



What's New in HR Law

Ontario Court of Appeal Rules that Severability Clause Cannot Save Void Termination Clause

December 8, 2017

BOTTOM LINE

The Ontario Court of Appeal ruled that an employer cannot rely on a severability clause in an employment contract to sever the invalid portion of a termination clause and allow the remaining portion of the termination clause to remain in force.

Facts: Employment agreement limited notice and severance pay to less than ESA minimums

The employee's employment was governed by an employment agreement. Under the sub-heading "Without Cause", the agreement limited the employee's entitlements to the minimum notice and severance pay required under the *Employment Standards Act ("ESA")*.

However, the termination clause concluded with the following statement:

In the event of the termination of your employment, any payments owing to you shall be based on your Base Salary, as defined in the Agreement.

The *ESA* requires that payment in lieu of notice and severance pay be calculated based on the *ESA* definition of “regular wages.” In addition to his salary, the employee also earned commission pay, which falls under this definition.

The employee argued that the agreement contracted out of a minimum entitlement provided for in the *ESA*. The *ESA* is clear that where parties attempt to contract out of or waive a minimum entitlement under the *ESA*, such contracting out or waiver is void.

The employee argued that the entirety of the termination clause was void, and as a result, his termination entitlements were not limited to the *ESA* minimum notice and severance pay.

Employer sought to rely on a severability clause

The employment agreement contained a severability clause, which stated:

If any part of the Agreement is found to be illegal or otherwise unenforceable by any court of competent jurisdiction, that part shall be severed from this Agreement and the rest of the Agreement’s provisions shall remain in full force and effect.

In defending the employee’s claim, the employer argued that if the sentence in the termination clause limiting termination entitlements to Base Salary offended the *ESA*, then the severability clause should operate to strike that sentence from the contract. This would leave the remainder of the termination clause intact and in force.

The Court’s Decision: The severability clause could not be used to save a portion of the termination clause

The Ontario Court of Appeal found that the severability clause could not be used to save a portion of the termination clause.

The Court relied on *Wood v. Fred Deeley Imports Ltd.*, 2017 ONCA 158 (“*Wood*”) and the oft-cited Supreme Court decision of *Machtiger v. HOJ Industries Ltd.*, [1992] 1 S.C.R. 986 for the proposition that where a termination clause contracts out of an employment standard under the *ESA*, the court is to find the entire termination clause to be void.

Applying this concept to the facts at hand, the entirety of the agreement’s termination clause was found to be invalid, not merely the sentence regarding “Base Salary.”

The Court indicated that there are sound policy reasons behind this interpretation. In reviewing *Wood*, the Court reiterated that the overarching theme in interpreting employment contracts is that there is inequality in bargaining power between employer and employee when an employment contract is negotiated.

As a result, the courts favour interpretations that “encourage employers to draft agreements that comply with the *ESA*.” If the only consequence for failing to comply with the *ESA* is that the contract is interpreted to be minimally compliant, then there is no such incentive. In this case, the employer’s proposed interpretation conflicted with this principle.

Check the Box

The Ontario Court of Appeal's reasoning is clear: courts will interpret employment contracts and the *ESA* in a manner that incentivizes employers to draft employment contracts that are compliant with the *ESA*. Therefore:

- Employers with non-compliant termination clauses in their employment contracts will not be able to rely on severability clauses to excise the invalid portions of a termination clause.
- If employers want to limit termination entitlements to less than the common law reasonable notice, they must take care to ensure that they do so in a way that does not offend the *ESA*.

Forum: Ontario Court of Appeal

Date: October 16, 2017

Citation: *North v. Metaswitch Networks Corporation*, 2017 ONCA 790

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