SETTLING WRONGFUL DISMISSAL ACTIONS

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I. INTRODUCTION

The purpose of this paper is to provide some tips to the Judges of the Ontario Superior Court of Justice about how to more effectively pre-try and settle wrongful dismissal actions.

II. WHAT IS A MONTH WORTH

When it is all said and done, 90% of the money in a wrongful dismissal action relates to the notice period. One extremely important element of the notice period is determining what one month of notice is worth. After that number is determined, you simply multiply it by the number of months of notice.

I always try to first get an agreement on what one month of notice is worth before I even talk of the notice period, because otherwise you run the risk that you think you have a deal on 7 month's notice, only to find that the parties are way apart on what they each believe one month is worth.

There are several troubling and difficult aspects of compensation that come up in wrongful dismissal cases. Here are some of the ways that I deal with this.

1) Use of T4: Many compensation arrangements have a myriad of compensation items, most of which show up on a T4: salary, bonuses, overtime , shift differentials, commissions, car allowances , employer paid STD, vacation pay, value of some benefits etc.

   Averaging the last 2 or 3 years T4s can be a useful way of determining an income over the notice period, if neither party is arguing that there would have been some dramatic change in the income over the notice period. However when using a T4 average you must be careful not to double count, that is to say add the amount of commissions to the T4 amount when it is already included.

   Having said that there are elements of compensation not included in the T4, these items should be added to the T4 amount to come up with a proper amount for the calculation of wrongful dismissal damages. This would include most health and welfare benefits, vested but unexercised stock options, club memberships and professional fees.

2) Parties often allege that past historical compensation figures are not helpful because the employee would have either made much more or much less over the notice period because of different economic conditions. It is perfectly legitimate to calculate damages in this fashion, if the information is available and not mere speculation (See *Chann v. RBC Dominion Securities* 2004 Carswell Ont 3341) This case further stands for the proposition that the fact of the termination itself cannot be used as a factor in lowering a bonus, even where the bonus plan itself refers to retention as one of the reason for the plan. In that case the defendant presented evidence to show that the overall bonus pool had shrunk by a certain percentage in the year after the termination. The judge reduced the notice period bonus by the same percentage and rejected the plaintiffs' argument for a backward 3 year average.

   At mediation we often do not know what the bonuses will be in the future as the mediation may be held within 3 to 6 months of the termination. A way to avoid speculating on this is to negotiate a "ride- along" clause, which says that the plaintiff will get his or her bonus at the same time as the other employees at an agreed level, (based on his or her performance being rated as satisfactory or based on the average of his or her agreed peer group).

   Don't forget what I call the "stub period". If the bonus year is 2011, and the notice period is 12 months, then the calculation for the bonus payout is 16 months: the stub period, which the employee actually worked at the defendant, from January 1, 2011 to May 1, 2011 and the notice period from May 1, 2011 to April 30, 2012.

3) Commissions :

   Calculating commissions over a notice period can be a tricky matter.

   Assume the plaintiff has a salary of $50,000 and a commission of 5% on sales that he or she makes, payable once the client pays the invoice. However, once the deal is closed, the salesman's job is complete, as he has no involvement with the customer after the order is accepted. In the last 4 calendar years his or her total income was between $75,000 and $80,000. Assume also that the notice period is 12 months and that during that 12

months the commissions earned would have been $55,000 because you are able to track the sales that were made by the plaintiff's replacement to the same group of clients.

One approach, presumably put forward by the employer, is that we can only look at the plaintiff's historical average, which is $77,500. You cannot look at the $55,000 because that represented the sales by the plaintiff's replacement, who has superior selling skills. In fact the reason the plaintiff was fired was because he was getting lazy and not going after new sales to existing clients, while that is exactly what his replacement did.

The plaintiff will say "no way". I worked hard for 4 years to build sales and it only after I left that the company vastly improved the warranty on the product, and that is why sales went up through the roof. In fact if I had been there, because of my long standing relationship with my clients, I would done even better than my replacement. Therefore I want $85,000 for commissions that I would have made had I worked another year. Furthermore, I would have sold hard to the last day and there would have been at least another $50,000 in sales in the pipeline, which I would have received over the next 9 months following my notice period as clients paid their invoices.

