eight weeks and severance pay is only payable for Ontario-regulated employers if their payroll exceeds 2.5 million and the employee's service exceeds five years. Coupled with this is the fact that 'reasonable notice' in any particular case is often subject to argument, and one never knows precisely what a court will allow until a judgment is rendered.

Thus, employers have an incentive to quantify and/or set out their obligations by drafting employment contracts which provide stated notice periods - often the minimums the employment standards legislation will allow.

<u>The Risks:</u>

There can be significant risks with respect to drafting employment contracts which employers both need to be aware of and deal with appropriately:

1. Offending Employment Standards Legislation:

Often employers will neglect to provide language which insures that an employee will obtain ALL PAYMENTS AND BENEFITS to which they are entitled under the relevant employment standards legislation. For example, in Ontario, if an employer is provincially regulated, they are required to not only provide the minimum notice under the *Employment Standards Act, 2000*, but must also provide all regular benefits during that period of notice. Just providing pay in lieu of notice is not enough. In addition, an employer in Ontario may also have a severance pay obligation. If the termination clause does not meet these minimum requirements, it is likely to be struck down and replaced with the common law obligations.

2. The Obligation to Mitigate:

The common law requires a terminated employee to try to find alternative employment to mitigate their damages. Thus, an employee who obtains alternative employment quickly will reduce the damages owed to him/her by the employer. However, if a contract of employment substitutes a contractual notice period for the common law notice period, that contract MUST INCLUDE a duty to mitigate on behalf of the employee. If it does not, the employer will likely be

required to pay whatever notice pay is set out in the contract even if the employee has been able to entirely mitigate their damages by securing another job. A very recent case had a fixed term contract that was terminated before the end of the term. The employer in that case was required to pay the employee damages for the remainder of the entire term notwithstanding the fact the employee had immediately obtained alternative employment at a higher salary.

3. *Contra Proferentem*

At law, if the contract is drafted by one party and there is any ambiguity to any of its terms the ambiguity will be interpreted by the courts contrary to the interest of the party that drafted it. This is almost always the employer. It is often difficult to think of all conditions that will apply to an employment contract when it is drafted. Therefore, great care must be taken in the drafting to insure there are no such ambiguities.

4. Old Employee - New Contract

Often employers want to impose a new or different contract on existing employees to quantify the employer's obligations. This is an inherently risky venture. Promising continued employment is NOT valid consideration for the new contract. Employees who are effectively forced to sign new conditions of employment can simply claim lack of consideration - the result of which is the new contract is void. To have a valid new contract with an existing employee there must be a voluntary acceptance of the new terms by the employee coupled with real consideration - a payment, a new (really new) position, a real promotion or other actual improvement to the contract.

5. New Rules after the Contract Signed

The one thing that is constant in employment law is change. Ontario is currently drafting amendments to many employment-related statutes. What complies with the law today may not comply tomorrow. Thus, any employment contract needs to be drafted so as to comply with changes in standards - or new standards - that may be introduced in the future.

6. U.S. Precedents

Often companies that are owned or affiliated with U.S. based entities try to use precedents from the U.S. in their Canadian employment contracts. The laws and standards in the U.S. are entirely different from the laws in Canada - and are based on fundamentally different principles. DO NOT use American precedents; they simply do not comply with Canadian law.

<u>Conclusions</u>

Employment contracts, when properly drafted can quantify and clarify the rights and obligations of both the employer and the employee. If done properly, they can reduce obligations to employees on termination from what they would otherwise be entitled at common law. They can also provide some protection to employers with respect to employees who wish to make use of confidential information after leaving their current employment, or improperly take advantage of

contacts they made while employed. However, this area of the law is complicated and changing. If you want to use employment contracts in your business, make sure you get competent advice about what you can and cannot include.