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13TH ANNUAL Employment Law Summit

The Relationship Between the ESA and Employment Contracts

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October 18, 2012

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I. Introduction

Our modern *Employment Standards Act* ("ESA") has its roots in late Victorian era laws aimed at most vulnerable of workers – children. The early legislation establishing minimum standards (no doubt enlightened in its time) regulated the factories of the industrial revolution by setting minimum working ages (12 for boys and 14 for girls); limiting the hours of work for children (60 per week); prohibiting factory owners from allowing children to clean machinery in a factory while the machinery was still in motion; and, requiring factories to provide "privies"[2]. From that modest beginning, we now have an ESA which regulates not just the working hours and working conditions for children in factories, but actually touches upon a whole host of issues that are often addressed within contracts of employment, including hours of work, wages, overtime, vacation, public holidays and rights on termination of employment.

It is well recognized that contracts of employment, including employer policies incorporated by reference into employment contracts, must not provide for less than any individual employment standard. The ESA provides that an employer and employee cannot contract out of or waive an employment standard and that any attempt to do so is void[3]; if an employment contract provides a greater right or benefit than an employment standard, the contractual provision providing a greater right will prevail[4]; and, civil remedies of an employee against an employer are not to be affected by the ESA[5]. The application of these seemingly straightforward principles has spawned considerable litigation. There are many ways in which employment contracts and the ESA may collide. When this happens, this can result in significant claims for employees and significant liability to an employer.

This paper will discuss contracts of employment and their relation to the employment standards dealing with the termination, overtime and layoff.

II. Termination Clauses

There is considerable litigation dealing with the enforceability of termination clauses within employment contracts. Termination clauses are challenged for a variety of reasons – lack of consideration, ambiguity, setting minimums not maximum and providing less than ESA minimums. These issues have been well addressed in a number of recent continuing legal education programs. I will focus on three narrow issues relating to employment contracts that:

[1] I gratefully acknowledge the research assistance of Simone Ostrowski, summer student.
[2] The Ontario Factories' Act 1884
[3] Section 5(1) ESA
[4] Section 5(2) ESA
[5] Section 8 ESA

1) provide for termination without any notice for "just cause"; 2) contain a potential violation of the ESA; and, 3) do not provide for benefit continuation during an ESA notice period.

a. Contracts providing for termination without any notice where there is "just cause"

Termination clauses which state that an employee will not receive any notice or pay in lieu in the event of a termination for just cause are exceedingly common. For example, many contracts state: "[w]e may terminate your employment for just cause at any time without notice, pay in lieu of notice, severance pay, or other liability."

Such termination clauses may not make reference to the ESA and may even include termination without cause language which exceeds ESA minimums. However, the enforceability of these clauses must be considered in light of Regulation 288/01 of the ESA which states:

> 2(1) The following employees are prescribed for the purposes of section 55 of the Act as employees who are not entitled to notice of termination or termination pay under Part XV of the Act:
> …
> 3. An employee who has been guilty of wilful misconduct, disobedience or wilful neglect of duty that is not trivial and has not been condoned by the employer.
> …
> 9(1) The following employees are prescribed for the purposes of subsection 64 (3) of the Act as employees who are not entitled to severance pay under section 64 of the Act:
> …
> 6. An employee who has been guilty of wilful misconduct, disobedience or wilful neglect of duty that is not trivial and has not been condoned by the employer.

Pursuant to Regulation 288/01, for an employee can be terminated without ESA notice, severance or benefit plan contributions during the notice period, she or he must be "guilty of wilful misconduct, disobedience or wilful neglect of duty that is not trivial and has not been condoned by the employer." The distinction between this standard, and common law "just cause"[6] has long been recognized in the decisions of ESA referees and the Ontario Labour Relations Board.

For example, in *Pemco Steel Sales Ltd. (Re)* [1995] O.E.S.A.D. No. 133, ESA Referee Wacyk held:

> The standard to be applied when determining whether a situation comes within subsection 57(10)(c) has been much discussed and considered. What is clear is that a finding of "just cause for dismissal" does not justify an exemption from termination pay (see Re Westminister Hotel, February 22, 1979 (Franks) E.S.C. 583; Re Space Circuits Ltd., November 22, 1982 (Rose) E.S.C. 1328; and Re Italian Mutual Benefit Society, September 13. 1985 (Aggarwal) E.S.C. 1948).

[6] Similarly, the distinction between "misconduct" under the *Employment Insurance Act* and common law just cause was recognized judicially in *Minott* v. *O'Shanter* (1999) 42 OR 3rd) 321 which held (at para. 27): "…an employee who is incompetent or persistently careless may be dismissed for cause though no misconduct is made out, because misconduct requires a wilful or reckless disregard of an employer's interest. In short, misconduct under the Act cannot automatically be equated with just cause for dismissal at common law."

> In cases such as this one, the issue is not whether there is just cause for some form of discipline or even for termination. Rather, as stated by Referee Raymond Brown in Argo Cleaners (Windsor) Inc., (July 10, 1985), E.S.C. 1918 at pp. 10-11:
>
> > Wilful misconduct for the purposes of the statute requires some deliberate or intentional act on the part of the employee. It is not enough to show that the employee failed to perform the duties he was required to perform or performed them incompetently if it is not also shown that his acts or omissions were the product of deliberation and design on his part. Thus acts which are done carelessly, thoughtlessly, heedlessly or inadvertently are not acts of wilful misconduct even if they are done repetitively and may have been the basis for summary dismissal at common law.