There is legitimacy to all these arguments, depending on the facts. If sales went up after the termination, and they would have done so even if the employee had remained on the job, then he should get the recognition over the notice period. Of course, if sales actually went down during the notice period then the parties will exchange arguments.

From a mediation point of view, especially when neither side has any convincing proof as what would have happened if the plaintiff had been permitted to work during the notice period, using a historical average is often the answer.

However this still leaves the issue of the pipeline. In the above example, there is an important difference between when a commission is earned and when it is paid. In the above example, as the salesman's job is done once the order is taken, one could say he has earned his commission, but he is not entitled to sue for the payment until the order has been shipped and

paid for .Therefore at the time of the order being taken, the defendant has a contingent liability to the salesman with respect to the commission.

So if the employee had been permitted to work out his notice period, on his last day of work there would probably be commissions which he has earned (as the order had been received by the company prior to the last day of the notice period) but for which he is not entitled to be paid for until the order has been filled and the invoice paid.. These are post notice period pipeline commissions, to which he the ex-employee is also entitled to, even though he had nothing to do with the sale. (See *Prozak v. Bell Telephone Company*, 1984 CarswellOnt 752 , Ontario Court of Appeal).

If the salespersons' duties went beyond the actual obtaining of the order. (sales follow-up, delivery, post-delivery issues,) then pipeline income should be reduced by virtue of the fact that he could not have done these other tasks after the expiry of the notice period and because the company presumably paid another employee to do these duties. Note that this sharing of the commissions does not apply to after sales follow-up that occurred within the notice period as these tasks would have been performed by the plaintiff if he or she had been able to work out the period of reasonable notice.

4) Benefits: In *Davidson v. Allelix* (1991) 39 CCEL 184, the Ontario Court of Appeal made it clear that in Ontario the rule is that benefits are valued at the cost to the employer, not the expense incurred or not incurred by the plaintiff to replace those benefits. There should be some evidence to determine this value as some judges will dismiss the claim altogether where there is no evidence of the cost, even though everybody must know that these benefits are not free. As this evidence is solely in the possession of the defendant, it seems somewhat harsh to punish the plaintiff for not providing the Court with information under the control of the defendant.

   In mediations I usually find that a skinny benefits package usually is claimed by the employer to cost between $150 and $350 per month, whereas a better package usually comes in at about 10% of base where that base salary is less than $100,000. This 10% usually includes some sort of pension benefit. Plaintiffs always ask for 15% but usually are quite happy with 10%.

III. DETERMINING REASONABLE NOTICE

As we all know there is no "rule of thumb" that says you get one month of notice for every year of employment. In one of many papers on this topic I reviewed what correlation there was.

In my article entitled *Revisiting Reasonable Notice Periods in Wrongful Dismissal Cases*, 2006 Edition 53 C.C.E.L. (3d) 60, I determined that when we just look at length of service, the cases show the following relationship between reasonable notice and length of service:

- How many Months per Years of Service

Years of Service	**Months per Year of Service**
.6 to 2.5	2.6
2.6 to 5	1.4
6 to 10	1.1
11 to 15	0.9
16 to 20	0.8
21 and 25	0.7
26 and 30	0.6
31 and 35	0.6
36 and 40	0.6

In other words, the average 10 year employee would get a reasonable notice period of 11 months (10 years x.9 months per year of service) and the average 28 year employee would get a notice period of 16.8 months (28 years x.6 months per year of service.

In a ground breaking case from our Court of Appeal called *Di Tomaso v. Crown Metal Packaging Canada LP,* 2011 CarswellOnt 5356, Mr Justice MacPherson said as follows:

27 Crown Metal would emphasize the importance of the character of the appellant's employment to minimize the reasonable notice to which he is entitled. I do not agree with that approach. Indeed, there is recent jurisprudence suggesting that, if anything, it is today a factor of declining relative importance: See *Bramble v. Medis Health & Pharmaceutical Services Inc.* (1999), 175 D.L.R. (4th) 385 (N.B. C.A.) ("Bramble") and *Paulin v. Vibert* (2008), 291 D.L.R. (4th) 302 (N.B. C.A.).

