LAVERY, DE BILLY
BARRISTERS AND SOLICITORS

Suite 4000
1 Place Ville Marie
Montréal, Quebec
H3B 4M4
Tel. : (514) 871-1522
Fax : (514) 871-8977

Suite 500
925 chemin St-Louis
Québec, Quebec
G1S 1C1
Tel. : 1-800-463-4002
Tel. : (418) 688-5000
Fax : (418) 688-3458

Suite 500
3080 boul. Le Carrefour
Laval, Quebec
H7T 2R5
Tel.: (514) 978-8100
Fax: (514) 978-8111

20th Floor
45 O'Connor Street
Ottawa, Ontario
Tel. : (613) 594-4936
Fax : (613) 594-8783

Web site: http://www.laverydebilly.com

Associated Firm:
Blake, Cassels & Graydon
Toronto, Ottawa, Calgary
Vancouver, London (England)

REORGANIZATION OF A BUSINESS AND CONSTRUCTIVE DISMISSAL: THE *FARBER* CASE[1]

In the current economic context, more and more businesses are forced to carry out administrative reorganizations in order to maintain a competitive position in their respective markets. The rationalization of operating costs and the maximization of revenues often lead to major changes in the hierarchical structure of a business and, consequently, in the work conditions of certain employees.

Are the employees affected by such a reorganization bound to accept the new position being offered to them? And what if, as if often the case, the position in question is less well paid than the old position, or simply less prestigious? What are the consequences for the employer of a refusal by the employee to accept the imposed changes? On March 27, 1997, the Supreme Court of Canada rendered an important decision regarding the notion of “constructive dismissal” in civil law as it applies in the context of a business reorganization, and regarding the damages to which one may be entitled following such a dismissal.

THE FACTS

David Farber had worked for the Royal Trust Company (hereinafter the “Company”) since 1976. Starting off as a real estate agent, he rapidly moved up in the company ranks and, as a result, in 1983, he held the position of regional manager for Western Quebec. In this capacity, his work consisted of supervising more than four hundred real estate agents and administering twenty-one offices having sales which that year exceeded sixteen million dollars. In 1983, Mr. Farber’s total remuneration was one hundred and fifty thousand dollars.

[1] *Farber* v. *Royal Trust Company*, Supreme Court of Canada, nº 24885, March 27, 1997.

Summary

The facts 1
The Superior Court and Court of Appeal Decisions . 2
The decision of the Supreme Court 2
Conclusion 3
Recent changes to the Labour Standards Act 4

In June 1984, as part of a major restructuring, the Company decided to eliminate certain regional management positions, including that of Mr. Farber. In lieu of his now eliminated position, the Company proposed that Mr. Farber should reassume a former position as manager in an office of approximately twenty real estate agents. The conditions associated with this position did not include a guaranteed salary and the office in question was one of the least profitable in the province. However, the Company added financial compensation to its offer, including in particular a relocation allowance of forty thousand dollars. Unsatisfied with this offer, Mr. Farber sought to negotiate with the Company, which refused to improve it. Mr. Farber eventually brought an action in damages against the Company alleging that he had been "constructively dismissed".

THE SUPERIOR COURT AND COURT OF APPEAL DECISIONS

At first instance, the Superior Court dismissed Mr. Farber's action. Justice Flynn carefully examined the terms of the offer made to Mr. Farber in light of the subsequent facts and decided that the offer was adequate and reasonable both in terms of the remuneration and the prestige associated with the position offered.

On appeal, the majority of the Court was of the opinion that the judge at first instance committed no patent error in deciding that the offer was reasonable and that in the absence of such an error, it should not intervene. Justice Fish dissented, being of the opinion that Mr. Farber had in effect been constructively dismissed.

THE DECISION OF THE SUPREME COURT

- **The Notion of "Constructive Dismissal"**

Justice Gonthier, writing for the Court, first recalled the principle according to which a party to an employment contract can unilaterally terminate such a contract by giving the other party reasonable notice thereof. The termination is considered a dismissal if it originates from the employer, and a resignation if it originates from the employee.

Proceeding then with an analysis of the notion of "constructive dismissal", the country's highest court explained that where the employer unilaterally decides to make substantial changes to the essential terms of an employee's employment contract, and where the latter does not agree with such changes and decides to leave his or her employment, this departure does not constitute a resignation but rather a dismissal. In such a case, and in view of the absence of an official dismissal by the employer, the situation is characterized as a "constructive dismissal". In other words, where the employer substantially changes the essential terms of the employment contract, it is in effect no longer fulfilling its obligations and repudiating the contract. Upon this "breach of contract", the employee can therefore leave the business and claim compensation in lieu of notice, as well as damages where appropriate.

In order to determine whether, in a given case, an employee was constructively dismissed, the Supreme Court of Canada proposes the following test: the judge must assess whether, at the time the offer was made, a reasonable person in the same situation as the employee would have

considered that this constituted a substantial change to the essential terms of the employment contract. In this regard, Justice Gonthier stated that the fact that the employee is prepared to accept the proposed change in part is not conclusive. Justice Gonthier also added that it is not necessary for the employer to have intended to force the employee to leave his or her employment or to have been in bad faith. In the latter case, however, damages may be awarded to the employee who suffered from such bad faith.