On this issue of just cause vs. wilful misconduct, the Ontario Labour Relations Board generally applies the standard set out in *VME Equipment of Canada Ltd.*, [1992] OESAD No. 230 which states:

> Much has been written on the meaning of the words 'wilful misconduct'. It seems to me, however, that that authority can be summarized briefly. In the first place, serious misconduct has to be proven. That is conduct that seriously interferes with either the performance of the employee's job duties or that of his or her co-workers. Normally the Employer would have to demonstrate that harm has been done to its operation and that the misconduct amounted to a repudiation by the employee of the employment contract. There are two general categories of serious misconduct. There will be single acts: insubordination, theft and dishonesty, and physical violence against other employees, for instance, which may, standing on their own, meet that standard of seriousness. As well, there will be less serious repetitive forms of misconduct, which if handled properly by the employer, will also meet this standard of seriousness. The employer, in this scenario, must have explained to the employee after each occurrence that the conduct in question was not acceptable and that if continued would result in termination and there must be, subsequent to these warnings, a culminating incident.
>
> In addition to proving that the misconduct is serious, the employer must demonstrate, and this is the aspect of the standard which distinguishes it from 'just cause', that the conduct complained of is 'wilful'. Careless, thoughtless, heedless, or inadvertent conduct, no matter how serious, does not meet the standard. Rather, the employer must show that the misconduct was intentional or deliberate. The employer must show that the employee purposefully engaged in conduct that he or she knew to be serious misconduct. It is, to put it colloquially, being bad on purpose.

This distinction between "just cause" and "wilful misconduct" under the ESA has found recent expression in a court decision finding liability against an employer for ESA entitlements where common just cause was established. In *Oosterbosch* v. *FAG Aerospace Inc.* [2011] O.J. No. 1135, the employee had received four written warnings dealing with lateness and unsatisfactory work performance under the employer's progressive discipline policy. The court found that the persistence of the employee's misconduct after coaching and warnings constituted a repudiation of the employment relation so as to make out just cause. However, the employee's misconduct was characterized as "…a sustained course of casual and careless conduct", but it was not "wilful" so as to disentitle him to ESA termination and severance payments. In the result, the employee was awarded 25.33 weeks of pay notwithstanding the determination that he was terminated for just cause.

Plester v. *Polyone Canada Inc.* [2011] ONSC 6068 (Canlii) involved a just cause termination after a serious safety breach and failure to report the breach by the employee. Though nothing

turned in the case on the distinction between common law just cause and wilful misconduct (given that the court ultimately found that cause was not made out), the court noted that the test for wilful misconduct is higher than for just cause and analyzed both issues separately. The court noted: "[b]oth counsel seemed to be slightly bemused by the recent authorities that distinguish between the definition of just cause and wilful misconduct". Justice Wein described wilful misconduct as involving "…an assessment of subjective intent, almost akin to a special intent in criminal law." An employee's misconduct could be "serious", but not "preplanned" and "wilful" so as to rise to the level that would disentitle the employee from statutory notice.

It has been said that there is often a "thin line"[7] between "just cause" and "wilful misconduct"; however, this distinction has important implications for the enforceability of employment contract termination clauses. The ESA requires termination and severance pay and benefit continuation during the ESA notice period, unless the employee is "guilty" of "wilful misconduct", disobedience or wilful neglect of duty that is not trivial and has not been condoned by the employer." Given that just cause is a lower standard than the ESA's wilful misconduct standard, an employment contract which provides that an employee terminated for cause receives nothing, is a contract which provides for less than what is required by the ESA. An employee is entitled to termination and severance pay, which may be as much as 34 weeks of pay without any reduction for mitigation, even if the employee is terminated for serious misconduct, unless that misconduct can also be shown to be "intentional" or "deliberate" or as stated in the ESA case law, the employee was "being bad on purpose." A contract which purports to deny ESA termination entitlements when common law cause but not ESA wilful misconduct is made out, provides less protection to an employee than the ESA requires as a minimum.

It is well established that a termination provision which provides for lesser rights than provided for under ESA minimums is not enforceable. It is void *ab initio*. In light of the long-standing law developed by ESA referees and the OLRB recognizing a distinction between just cause and wilful misconduct, and the recent judicial recognition of that distinction within the wrongful dismissal context, in my view, just cause termination provisions which state that there shall be no notice or pay in lieu where there is cause are not enforceable.

An easy way to avoid this issue entirely is to draft contracts which simply state that, in the event of termination for cause, the employee "shall receive only the payments and benefits required by the *Employment Standards Act* (Ontario) as amended from time to time".

If a just cause/no notice termination clause is unenforceable, what implications would this have for other parts of a termination clause which do not run afoul of the ESA (e.g. without cause provisions which are consistent with the ESA)?. Is there a risk that an entire termination clause, including acceptable no cause termination provisions, will fall? In my view, the answer will turn on whether: 1) the other branches of the termination clause are drafted as standing alone provisions; 2) clear severability language is included in the employment contract; and, 3) saving

[7] K. Parry and D. Ryan, Employment Standards Handbook, 3rd Ed., 2001, Canada Law Book

language is included stating that the ESA minimums will apply in the event a finding of a breach of the ESA.