28 This is particularly so if an employer attempts to use character of employment to say that low level unskilled employees deserve less notice because they have an easier time finding alternative employment. The empirical validity of that proposition cannot simply be taken for granted, particularly in today's world. In *Bramble*, Drapeau J.A. put it this way, at para. 64:

> The proposition that junior employees have an easier time finding suitable alternate employment is no longer, if it ever was, a matter of common knowledge. Indeed, it is an empirically challenged proposition that cannot be confirmed by resort to sources of indisputable accuracy.

Unfortunately the Court did not go as far as *Bramble* did, which said that the Court must have empirical evidence before it on the actual period of time that a certain class of employees will normally remain unemployed before this *Bardal* factor can be considered. In the *Bramble* world, character of employment is virtually irrelevant. At least now in Ontario it should not be used to lessen the notice period for lower wage employees.

As the law now stands after *DiTomaso*, I submit that length of service is the most important factor, age second and character of employment a distant third. Some Courts give lip service to the other *Bardal* factor of 'the availability of comparable employment in the market." However I rarely see anybody present actual evidence on this issue. To do in any convincing manner would require the introduction of expert evidence. There is rarely enough money in a wrongful dismissal case to pay the lawyers, let alone experts. In any event what more convincing and relevant evidence could there be of "market conditions" than the

actual time a diligent plaintiff took to find comparable employment. However we all know that the one thing the Court never actually considers is the actual period of time this actual plaintiff took to find a job. Rather we create the illusion of what is the reasonable period of time that it should take for such a person to find a job, based not on any actual empirical or scientific evidence, but rather on a series of largely subjective assumptions that have never actually been tested to see if they are accurate.

For a further rant on my personal pet peeve, see

A New & Improved Theory of Reasonable Notice for Wrongful Dismissal after Honda Canada Ltd. v. Keays 2008 CCEL (3rd) 163

On the other hand our same Court of Appeal tells us that for senior executives with short service it is important not to overemphasize the short service and undervalue the level of employment. So in *Love v. Acuity*, 2011 CarwellOnt 1060, our Court of Appeal increased the 5 month notice period awarded at the trial to Mr. Love (50 years old, Vice President, two years and seven months service) to an alarming 9 months' notice. Here is the rationale.

18 In my opinion, the trial judge's determination of the appropriate period of reasonable notice reflects error in principle in three respects.

19 First, it overemphasizes the appellant's short length of service. While short service is undoubtedly a factor tending to reduce the appropriate length of notice, reference to case law in a search for length of service comparables must be done with great care. The risk is that while lengths of service can readily be compared with mathematical precision that is not so easily done with other relevant factors that go into the determination of notice in each case. Dissimilar cases may be treated as requiring similar notice periods just because the lengths of the service are similar. The risk is that length of service will take on a disproportionate weight.

20 In my view, that appears to have happened here. The two cases from which the trial judge drew guidance in awarding 5 months were cases in which the length of service was comparable to the appellant's and the notice period was assessed at 4 and 5 months respectively. However these cases can provide very little guidance if one looks at other important factors. They were not cases involving a senior executive reporting to the chief executive officer. In neither

case was the employee an owner of the business. In both cases, the employee's average annual compensation was a small fraction of the appellant's. The fact that these employees were awarded 4 and 5 months' notice is of little help in deciding what was appropriate for the appellant.

21 The second error is the under-emphasis on the character of the appellant's employment. To describe it as a senior vice president holding a senior level sales position but not supervising others ignores a number of relevant aspects of the appellant's employment. He was one of only two senior vice presidents. He reported directly to the chief executive officer. He was responsible for an important part of the respondent's operation, namely the investments of its institutional clients. He received significant average annual compensation and was one of nine owners of the company. He was clearly a high level employee, something that this court has said favours a longer notice period: see *Cronk v. Canadian General Insurance Co.* (1995), 25 O.R. (3d) 505 (Ont. C.A.).

