Silver Linings: Court of Appeal Upholds Clause Limiting Bonus Entitlement on Termination

By Landon Young and Amanda Boyce

Recent Canadian jurisprudence has been quite unfavourable on the issue of liability for bonuses payable after termination of employment. Where employees are entitled to bonus payments during their employment, entitlement to such amounts after termination can be part of their entitlement to pay in lieu of reasonable notice under the common law. A recent case from the Ontario Court of Appeal illustrates that, despite this disappointing trend, the courts will enforce lawful bonus provisions that are drafted clearly and unambiguously.

Backgrounder on Bonus Clauses

Where bonuses are non-discretionary, integral components of compensation, they are generally recoverable in actions for wrongful dismissal. This is because, barring enforceable contractual agreements to the contrary, employees are entitled to recover for the total contractual compensation they would have otherwise received during the notice period (or the notional notice period, if pay in lieu of notice is provided instead).

Where a bonus is truly discretionary, employees may be disentitled from receiving bonus payments after they are dismissed under certain circumstances. For example, in one recent case, an employee's contract stated that he was "entitled to participate" in the employer's bonus plan; however, the bonus plan was not based on any sort of formula, and the contract did not guarantee the amount of his bonus. The owner decided the amount every year based on a number of factors. As such, the bonus plan was completely discretionary. In that case, the employee was an under-performer. The employer was able to prove that it would not have awarded him any bonus that year, even if he had still been actively employed.

Where bonus plans are not discretionary, it is possible to limit an employee's entitlement to receive such bonuses after termination. However, recent decisions from the Ontario Court of Appeal illustrate that this requires the use of clear, unambiguous language, and is difficult to do in practice.

When an employee claims an amount in respect of her bonus on a claim for wrongful dismissal, she is not claiming the bonus payment itself. Rather, she is seeking contractual damages for the bonus income she would have received during her reasonable notice period had she not been wrongfully dismissed.

As such, the Ontario Court of Appeal noted in Paquette v TeraGo Networks that courts must first consider the common law right to damages for breach of contract, and second, whether the terms of the plan alter or remove a common law right.

The Court in Paquette noted that a term requiring an employee to be "actively employed" on the date of the bonus payout is not sufficiently clear, by itself, to limit an employee's common law entitlements. This is because, according to the Court, employees have a contractual right to work during the notice period, and to be paid their salary and any other benefits. If the employer had not unlawfully breached the contract by terminating the employee without notice, he would have been "actively employed" on the bonus payout date.

The Court refers to its own jurisprudence for the proposition that, "the parties must be taken to have intended that the triggering actions…would comply with the law in the absence of clear language to the contrary". Where the triggering event for a loss of bonus entitlement is termination, it is to be presumed that the termination is lawful (i.e. with reasonable notice).

Although it does not say so definitively, the Court seems to suggest that in order to be sufficiently clear and unambiguous to trigger a cancellation of an employee's right to a bonus, a limiting clause would need to specify that the loss of bonus entitlement is triggered by the termination of the employment contract *without just cause and without reasonable notice.*

In another recent bonus entitlement case, the Alberta Court of Appeal found that a requirement of "active employment", where the contract specified that a period of reasonable notice did not qualify as "active employment", was sufficiently clear and unambiguous. The Court found that the contract, "left no doubt as to whether the participant had to be actively employed on the vesting date. It also left no doubt that any period of "reasonable notice" required in lieu of notice of termination did not qualify as "active employment"".

The Case

In Kielb v. National Money Mart Company, the employee was terminated without cause approximately five months before the bonus pay-out date for that year. The trial judge found that a non-discretionary bonus was an integral part of the employee's compensation.

In upholding the trial judge's ruling that the employee was not entitled to the bonus payment, the Court of Appeal noted that the employment contract also contained a limitation clause that provided that the bonus did not accrue, and was only earned and payable on the pay-out date. The employment contract also contained a termination clause which limited the employee's entitlements upon termination to the statutory minimum. The bonus clause further stated as follows:

> For example, if your employment is terminated, with or without cause, on the day before the day on which a bonus would otherwise have been paid, you hereby waive any claim to that bonus or any portion thereof. In the event that your employment is terminated without cause, and a bonus would ordinarily be paid after the expiration of the statutory notice period, you hereby waive any claim to that bonus or any portion thereof.

Section 60 of the Ontario Employment Standards Act ("ESA") prohibits employers from reducing an employee's wage rate or altering the terms and conditions of employment during the statutory notice period. The Court of Appeal found that the clause was not ambiguous when read in its entirety, and that it did not contravene the ESA. If the bonus pay-out date fell within the employee's statutory notice period, the clause made clear that the employer would have paid it out.

The termination clause also provided that a defined amount of additional pay in lieu of notice, above the ESA minimum, would be provided in exchange for a signed release. The employee declined to sign a release, and so was not given the additional notice under that clause.

The Court of Appeal remarked, in addition, that even if the employee had signed the release and accepted the additional six weeks, the bonus pay-out date would still have been outside of the extended notice period. The employee would still not have earned or have been eligible to receive the bonus payment under the terms of his employment contract.

The employee had the chance to earn a significant bonus. Although the outcome for the employee was seemingly harsh, the Court of Appeal upheld the trial judge's ruling that, "Public policy would be ill served by permitting the plaintiff to accept a potentially lucrative position with the full knowledge that it contained a potentially unfavourable limitation clause and then to complain when that clause was actually executed."

The Takeaway

Employers should be encouraged by the Court of Appeal's ruling in this case, but should also remain conscious of the two other recent cases wherein the Ontario Court of Appeal found that clauses requiring "active employment" were insufficient to disentitle employees to bonus payments after termination. Of course, in those other cases, unlike this one, the bonus would have been payable during the common law reasonable notice period found by the courts.

Interestingly in this case, the employee did not challenge the enforceability of the termination clause in his employment contract which limited his entitlements upon termination to the statutory minimum at trial. As such, he was prevented from raising this argument on appeal.

Had this clause been found to be unenforceable, the employee would have been entitled to reasonable notice under the common law. Although he was a relatively short service employee, it is plausible that such common law notice period would have been long enough to encompass the bonus pay-out date. If that were the case, the court would likely have found the bonus to be payable, based on the jurisprudence discussed above.

This underscores the need for employers to seek legal advice when drafting employment agreements, especially when including such limiting language. The courts have clearly indicated a willingness to rule against employers where there is any ambiguity.

It is also imperative to take a holistic view of the employment agreement. In this case, a faulty termination clause could have jeopardized the effectiveness of the bonus limitation clause. Employment counsel are uniquely positioned to draft agreements that avoid such pitfalls.

Courts are often sympathetic to employees, especially where a similar 'zero-sum game' is involved. In finding that the bonus limitation clause was not contrary to public policy, the trial judge considered that the employee was a lawyer, and that he had re-negotiated several terms of his employment contract, but did not raise his concerns about the limitation clause. The result in this case may have been different if the employee had been less sophisticated.

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