The risk that a just cause termination provision will not be enforced is a real one, particularly when you consider the evolving case law involving contingent or potential violations of the ESA addressed in the next section.

b. Potential Violations of the ESA

A contractual termination clause may not violate the ESA at the time of termination, but be drafted in a manner such that it could, on a future termination date, violate the ESA. This issue was addressed in *Wright* v. *The Young and Rubicam Group of Companies (Wunderman)* [2011] ONSC 4720 (Canlii), a recent Ontario Superior Court of Justice decision.

Prior to *Wright*, two British Columbia cases, *Shore* v. *Ladner Downs*, [1998] BCJ No. 1045 (BCCA) and *Waddell* v. *Cintas Corp.* (2001), 15 CCEL (3d) 15 (BCCA), addressed this issue. *Shore* has been cited with approval in the trial decision in *Slepenkova* v. *Ivanov*, [2007] OJ No. 4708 (SCJ), aff'd [2009] ONCA 526 (CanLII), and now in the recent decision in *Wright*. *Slepenkova* states (at para. 81):

> The defendant further argued that the provision should not he held to violate the Act because at the time of termination, Slepenkova had not yet passed the three-year mark in her employment and the specified notice complied with the minimum notice requirements of the Act. This distinguishes this case from Machtinger, supra, where the notice period specified in the contract was less than the statutory minimum at the time of termination. The British Columbia Court of Appeal considered this issue in Shore v. Ladner Downs, [1998] B.C.J. No. 1045 (B.C.C.A.). In that case, the statutory minimum notice period was less than the period specified in the contract. The statutory minimum would not have exceeded the contractual period for five years and the contract was terminated after nine months. In that case the defendants argued that contractual term should only become void when the statutory requirement rose above the contractual period. The Court in Shore relied on the policy considerations outlined in Machtinger and concluded as follows:
>
> > The policy considerations applied in Machtinger would not be served if the contract were to be interpreted in favour or the employer so as to leave the individual employee responsible for determining at the point of termination, whether the statutory minimum had risen above the notice period stated in the contract. It is neither reasonable nor practical to leave the individual employee in the position of having to keep an eye on the relationship between the statutory minimum and the contractual term.
>
> I find the reasoning in Shore persuasive. I find that the contractual term in the contract between Ivanov and Slepenkova was void from the beginning for noncompliance with the statutory notice provisions. The presumption of reasonable notice is not therefore rebutted by the contract.

Following on *Slepenkova*, *Wright* addressed a potential violation of the ESA. The Court considered the enforceability of a termination clause which provided for pay in lieu of notice fixed at a number of weeks of "base pay" with the number of weeks of notice increasing commensurate with the number of years of service. The clause in question stated:

> The employment of the Employee may be terminated by the Employee at any time on 2 weeks prior written notice (one week's notice during Probationary Term), and by the Company upon payment in lieu of notice, including severance pay as follows:
> a) during Probationary Term – one week's notice;
> b) within two years of commencement of employment – four (4) weeks Base Salary;
> c) after two and up to three years after commencement of employment – six (6) weeks' Base Salary;
> d) after three but less than five years after commencement of employment – eight (8) weeks' Base Salary;
> e) five years or more and up to ten years after commencement of employment – thirteen (13) weeks' Base Salary, plus one (1) additional week of Base Salary for every year from 6–10 years of service up to a maximum of 18 weeks;
> f) after more than ten years but less than 19 years from the commencement of employment – six months' Base Salary;
> g) After 19 years or more from the commencement of employment – 34 weeks' Base Salary (or eight months)
> This payment will be inclusive of all notice statutory, contractual and other entitlements to compensation and statutory severance and termination pay you have in respect of the termination of your employment and no other severance, separation pay or other payments shall be made.

The employee in that case was a five year employee who would have been entitled to 10 weeks of combined termination and severance pay, if ESA severance was applicable. The application of the contract resulted in the payment of 13 weeks of pay in lieu of notice, an amount in excess of ESA notice and severance. However, the court noted that at 8.5 or 9.5 years of employment, the contract would result in the employee receiving less than the amounts required for ESA notice and severance pay. In the result, with reliance upon *Shore* v. *Ladner Downs* and *Slepenkova* v. *Ivanov*, the Court held that the contract was unenforceable, relying in part on the potential for a violation of the ESA at a future date. The employee was awarded 12 months of pay in lieu of notice.

Wright underlines the importance of drafting contractual language which is forward-looking and ensures that, in future years or in the event of a change of circumstance (e.g. growth of the employer resulting in severance pay obligations), there can be no potential violation of the ESA.

c. Failure to provide benefit continuation during statutory notice period

In addition to the potential violation of the ESA issue discussed above, *Wright* v. *The Young and Rubicam Group of Companies (Wunderman)* also considered whether a contractual termination provision breached the ESA because it excluded benefits.