22 Third, the trial judge gives no consideration at all to one of the Bardal factors, the availability of similar employment. Both his substantial average annual compensation and the possibility of equity participation in his employer were important aspects of the appellant's employment. Both are relevant in assessing similar employment opportunities: see *Belzberg v. Pollock* (2003), 10 B.C.L.R. (4^{th}) 255 (B.C. C.A.) for an example of the relevance of equity ownership in this assessment. Here both considerations suggest that obtaining similar employment would be harder rather than easier. This *Bardal* factor therefore clearly points to a longer period of reasonable notice.

23 Taking these errors together, I conclude that the trial judge's assessment of five months is the product of error in principle. Moreover, the award is sufficiently wanting that this court is warranted in substituting its own figure. Considerably more than tinkering is required to adequately reflect the factors under-emphasized or ignored.

24 In my view, the character of the appellant's employment, viewed fully, and the challenge of finding similar employment both require a significantly longer period of notice. Giving appropriate weight to these factors, and keeping in mind the appellant's age and short service I would set aside the 5 months awarded at trial and substitute a period of 9 months.

Now you have a good idea why we all spend so much time and effort trying to guess what a judge might award as reasonable notice. The best one can do is look at all the relevant cases and try to get the parties to agree on something like the average.

IV. PUNITIVE, AGGRAVATED, WALLACE AND OTHER NON-PECUNIARY DAMAGES

Since *Keays v. Honda* this is pretty well a dead subject in mediations. Plaintiffs don't waste a lot of time on this because the SCC has virtually made it impossible to actually get these damages. First you have to show that the conduct was so outside the pale that it is deserving of extra damages. That is not the big problem. Our Court of Appeal virtually requires that you also have medical evidence to support the damage claim as all of these claims seemed to have morphed into a mental distress , personal injury type of claim . However, you do not get general damages for the mere fact of the dismissal itself, raher it must be tied to the manner of the dismissal.

How do ever get a doctor in an expert report to opine on whether the mental distress that the plaintiff suffered following his dismissal flowed from the actual loss of employment or from the manner of the dismissal?.

Picture this first scenario. Sam is a 30 year foreman making $50,000 a year, with a spouse who works part-time at Wal-Mart and has two kids in school. Sam is fired and given his ESA minimums, which in this case are only 8 weeks because he unfortunately worked for an employer who has a payroll of less than 2.5 million dollars in Ontario. At the termination meeting the boss says that he is letting Sam go because he knows, but he can't prove, that Sam stole a wrench last year. Sam goes home, tells the wife and kids, and then faces bankruptcy and depression because he was living paycheque to paycheque and will lose his house in 3 months.

Change only one fact. In scenario 2, the boss says, "Sorry Sam, Head Office said I had to let one foreman go and since you make the most money, we chose you. It is nothing personal, that's business. Good luck. Say hello to Marge and kids for me and tell them how sorry I am".

Does anyone honestly believe that Sam in scenario two is going to suffer less mental distress than in scenario one?

Clearly the distress is being caused by the fact of the dismissal and the fact that he is not getting anything close to his proper severance so that he now faces immediate ruin. If the employer had up front paid him his proper common law entitlement, then Sam would undoubtedly be less distressed. However, the Courts have traditionally not found that refusing to pay a dismissed employee his or her common law entitlements at the time of dismissal to be conduct warranting damages for mental distress. Not paying someone what he or she is legally owed is par for the course, however sending the termination letter home in a cab or firing someone just before Christmas is outside the pale.

Personally I would rather get the proper severance money sent to my home in a cab on Yom Kippur than have to sit in some office and listen to a 20 something HR type tell me how sorry the Company is that they have to let me go because the factory is being moved to the a country where they can pay $1.00 per hour to a grateful workforce.

If you want to see the devastation that can flow from a “properly handled” termination watch George Clooney in “Up in the Air”.

As a closing note, one of the most difficult situations in a mediation is when the parties are criticizing what they see as the unfairness or illogic of certain areas of employment law. I often agree with them but retreat to the line that “I do not make the law, I am only here to help you get a settlement within the law as it exists.

