



Supreme Court issues first ruling on constructive dismissal

July 1, 1997

Employers restructuring their operations may have to consider altering the terms of employment for certain employees. If these changes are sufficiently significant, employees may be in a position to claim damages for constructive dismissal. In *Farber v. Royal Trust Company* (March 27, 1997), for the first time, the Supreme Court of Canada has ruled on a case of constructive dismissal.

In 1983, Farber held the position of Regional Manager for Western Quebec, and supervised 400 real estate agents working out of 21 offices; he earned \$150,000, of which \$48,800 was a base salary. All that changed in 1984 when his employer eliminated most of its Regional Manager positions. Farber was offered a position as a branch manager in the Dollard office, one of the least profitable in the province, from which he had been promoted eight years earlier.

As compensation, he was offered a \$40,000 reorientation allowance, a branch manager's commission which, for the remainder of 1984 and 1985 was to be higher than usual, and a lump sum payment of \$48,000 for commissions he had earned as Regional Manager in the first half of 1984. He would no longer receive a guaranteed base salary. Farber estimated that this package would cut his income by half.

Farber attempted to persuade the employer either to post him to a more profitable branch, or to offer a guaranteed base salary for three years. When the employer refused, Farber declined to take up his new duties, and instead sued for constructive dismissal.

LOWER COURTS: EMPLOYER'S OFFER REASONABLE

The trial judge, whose decision was upheld by a majority of the Quebec Court of Appeal, ruled against Farber, holding that the offer was reasonable both in terms of the compensation and the prestige of the new position.

In comparing Farber's previous position with that being offered by the employer, the trial judge, against Farber's objection, admitted into evidence the sales figures of the Dollard office for the second half of 1984. These sales figures far exceeded what even the employer had anticipated at the time it made its offer to Farber. As a result, the judge concluded, Farber would have suffered no loss in compensation had he accepted the new position.

SUPREME COURT OF CANADA: EMPLOYEE'S CONTRACT SUBSTANTIALLY ALTERED

A unanimous five-judge panel of the Supreme Court overturned the lower court rulings, and awarded



Farber one year's notice with interest from 1984, or some \$350,000.

To conclude that an employee has been constructively dismissed, a court must determine that the employer has unilaterally substantially altered the essential terms of the employment contract. To do this, the court held, it must ask "whether, at the time the offer was made, a reasonable person in the same situation as the employee would have felt that the essential terms of the employment contract were being substantially changed". The fact that the employee may have been prepared to accept some changes was not decisive, as the employee may have had other reasons for being willing to accept less than he or she was entitled to.

Nor was it necessary to find that the employer intended to force the employee to leave or that it was acting in bad faith, although such findings might influence the amount of damages awarded to the employee. In Farber's case, the court added, it was clear that the employer was acting in good faith in attempting to restructure its operations.

In surveying cases on constructive dismissal, the court noted that demotion, which generally involves a loss of status and prestige, amounts to a substantial change of the contract terms. A similar conclusion is justified when the employee's method of remuneration calculation is changed, or when the employee's income is significantly reduced.

Here, the court ruled, the employer's offer was a substantial alteration of Farber's contract. The new position was a serious demotion, with drastically reduced responsibilities and consequent loss of status and prestige. As well, the loss of a guaranteed salary was detrimental to Farber's financial security.

Turning to the question of salary level, the court held that Farber was fully justified in concluding that his income would be cut in half. The trial judge was wrong to have admitted "subsequent event evidence" of the Dollard branch's sales for the second half of 1984, as this upturn could not reasonably have been foreseen by Farber at the time the employer's offer was made. In relying primarily on evidence of subsequent, unforeseeable events to hold that Farber should have accepted the offer, the trial judge had strayed from the real issue: whether the offer substantially changed the essential terms of Farber's employment contract.

IN OUR VIEW

It is not clear that even if the court had admitted evidence of the improved sales figures, it would have found in the employer's favour. This is because the court held that the employee's loss of a guaranteed base salary and demotion were themselves sufficient to support a finding of constructive dismissal. This means that employers should consider the effect of their proposed changes on more than just employees' salary levels.

Not all changes to an employee's terms of employment will amount to a substantial change, of



course. The court stated that the employer can make any changes to an employee's position that are allowed by the contract, most notably as part of its discretion to exercise its managerial authority.

(For a similar case, see [“Court of Appeal says employee who refused transfer was constructively dismissed”](#) on our Publications page.)

For more information on this subject, please contact [Jacques A. Emond](#) at (613) 563-7660, Extension 224.