Sections 60 and 61 of the ESA deal with benefits continuation during a period of ESA notice as follows:

> 60(1) During a notice period under section 57 or 58, the employer,
> (a) shall not reduce the employee's wage rate or alter any other term or condition of employment;
> (b) shall in each week pay the employee the wages the employee is entitled to receive, which in no case shall be less than his or her regular wages for a regular work week; and
> (c) shall continue to make whatever benefit plan contributions would be required to be made in order to maintain the employee's benefits under the plan until the end of the notice period. 2000, c. 41, s. 60 (1).
> ...

> 61(1) An employer may terminate the employment of an employee without notice or with less notice than is required under section 57 or 58 if the employer,
> (a) pays to the employee termination pay in a lump sum equal to the amount the employee would have been entitled to receive under section 60 had notice been given in accordance with that section; and
> (b) continues to make whatever benefit plan contributions would be required to be made in order to maintain the benefits to which the employee would have been entitled had he or she continued to be employed during the period of notice that he or she would otherwise have been entitled to receive. 2000, c. 41, s. 61 (1); 2001, c. 9, Sched. I, s. 1 (14).

In *Wright*, the employer actually continued benefits during the notice period in compliance with the ESA. However, the employment contract, as noted above, provided for a fixed number of weeks of pay in lieu of notice based on base salary and further stated that the contractual termination provisions "…will be inclusive of all…entitlements to compensation". The Court reasoned (at para. 16 and 17):

> Benefits are part of the compensation. Benefits are purchased for the employee by payments made by the employer to a benefits provider. This agreement was drawn by the employer. Even if there is an ambiguity, the ambiguity should be resolved in accordance with the principle of contra proferentum. The fact that the defendant continued benefits for the statutory notice period under the Act does not change the meaning of the language used in the agreement stipulating that the payments under the termination provisions are to be inclusive of "all … entitlements to compensation". The agreement provides for payment of base salary only. Payment of base salary, if treated as inclusive of all entitlements to compensation, means that there will be no other compensation flowing to the employee – in short, no benefits.
>
> In my view, the clause excludes benefits and is therefore in violation of s. 5(1) and s. 61(1)(b) of the Act.

Interestingly, the Court distinguished *Roden* v. *The Toronto Humane Society* [2005] O.J. No. 3995 (C.A.), an Ontario Court of Appeal decision which rejected the argument that a contract breached the ESA due to a lack of benefit continuation. In *Roden*, the Court determined that there was no breach of the ESA because, while the contract was silent on benefits, it did not explicitly exclude benefit continuation during the notice period.

Silence with respect to benefit continuation in an employment contract may be acceptable and result in the reading of the contract in a way that does not seek to contract out of ESA entitlements. However, contractual provisions that limit entitlements on termination to "base salary" or use the language of "all compensation" may be read to exclude benefits continuation with the result that the entire termination provision is rendered unenforceable. Clearly, the safest course is to expressly reference all rights and benefits under the ESA. For example, "you shall receive the notice (or pay in lieu of notice) and any other payments and benefits required by the *Employment Standards Act* (Ontario) as amended from time to time."

III. Overtime

Many employees now operate in a world where work may be performed anywhere and anytime; employers often demand access and responsiveness from employees outside of traditional working hours; and, employees often value flexibility over hours of work in order to

manage personal and family responsibilities. This resultant blurring of the work and personal spheres, particularly in the relation to hours of work, overtime, vacation and public holidays standards, creates ESA issues. There are many cases involving overtime claims, including several recent significant class action lawsuits[8]. A review of that case law is beyond the scope of this paper. I will simply address a few common issues in relation to the intersection of employment contracts and the ESA hours of work and overtime provisions. Though there are exceptions under the ESA overtime provisions (e.g. for managers and supervisors), this section of the paper relates only to employment contracts where no exception is applicable.

a. All-In Salary Contracts

Contracts of employment often provide for an annual salary without reference to a specific number of hours of work or hourly wage rate. The contract of employment for a salaried employee may simply state an annual salary along with an expectation that the employee will dedicate her or his full-time and attention to completing the tasks associated with the position.

Within this contractual context, questions arise regarding entitlement to overtime, what the threshold number of hours is before pay for additional hours or overtime pay is required and what the hourly rate of pay is when overtime is worked.

i. Contracts which do not specify hours of work

Generally, a contract for a fixed salary, where there is a no contractual provision express or implied dealing with hours of work, will compensate an employee for all hours of work up to 44 hours in a week. Further, an employee will be entitled to overtime pay for hours worked over 44 hours in a week (unless the employee falls within one of the exceptions to the ESA's overtime provisions). An employee on a fixed salary will be entitled to overtime even if the employee is highly paid and there is no breach of the ESA's minimum wage standards when hours of work and overtime are quantified.