It usually works, but it doesn’t always feel good saying it.

V. THE MYTH OF TAX FREE DAMAGES

One of the most common myths of wrongful dismissal damages is that it is easy to characterize them in such a fashion so as to make them tax-free. This is simply not so.

CRA Interpretation Bulletin IT -337R4 (consolidated) sets out the position of the CRA towards these matters as follows:

Types of Receipts

Damages

9. Generally, compensation received by an individual from the individual's employer or former employer on account of damages may be employment income, a retiring allowance, non-taxable damages, or a combination thereof. Such a determination is a question of fact, which requires a review of all relevant facts and documentation of each particular case.

10. Special damages, such as those received for lost (unearned) wages or employee benefits, are taxable as employment income if the employee retains his or her employment or is reinstated.

11. The definition of a retiring allowance includes an amount received in respect of a loss of office or employment of a taxpayer, whether or not received as, on account or in lieu of payment of, damages or pursuant to an order or judgment of a competent tribunal. As discussed in 5, the words "in respect of" denote a connection between the loss of employment and the subsequent receipt**. Accordingly, where an individual receives compensation on account of damages as a result of a loss of employment, the amount received will be taxed as a retiring allowance. This applies to both special damages, as well as general damages received for loss of self-respect, humiliation, mental anguish, hurt feelings, etc.**

12. Where personal injuries have been sustained before or after the loss of employment (for example, in situations of harassment during employment, or defamation after dismissal), the general damages received in respect of these injuries may be viewed as unrelated to the loss of employment and therefore non-taxable. In order to claim that damages received upon loss of employment are for personal injuries unrelated to the loss of employment, it must be clearly demonstrated that the damages relate to events or actions separate from the loss of employment. In making such a determination, the amount of severance that the employee would reasonably be entitled to will be taken into consideration.

Similarly, general damages relating to human rights violations can be considered unrelated to a loss of employment, despite the fact that the loss of employment is often a direct result of a human rights violations complaint. If a human rights

tribunal awards a taxpayer an amount for general damages, the amount is normally not required to be included in income. When a loss of employment involves a human rights violation and is settled out of court, a reasonable amount in respect of general damages can be excluded from income. The determination of what is reasonable is influenced by the maximum amount that can be awarded under the applicable human rights legislation and the evidence presented in the case. Any excess will be taxed as a retiring allowance

In other words, for a damage claim to be classified as tax free, it must exist independently of the dismissal. Thus anything that flows from the dismissal, (i.e. *Wallace* damages, probably punitive and aggravated damages, compensation for failing to reinstate etc.) are taxable , as , but for the dismissal , the damages would not have occurred. Remember that the essence of *Wallace* damages is that the Court found that there was a duty of good faith in the **manner** of the dismissal. Therefore, from a CRA point of view, these damages are in respect of the dismissal and therefore constitute a retiring allowance, that is, they are taxable.

The key, therefore, is to find a cause of action unrelated to the dismissal. This could include:

1) Pre-dismissal harassment, either human rights based or generalized
2) Defamation
3) Intentional or negligent infliction of mental suffering, if the stated goal is not to get the plaintiff to quit.
4) Harassment under Bill 168 (Occupational Health and Safety Act) or pursuant to a harassment policy
5) Assault
6) Intentional interference in contractual relations
7) Inducing breach of contract, as in this case the defendant is not the employer.

Very few lawyers know how strict CRA is on this issue, or if they do know they and their clients do not seem to care very much. However as Judges of the Superior Court , you should be very careful not to endorse or suggest questionable tax characterizations in a pretrial.

Actual legal fees incurred by the plaintiff in the course of his or her wrongful dismissal lawsuit are not taxed as income as long as the payment is made directly by the defendant to the plaintiffs lawyer.

Prejudgment interest is taxable as interest income, but the employer need not withhold income tax at source.

Once in a while someone is fired before they even start work. In this case the damages from flow from that anticipatory breach of contract are not taxable,. (See *Schwartz v. Canada*, [1996] 1 SCR 254.

