Court clarifies severance in M&As

Employers take note: Reasonable notice went under the microscope in an Ontario court recently, clarifying both an employee's rights and the employer's obligations when a worker is terminated shortly after a purchase agreement, writes **John Dujay**

WHEN buying a business, employers obviously face a myriad of considerations, but now they may be forced to look even more carefully at severance payments, in light of a recent Ontario Court of Appeals decision.

In the July 28 *Manthadi v. ASCO Manufacturing*, Justice Russell Juriansz ruled that the judge for the Superior Court of Justice erred in awarding a summary judgment during the previous trial for wrongful dismissal. The case was ordered to proceed to a new trial in front of the Superior Court.

At the heart of the dispute was the termination pay given to Sandra Manthadi, a welder who had worked for "63732 Ontario" since 1981. Manthadi was awarded $66,391 for damages for wrongful dismissal plus $11,958 for costs, but that judgment was overturned.

"The motion judge concluded summary judgment was appropriate primarily because she proceeded on an incorrect understanding of the common law that governs an employee's rights to reasonable notice from the purchaser of an ongoing business. This appeal presents the opportunity to review and restate the applicable law of Ontario," said Juriansz.

ASCO purchased the assets of 63732 Ontario in 2017 and terminated Manthadi's employment about a month later.

But Manthadi claimed that her employment with ASCO was indefinite and ongoing, while the employer said she had been hired on a fixed term solely to help with the transition.

"Absent a valid agreement limiting her notice from 637 to her Employment Standards Act (ESA) entitlement, the fact that the amount of the payment was less than the notice a long-term employee might have expected could support the inference that Manthadi understood she would be employed by ASCO on an indefinite basis and that she would successfully mitigate all of the damages from her termination by 63732. The motion judge erred in concluding the settlement and release agreement was not relevant," said Juriansz.

Vigilance is required

What should employers take away from the ruling? When a business is sold, the purchaser needs to be vigilant in assessing the liabilities that are attached to incumbent employees, says Mark Van Ginkel, an associate lawyer at Filion Wakely Thorup Angeletti in Toronto.

"Where employees are provided a severance package by the seller and then rehired by the purchaser, the employee's period of service with the seller is going to factor into the reasonable notice calculation if and when their employment is eventually terminated by the purchaser."

For employers that take over a new business, considering the correct amount to pay out in separation pay has become clearer after this ruling, according to Kyle Lambert, a partner in the advocacy and litigation group at McMillan in Ottawa.

> "The employee's period of service with the seller is still going to factor into the reasonable notice calculation."
>
> Mark Van Ginkel, Filion Wakely Thorup Angeletti

"What the court's worrying about here is that you might have somebody that had been employed for 10 years, 15 years, 20 years, who's been terminated, they've signed a release and they come on with the purchaser and then they're let go after six months and the purchaser says, 'We owe you a week, according to the ESA and maybe a little bit more for common law.'

The court is saying, 'No, that's not accurate,' because in that period of time, all of the skill, experience and knowledge that was built up with the vendor might have provided the purchaser with far more value than hiring somebody off the street," he says.

"That needs to be taken into account figuring out what termination entitlements are."

After a successful purchase agreement, wrongful dismissal cases such as *Manthadi* are commonplace, says Liam Ledgerwood, an associate in the labour and employment group at Siskinds in London, Ont., but this case is unique.

"It highlights the complexity of corporate transactions and asset transactions in particular, because the common law treatment of an asset transaction is exactly opposite to the Employment Standards Act treatment when it comes to continuity of employment," he says.

"There's an interruption of employment for the purposes of the common law, but there's deemed continuity of employment for the purposes of the ESA.

"The employee's prior experience with the vendor will still be considered by the court as one of the Bardal factors when they're assessing reasonable notice," says Ledgerwood.

The 1960 decision *Bardal v. Globe &*

MERGERS AND ACQUISITIONS POPULAR IN CANADA

2,967
Number of total corporate takeovers announced in Canada in 2019

$265 billion
Value of all mergers and acquisitions in Canada in 2019

63,413
Number of transactions announced by Canadian companies since 1985

Source: Institute for Mergers, Acquisitions and Alliances (IMAA)

Mail set out key factors to be assessed in determining reasonable notice, such as the type of employment, the length of service, the employee's age and the likelihood of finding future employment.

Severance not given undue consideration

Manthadi was paid out by 63732 Ontario, but "the weight given to the original severance was actually one of the issues that the Court of Appeal remitted back for reconsideration at a new trial, so it isn't really clear how much weight the severance is going to be given," says Van Ginkel.

But the amount paid out often reveals plenty, he says.

"A smaller severance might provide evidence that an employee expected continued indefinite employment with the purchaser, whereas a substantial severance package could possibly provide evidence that the employee expected to enter into a fixed term arrangement".

Manthadi was paid $5,900, "representing eight weeks' gross compensation in full satisfaction of all claims... including all severance pay, termination pay or other compensation howsoever arising," said the ruling.

Severance was noted by the appeals judge, says Ledgerwood, but it wasn't given undue consideration in the final outcome.

"The vendor and the employee had a purported settlement agreement under which the employee waived all claims that were related to employment issues and, in exchange, the vendor employer provided the employee with just under $6,000, which was about eight weeks of that employee's compensation — the maximum that she would have been entitled to under the ESA."

But the principle of privity of contract meant that ASCO might not be held liable, he says.

"The purchaser employer was not a party to that agreement because, in Ontario, the rule is if you're not a party to a contract, you generally can't rely on it. However, one interesting nugget is that, unlike the summary judgment decision, the Court of Appeal still held that $6,000 was one relevant consideration that would go into the reasonable notice analysis, because the Court of Appeal confirmed that employees generally shouldn't be entitled to double dip and receive termination pay that isn't offset in a later decision."

HR's role in managing payouts

Keeping track of termination entitlements by human resources would go a long way in preventing disputes after the purchase agreement is settled, says Ledgerwood.

"HR departments should be aware that length of service will be continuous for ESA purposes following the sale of businesses like this but not necessarily for common law purposes, and that specific steps can be taken during the transaction process to limit or recognize length of service for the common law purpose," he says.

"Tracking that length of service in internal HR systems to ensure that employers don't make any mistakes in the future when determining what an employee's ESA entitlements are would be important."

And human resources can be a key resource consoling the workplace after a purchase by "providing employees with assurances and almost being a safe space for employees who may be ill at ease as a result of the transaction," says Lambert.

"HR is generally not going to speak to the legal ramifications or issues relating to the interpretation of employee contracts, but there's that softer side of employee management and making sure that everybody knows that they're still rowing in the same direction." CHRR

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