McKaye (Re) [1996] O.E.S.A.D. No.102 ("*McKaye*") held that in the absence of an agreement that overtime pay will be paid after 40 hours, the statutory threshold of 44 hours weekly applies. The employee sought to recover unpaid overtime and claimed to have worked "long hours" to ensure that the employer's store was staffed. The employee was paid a salary, and his pay stubs indicated a typical work week of 40 hours. As a result, the employee submitted that all hours worked beyond 40 in a week were to be compensated as overtime hours. However, the Ontario Labour Relations Board (the "Board") rejected the employee's submission as he was "not paid an hourly rate, but instead was paid a salary, a fixed sum paid

[8] *Fresco* v. *Canadian Imperial Bank of Commerce* [2012] ONCA 444 (Canlii), *Fulawka* v. *Bank of Nova Scotia* [2012] ONCA 443 (Canlii), *McCracken* v. *Canadian National Railway Company* 2012 ONCA 445 (Canlii) and *Brown* v. *Canadian Imperial Bank of Commerce* [2012] ONSC 2377. Currently, *Fresco* and *Fulawka* are subject to leave applications before the Supreme Court of Canada and a Notice of Appeal to the Divisional Court has been served in *Brown*. These cases all involve class action certification applications under the *Canada Labour Code*, not the ESA, and deal in large part with suitability of class proceedings.

bi-weekly, regardless of the number of hours worked." Further, the Board found that the evidence did not suggest an agreement that the employee would be paid overtime for more than 40 hours worked in a week. The Board noted that in the absence of such an agreement, anything short of hours in excess of 44 are considered to be compensated by an employee's salary. As such, the employee was only entitled to overtime for hours worked in excess of 44 in a week.

Similarly, in *1076640 Ontario Inc. (c.o.b. Architronics Integrated Electronics Systems),* [2006] O.E.S.A.D. No. 933, the Board rejected an employee's claim for overtime as there is no statutory entitlement for an hourly wage for hours worked over and above a salaried employee's regular hours of work, unless those hours exceed 44 hours. However, the Board did recognize that an "employer and employees can enter into agreements that pay additional wages for hours over a set limit."

The approach taken in *McKaye* and *Architronics* has also been adopted by courts. In *Kyle v. Price Business Development Corporation,* 2010 ONSC 3567, a decision of the Ontario Superior Court of Justice. In *Kyle*, the plaintiff sought unpaid overtime after being terminated from her employment with the defendant. The plaintiff submitted that she had had an agreement with the defendant that all hours over 40 in a week would be paid as overtime. The Court rejected the plaintiff's claim to overtime for all hours worked over 40 in a week. The Court recognized that parties may enter in to an agreement that overtime pay may accrue at less than 44 hours in a week and that this would be a greater right or benefit within the meaning of Section 5(2) of the ESA. However, the Court held that there must be clear evidence of such an agreement for it to be enforceable. In *Kyle*, there was no evidence of such an agreement in the correspondence between the parties, nor did the plaintiff allege that there had been an oral agreement and, as such, the regular overtime threshold of 44 hours weekly was held to apply.

The case law suggests that in the absence of a clear agreement such as a written contract of employment, the overtime threshold will be 44 hours where there is a contract for a fixed salary with no specified hours of work.

ii. <u>Contracts which set lower threshold for hours of work – greater right or benefit</u>

Where a contract provides an all-in salary and also clearly provides for a "set" or "regular" number of hours per week which is lower than the ESA's overtime threshold of 44 hours per week, the lower threshold may apply as a greater right or benefit under Section 5(2) of the ESA. If a contract of employment sets 35 or 40 hours as a regular work week, an employee's hourly wage rate would be determined by dividing 35 or 40 hours by the employee's weekly wage rate. In these circumstances, though not an overtime issue per say, the employee would have a claim for hours of work over a regular work week based on straight time up to 44 hours and for overtime at time and one half for hours over 44 hours.

There are cases enforcing contractual terms setting a lower threshold than 44 hours. For example, *Ontario Nurses Association*, [1998] O.E.S.A.D. No. 199, the Ontario Labour Relations

Board (the "Board") considered the evidence of the employer's practices in determining a salaried employee's "set" or "regular" number of hours per week. In that case, twenty-two employees of the Ontario Nurses' Association ("ONA") filed a complaint with the Employment Standards Branch alleging that their employer had failed to pay them for certain hours worked and that as a result of the overtime and compensatory policies of their employer, they had worked for no pay. The employer's position was, *inter alia*, that the claimants were "well paid to recognize that employees may have to work long hours in the course of the completion of their work, hence there is no hourly rate for those employees". The Board found that on the basis of a collective agreement in place and the practice by which compensatory lieu time was accumulated within the workplace, that the regular work week was 35 hours. In the result, the employees' wage rate was calculated on the basis of a 35 hour work week, rather than a 44 hour work week, and the employees were entitled to be compensated at straight time for hours worked between 35 and 44 and at time and one half for hours worked over 44.

Thus, where the parties have reached a clear agreement establishing the number of hours in a regular work week, the employee will be entitled to be compensated for the additional hours worked in excess of that threshold at straight time up to 44 hours, and as overtime for the hours thereafter.

iii. Contracts which provide salary which includes overtime pay – "bundling"

Employers sometimes attempt to deal with overtime issues by drafting a contract that provides for a blended salary or wage rate which captures overtime, and there are a number of cases that address such attempts.

Not all employer-employee agreements to pay a salary which includes overtime pay will be found in violation of the ESA. In *D & D Diamond Cutting and Coring Inc. (Re),* [1993] O.E.S.A.D. No. 162, the claimant testified that he was hired on the expectation that he would work a 50 hour week, and would be paid $700.00 per week for those hours. The employer denied any liability for overtime, and stated that claimant was "paid at a rate that specifically incorporated payment for overtime." The employer successfully argued that an employment contract had been negotiated between the parties which provided for a guarantee of 50 hours per week. The employer submitted that the negotiated weekly salary was arrived at based on the employee's hourly rate for 44 hours and time and one half the employee's hourly rate for 6 hours and then rounded up to $700. On this basis, the Referee was able to determine an hourly wage rate and determine that the weekly salary provided for payment for all hours worked and overtime pay.