VI. LEGAL COSTS

Nothing irritates plaintiffs more than having to pay their own lawyer. However, defendants also dislike paying the plaintiff's lawyer, let alone their own. Both sides often treat this topic with great emotion, often completely out of proportion to the amount involved.

The parties often have to be reminded of two fundamental aspects of our costs regime: The loser pays part of the winners' fees and the winner pays the balance.

Payment of a portion of the plaintiff's legal fees is the grease in the settlement. The best use of defendant's money is often to help pay the plaintiff's lawyer.

As to how much is usually contributed in a settlement, obviously the amount varies considerably based on numerous factors. I would say that in the majority of the mediations that I am involved with, the mid-range of contribution to costs is between $3,500 and $7,500 for a case that did not go to discoveries or have any motions.

VII. EI REPAYMENT OBLIGATION

The *Employment Insurance Act* provides that if a person received EI, and later received a settlement, there is an obligation to repay EI. For example if the person received EI for 6 months and subsequently received a settlement that compensated for 6 months income all the EI would have to be repaid.

In summary, EI will not treat as earnings, that part of the settlement that is fairly shown to be:

1) Legal fees
2) Mental distress or pain and suffering if accompanied by evidence of medical care
3) Reimbursement of job search, relocation or retraining expenses
4) Damages for loss of dignity, self-worth and reputation
5) Paid in lieu of an existing right to reinstatement of employment

VIII. WHAT COUNSEL AND THE PARTIES WANT FROM THE PRE-TRIAL JUDGE

1) A strong sense that the judge understands the issues and their relative importance.

    Depending on the quality of the briefs, you will probably learn more about the case through the oral discussion than the written briefs. Showing the parties that you understand not just the pure legal issues but also the human and business realities can go along way to enhancing your credibility with the litigants and their lawyers. The more credibility you have with them, the more your settlement opinion matters. Whenever I had a disastrous pretrial. I would say to my client "Thank God he was the pretrial judge". When my client appeared shocked at my comment, I reminded them that the pretrial judge cannot be the trial judge.

2) Offer an opinion if it will be helpful to settlement but don't over extend or under play the opinion.

    Sometimes in a pretrial you have all the info that you would need to make an informed decision on the merits, for instance, a contract interpretation case or a straight forward notice case.

    Other times there is such a gap in the available information that you could not in good conscience make any helpful comment about the likely court outcome.

In the first instance, your considered opinion will probably be very helpful in getting a deal and throw a wrench into the losing litigants' game plan of "dragging the other party through the litigation mud".

In the second case, offering an off the cuff opinion can be disastrous both to the ability to settle the case at that time and in the future. It would be more helpful to make a comment like "Right now this is a "he said, she said " type of case and I can't say anything about who is more believable. However I note that each of you seem to rely on the anticipated evidence of Mr. Third Party, although neither lawyer seems to have actually spoken to Mr. Third Party about what he would actually say if he were testify in Court. Why don't you arrange with Mr. Third Party to meet with both lawyers and discuss what his evidence actually would be. Then we can reconvene the Pre-Trial and settle this case. I have no idea what he might say but I know that both of you cannot be right, however, both of you could be wrong"

3) Your job is to close the gap between settlement positions, not to make it harder to settle.

Don't offer your settlement opinion until you have heard from the parties what their last settlement offer is. If the Plaintiffs' offer is $100,000 and the Defendants' is $65,000 and you think that the court result would be $125,000, using phrases like "I think that the Plaintiff's offer is much closer to the pin" can bring about a quick and fair resolution. If on the other hand you offer your opinion of $125,000 before you even know of the parties outstanding offers, you create a situation where the plaintiff now thinks his lawyer is an incompetent schmuck who sold him down the river and the defence lawyer tells his client " Thank God she was the pretrial judge."

IX. CONCLUSION

In the cases that you see, the parties probably have not had a mediation, as it is not mandatory in your region as it is in Toronto, Ottawa and Windsor. The pretrial may well be their best opportunity to settle the case before the trial begins. In employment cases it is quite common that neither side has ever been involved in

any type of litigation let alone an employment case. An effective pretrial conference can go along way towards resolving both simple and more complex employment disputes.