- **Substantial Changes to the Essential Terms of the Employment Contract**

Although Justice Gonthier was careful to emphasize that in the area of constructive dismissal each case is fact-specific, and that it is necessary to examine the particularities of each contract and of each situation before reaching a conclusion, it is interesting to note the practical examples cited by the Supreme Court on the notion of a substantial change in the terms of employment. In this regard, the Court was inspired both by examples from the French civil law and by the rules of the Canadian common law provinces (the rule on the subject being the same). The Court indicated in particular that a significant salary reduction, or a change in the manner of calculating the salary, or a demotion combined with a decrease in pay or a reduction in status or prestige may be regarded as changes to the essential terms of the employment contract.

- **The Specific Holding in *Farber***

After stating the principles summarized above and applying them to Mr. Farber's case, the Court came to the conclusion that he had in fact been constructively dismissed by the Company. The offer made to Mr. Farber clearly involved a substantial change of the essential terms of his employment contract, and any reasonable person finding himself or herself in the same situation as this employee would have reached the same conclusion, taking into account the information that was available at the time the offer was made. In fact, the change offered to Mr. Farber imposed on him, on the one hand, a significant demotion in terms of his responsibilities, status and prestige and, on the other hand, a substantial alteration of his salary conditions. With respect to the latter, Justice Gonthier noted that the elimination of the guaranteed base salary was extremely detrimental to Mr. Farber's financial security. This fact alone, combined with the demotion, was sufficient for the Court to conclude that there had been a constructive dismissal.

- **Reasonable Compensation in Lieu of Notice**

Justice Gonthier recalled that the primary purpose of an indemnity in lieu of notice is to compensate, and that it must be reasonable in view of all the circumstances, notably in relation to the dismissed employee's previous remuneration. In Mr. Farber's case, the Court decided that one (1) year's remuneration in lieu of notice was not unreasonable. Consequently, the Company was required to pay its former employee the sum of one hundred and fifty thousand dollars.

CONCLUSION

- **The Employer's Flexibility in the Context of an Administrative Reorganization**

In view of the above, the employer's room for manoeuvre in the context of an administrative reorganization may seem quite limited. However, in this judgment, the Supreme Court also recalled that the employer, through its managerial authority, retains the right to make all the changes to

the employee's situation which are permitted by the employment contract. Thus, the employer's flexibility will depend on the agreement between the parties at the time the contract was entered into. From this teaching provided by the country's highest court, the astute employer will recognize, today and more so than ever before, the ever-increasing importance of having particularized, detailed and well-drafted employment contracts. In fact, an employment contract which is drafted with special attention to the guidance provided by this decision of the Supreme Court could considerably increase the employer's room for manoeuvre in the context of an administrative reorganization.

RECENT CHANGES TO THE LABOUR STANDARDS ACT

On March 20, 1997, Bill 37, entitled *An Act to amend the Act respecting labour standards* was sanctioned by the National Assembly. This bill introduces change to the *Labour Standards Act* [2] which will enable the *Commission des normes du travail* to represent employees having more than three (3) years of uninterrupted service who believe that they have been dismissed by their employer without just and sufficient cause. It should be recalled that the Commission can only represent an employee who is not a member of a group of employees certified pursuant to the *Labour Code*, for complaints submitted as of March 20, 1997, the date the provisions came into force.

In addition, Bill 88 entitled *An Act to amend the Act respecting labour standards as regards annual and parental leave* was also sanctioned last April 16. On the one hand, this bill modifies the *Labour Standards Act* by increasing the duration of parental leave from 34 to 52 weeks. On the other hand, the bill enables employees having accumulated from one (1) to five (5) years of uninterrupted service to apply for the number of days of leave without pay required to increase their annual leave to three (3) weeks. The provisions of this Act have been in force since April 16, 1997.

Dominique L. L'Heureux

[2] R.S.Q. c. n-1.1.

THE LABOUR LAW GROUP

Montréal

Jacques Audette
Pierre L. Baribeau
Jean Beauregard
Dominique Benoît
Denis Charest
Pierre Daviault
Jocelyne Forget
Philippe Frère
Alain Gascon
Michel Gélinas
Jean-François Hotte
Monique Lagacé
Guy Lemay
Carl Lessard
Dominique L. L'Heureux
Danièle MacKinnon
Catherine Maheu
Jacques A. Nadeau
Marie-Claude Perreault
Jean Pomminville
Érik Sabbatini
Charles-André Sauvé

Laval

Serge Benoît
Patricia Borrelli
Michel Desrosiers
Francis Gervais
Claire Gonneville
Paul Leduc
Luc Villiard

Québec

Pierre Beaudoin
Danielle Côté
Christian R. Drolet
Pierre C. Gagnon
François Houde
Bernard Jacob
Claude Larose
Véronique Morin
Nancy Paquet
Claudia P. Prémont

LAVERY, DE BILLY
BARRISTERS AND SOLICITORS

All rights of reproduction reserved.
The Bulletin provides our clients with general comments on recent legal developments.
The texts are not legal opinions. Readers should not act solely on the information contained herein.