The Referee found that this was not a case where the employer was trying to defeat the overtime provisions of the ESA by paying a flat salary regardless of the actual hours worked. Rather, "the essence of the employment contract" here was found to be 50 hours of work per week, which informed the parties' agreement regarding salary. Importantly, the Referee noted that the parties here had "intended to draw a distinction between regular hours and overtime

hours on a weekly basis and to compensate accordingly." In the result, the employee was still entitled to overtime for hours worked over 50 hours per week.

However, *Astro Dyeing & Finishing (Canada) Ltd. (Re)*, [1989] E.S.C. 2631 ("*Astro*") demonstrates that even where there is evidence that an employer intended for an employee's salary to cover overtime, but did not specify the number of overtime hours, additional compensation for the overtime may still be required under the ESA. In *Astro*, the employee was hired in March 1988 at a rate of $360.00 per week for a 44 hour week. However, his weekly pay was raised to $500.00 only a few months later in July 1988, which the employer claims was mainly to reflect an increase in the employee's hours to 50 per week. The Referee found that the employer owed the employee overtime, despite the employer's genuine belief that the $500 flat rate would cover any overtime worked by the employee. The Referee accepted that it was the employer's intention, when it increased the employee's pay in July 1988, to "compensate him for having to work overtime." However, the employee's weekly pay was simply expressed as $500.00 per week. The Referee relied on the provisions of the ESA which require overtime pay for hours worked over 44 and the provisions which prohibit contracting out of the ESA in finding that the employee was entitled to additional overtime pay. The employer may have acted in good faith in bundling an employee's regular and overtime pay together; however, additional overtime pay was required.

Similarly, in *Mariposa Cruise Line and Ontario Ministry of Labour (Re),* 1999 CanLII 19169 (ON LRB), the Board held that an employer who effectively bundles in regular and overtime wages in a flat hourly "wage" may be liable to pay additional overtime pay. In *Mariposa*, the employer had offered the employee two choices regarding payment – he could be paid at $6.85 per hour, plus overtime when applicable, or be paid at $10.00 per hour regardless of the number of hours worked. The employer claimed that the second option was an advantage to the employee during slower periods. Here, the employee had taken the $10.00 per hour option, and the Board found this payment method indeed created a higher total pay during an entire season. Regardless, the Board rejected the use of the $10.00 flat hourly rate, and the Board stated that subsection 24(1) of the ESA, which set out the overtime hourly pay rate, "must be observed and parties are not legally competent to contract out of that portion of the statute, no matter how good an idea it appears to be to one or both of them." While the $10.00 rate was advantageous to this particular employee, the benefit to the employee was dependent on the actual number of hours worked whereas with a different work schedule it could provide less than what overtime pay under the ESA would require.

The Board contrasted the unacceptable flat hourly rate here with the situation in *D & D Diamond* which scenario involved a "situation where hourly wages combined with a *guaranteed* number of hours per week create a fixed salary as the basis for payment," which was still acceptable according to the *ESA.*

iv. Summary

Generally, a contract providing for an all-inclusive or fixed salary which makes no reference to the hours of work will only compensate for hours up to 44 hours in a week and overtime pay will be required for hours worked over 44. This is, of course, subject to the application of any overtime exemptions (e.g. managerial or supervisory employee). An hourly wage rate will be determined by dividing the weekly salary by 44 hours and overtime at time and one half will be required for hours worked over 44 in a week.

A contract which provides for a lower number of hours in a work week (e.g. 35, 37.5 or 40 hour work week) will generally be considered a greater right or benefit under Section 5(2) of the ESA. A finding of such a contract generally requires clear evidence. Lower regular or set hours will result in an entitlement to pay at straight time for hours worked over the set hours and below 44 and the time and one half for hours over 44. Further, a lower threshold for regular hours will result in an increased hourly wage rate for purposes of quantifying overtime pay.

In principle, a contract can explicitly specify a salary which covers both regular hours and overtime hours. However, attempts to do so are often unsuccessful. The statement of an all-inclusive salary which is said to be for regular and overtime hours or "bundling" has often been considered an attempt to contract out of the ESA and thereby invalid. This is the case when a salary is paid without regard to the number of hours worked by the employee. The exception, though not without risks, is a contract which actually explicitly sets out the hours of work, including overtime hours, and provides a salary that is explicitly derived from both a rate for hours worked up to 44 and a time and one half rate for hours worked over 44. If such an approach is taken, an employment contract which provides for more than 48 hours in a work week would also generally require approval of the Director of Employment Standards[9].

b. Trade offs

Employers may seek to trade off overtime for other rights or benefits, such as bonuses or vacation time; however, such attempts will likely fail. For example, a contract which provides that the employee will not receive overtime but instead will receive a bonus for extra work or additional vacation will not be enforced. Generally, a contract providing for a bonus or vacation beyond ESA minimums will be considered a greater right or benefit and it cannot support an attempt to contract out of the ESA right to overtime.

In *Kyle v. Price Business Development Corporation,* 2010 ONSC 3567, cited above, the employer sought to rely on a policy for administrative employees that provided that employees would receive an additional week of vacation per year and employees would not then receive overtime for the first 40 hours of overtime worked within a year. This was held to contravene the ESA.

[9] Sections 17 and 17.1 ESA

c. Lieu Time

The ESA does allow employers and employees to agree to compensation for overtime hours as lieu time rather than overtime pay. Lieu time is to be provided at time and one-half and is to be taken within three months of when it is earned or with an employee's further agreement within 12 months of the week in which it is earned. Section 22 of the ESA states:

> 22(7) The employee may be compensated for overtime hours by receiving one and one-half hours of paid time off work for each hour of overtime worked instead of overtime pay if,
> (a) the employee and the employer agree to do so; and
> (b) the paid time off work is taken within three months of the work week in which the overtime was earned or, with the employee's agreement, within 12 months of that work week. 2000, c. 41, s. 22 (7).
>
> (8) If the employment of an employee ends before the paid time off is taken under subsection (7), the employer shall pay the employee overtime pay for the overtime hours that were worked in accordance with subsection 11 (5). 2000, c. 41, s. 22 (8).

Contracts of employment or employer overtime policies will sometimes include "use it or lose it" clauses or lieu time caps. An employment contract or policy which provides that lieu time is forfeited if it is not used within a certain time frame would breach the ESA as such a clause could result in an employee not being compensated for overtime worked. This was the case in *Ontario Nurses Association*, [1998] O.E.S.A.D. No. 199 referred to above. In that case, the contract in question limited an employee's ability to carry forward lieu time from one calendar year to the next. Similarly, provisions that place a limit on the number of lieu hours that may be accumulated thereby result in overtime being worked that is not added to an employee's banked hours would breach the ESA. Finally, a contractual provision which provided that lieu hours have no cash value on termination would also breach the ESA as Section 22(8) of the ESA requires payment for overtime hours banked which have not been taken when employment ends.

d. Contracts Requiring Prior Authorization for Overtime

Contracts and policies will often require pre-approval for overtime work. However, where an employment contract or policy states that overtime pay will not be paid unless pre-approval to work the overtime is obtained, this may breach the ESA overtime provisions.

Prior approval of overtime, and recording of overtime hours, are at issue in two major class action lawsuits brought by bank employees, *Fresco v. CIBC,* 2012 ONCA 444 (CanLII) ("*Fresco*") and *Fulawka v. Bank of Nova Scotia*, 2012 ONCA 443 ("Fulawka"). These cases involve federally regulated employees and, as such, they are being litigated under the *Canada Labour Code* ("CLC"), rather than the ESA. The plaintiffs allege that their employers' failure to implement record-keeping systems, and policies that require all overtime hours to be pre-approved by management resulted in Scotiabank and CIBC systematically avoiding their obligations to pay overtime under the CLC. Given the similarities in these two cases, the Ontario Court of Appeal

released judgment for both *Fulawka* and *Fresco* on the same day. There are leave to appeal applications pending before the Supreme Court of Canada in both cases.

The plaintiffs relied on Section 174 of the CLC which provides that "[w]hen an employee is required or permitted to work in excess of the standard hours of work, the employee shall … be paid for the overtime at a rate of wages not less than one and one-half times his regular rate of wages." Sections 252(2) and 264(a) of the CLC and accompanying regulations under the CLC require employers to accurately record all hours worked by employees, and to keep these records for at least three years.

In *Fresco*, the policy in issue defines employees "eligible for overtime pay" as those who received pre-approval to work more than 8 hours in a day or more than 37.5 hours in a week. The policy specifically states that overtime hours for which prior management approval was not obtained "will not be compensated unless there are extenuating circumstances and approval is obtained as soon as possible afterwards." The plaintiffs in *Fresco* alleged four deficiencies with employer's overtime compensation system as follows:

1. CIBC's overtime policy and practice unlawfully restricts overtime compensation;
2. CIBC discourages class members from claiming overtime to which they are entitled;
3. CIBC fails to record the overtime hours that class members work; and,
4. CIBC fails to ensure that class members are prevented from working overtime that CIBC does not intend to compensate

In *Fresco*, Chief Justice Winkler held that a pre-approval requirement for overtime hours went against the language "required or permitted" as stated in the definition of overtime work in the CLC. By providing that only pre-approved overtime would be paid, the banks had created a narrower obligation than their statutory duty. While *Fresco* is a class action certification decision, Chief Justice Winkler stated that "it is arguable that the pre-approval requirement in CIBC's current Policy served as an institutional impediment to claims for overtime that would otherwise have been compensable under s. 174 of the CLC."

The ESA provisions dealing with when work is deemed to be performed are similar to those under the CLC. Work is deemed to be performed when it is "permitted or suffered to be done." Section 6 of Regulation 285/01 of the ESA states:

> 6(1) Subject to subsection (2), work shall be deemed to be performed by an employee for the employer,
> (a) where work is,
> (i) permitted or suffered to be done by the employer, or
> (ii) in fact performed by an employee although a term of the contract of employment expressly forbids or limits hours of work or requires the employer to authorize hours of work in advance;

Further, the ESA places obligations on an employer to keep records of hours worked by employees. Specifically, Section 15 of the ESA states:

15(1) An employer shall record the following information with respect to each employee, including an employee who is a homeworker:

…

4. The number of hours the employee worked in each day and each week.

…

Exception

(3) An employer is not required to record the information described in paragraph 4 of subsection (1) with respect to an employee who is paid a salary if,

(a) the employer records the number of hours in excess of those in his or her regular work week and,

(i) the number of hours in excess of eight that the employee worked in each day, or

(ii) if the number of hours in the employee's regular work day is more than eight hours, the number in excess; or

(b) sections 17 to 19 and Part VIII (Overtime Pay) do not apply with respect to the employee. 2000, c. 41, s. 15

The ESA goes further than the CLC in that it provides that even where a contract purports to forbid or limit hours to those authorized in advance by the employer, work will still be deemed to be performed with wages payable when it is performed.

In *TCS Express v. Yasin,* 2006 CanLII 19423 (ON LRB), the Ontario Labour Relations Board confirmed that the failure to obtain pre-approval for overtime does not disentitle an employee to compensation. The employer submitted that the employee's overtime was unauthorized as the company policy required the employee to seek written permission before working any overtime. The employer sought to rely on its policy for pre-approval of overtime; however, the Board rejected that defence and held that the "deemed work" provisions in section 6 of Ontario Regulation 285/01 provided that the work performed by the employee was compensable even if it was performed in violation of company policy. The Board held that the employer was free to discipline the employee for violating its overtime policy, but denying her overtime pay was not available given the legislation.

Employment contracts and policies which deny payment for overtime hours worked where pre-approval has not been obtained are at odds with Section 6 of Regulation 285/01 of the ESA. An employer can put in place a system for pre-approval and discipline employees for failing to follow the policy; however, denying overtime pay in the absence of pre-approval would violate the ESA.

IV. Layoff

The ESA allows for temporary layoffs without triggering the obligation to pay ESA termination and severance pay. However, there is no common law right to layoff an employee. Consequently, it is well settled that, in the absence of a contractual provision permitting temporary layoff, an employee who is laid off would have a claim for constructive dismissal. This principle was clearly stated in *Elsegood* v. *Cambridge Spring Service (2001) Ltd.*, [2011] ONCA 831 (Canlii), a recent decision of the Ontario Court of Appeal.

Elsegood considered the intersection of the ESA and common law within the lay-off context. The employee in *Elsegood* was laid off twice. When the cumulative period of lay-off reached 35 weeks, the employee brought a claim for common law wrongful dismissal damages. The employer took the position that the ESA and common law are independent regimes and argued that notwithstanding the layoff for 35 weeks and termination under the ESA, the employee could be on a "prolonged indefinite layoff" at common law. The Court Appeal rejected this position and the argument made in support that the ESA and common operate as independent regimes. The termination of employment under the ESA layoff provisions is a termination for all purposes, both ESA and common law.

Further, in relation specifically to contracts of employment, the Court stated:

> At common law, an employer has no right to layoff an employee. Absent an agreement to the contrary, a unilateral layoff by an employer is a substantial change in the employee's employment, and would be a constructive dismissal.

The Court also addressed the employer's argument that the contract of employment contained an implied term allowing an employee to be placed on indefinite layoff subject to recall. The Court held:

> For the purposes of this discussion, I proceed on the basis that the employment agreement in this case had an implied term allowing the employer to place the employee on indefinite layoff exceeding 35 weeks in a 52 week period. The minimum standard of the ESA is that layoff amounting to 35 weeks in 52 results in the termination of employment. Since the indefinite layoff provision of the agreement fails to meet the ESA's minimum standard, it is null and void. The term is not read down to allow a layoff limited to 35 weeks in 52, but is excised from the agreement. The result is that the employment agreement is left without a term allowing any layoff at all and, if the common law applied, the employee could claim constructive dismissal as of the first day of the layoff.
> …
> A term in an employment contract that provides for a layoff exceeding 35 weeks without providing the employee with the election available under s. 67(3) would be null and void, because it fails to provide the minimum standard set out in the ESA.

As such, a contract of employment must either expressly or impliedly permit temporary layoff for layoff not to constitute a constructive dismissal. Further, a contract may not generally provide for a longer layoff than 35 weeks in 52 consecutive weeks as this would be a breach ESA and be unenforceable following *Machtinger*. Finally, a term in a contract which did allow for a layoff exceeding 35 weeks would need to provide an employee with right to elect as between termination and severance pay or to retain the right to recall in accordance with Section 67(3) of the ESA. Without the right to election, a contract allowing for layoff beyond 35 weeks without obligation to pay termination and severance pay would breach the ESA.

V. Conclusion

There are many ways in which contracts of employment and employment policies may run afoul of the ESA. The general principles – you cannot contract out of the ESA, a greater right or

benefit will prevail and civil remedies are not affected by the ESA – are well known. However, cases continue to be litigated demonstrating the challenges arising when contracts of employment and the ESA collide. While few employers fail to provide privies nowadays, the challenge of ensuring compliance with the ESA continues.