

**PERSPECTIVES ON SALARY CONTINUATION**

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## PERSPECTIVES ON SALARY CONTINUANCE

### **I. Introduction**

Employers, employees, and their advisors are vitally interested in developments in the law relating to the appropriateness of salary continuance. These considerations have until recently created significant settlement difficulties in many instances.

After termination, employers sometimes advance salary continuation offers, which are not accepted, and unilaterally pay continuance after dismissal. Employers then defend on the basis that the employee's action is not supportable, as no damages are suffered.

#### **The Typical Fact Situation**

"Salary Continuance" (or "Continuation") is a phrase used to discuss a situation which often arises after the termination by an employer of an employee. A practice has developed in the province of British Columbia where employers terminate employees without just cause, and with insufficient or no notice, and then advance an offer to the dismissed employee to continue payment of base salary and some benefits. The typical offer normally has the following elements:

1. The offer is normally based on continuance of base salary for a certain number of months;
2. Basic benefits may or may not be continued during the period salary continuance – but often not disability insurance, bonuses or other financial benefits;
3. Salary & benefits continuance normally ends when and if the employee finds and starts "alternative employment". At that time the employer is to pay a lump sum equivalent to 50% of the amount that would have been paid if continuance had carried on to the original end date;
4. The employee would sign a Release of claims;
5. Failing acceptance by the employee, the employer will unilaterally continue to pay salary continuance on the same terms.

There are of course many possible variations of the form of a salary continuance offer. For example:

- The offer might not mandate cessation of continuation until the full period elapses, (i.e. even if alternative employment is found);

- There might be a more precise definition of what is meant by “alternative employment” (e.g. with equal pay, not including short term consulting earnings, etc.);
- Upon the employee finding alternative employment, there could be a different outcome than cessation of continuance and payment of a lump sum (eg. perhaps recognition and deduction of some or all of the earnings from new employment).

It is of course open to employers and employees to voluntarily agree on a severance package based on salary continuance. That might be in the mutual interests of employer and employee in some situations, particularly where the employee is at the stage of choosing retirement or semi-retirement.

What is more interesting (and will be the situation that we address in this paper) is where, after wrongful dismissal, the employer advances an offer of salary continuance, which is not accepted, but then continues to pay continuation.

The question then is – *Can the employee obtain a remedy in court for damages to be assessed on a lump sum basis?*

The employer may argue that the employee cannot do so, that he/she is obliged to stand by, attempt to mitigate, and receive continuation until re-employment or expiry of the notice period.

## **II. Benefits of Salary Continuance from the Employer’s Perspective**

Employers often choose to pay salary continuation for various reasons, some of which may include:

- the employee may find alternative employment during the continuation period, and with the cessation of continuation, the employer incurs less overall expense;
- there are certain cash flow benefits to the employer when it is not required to pay a lump sum equivalent of damages at the time of dismissal;
- it permits the employer to continue some basic benefits economically as the employee continues to be part of the employer’s group benefits plan

## **III. Problems with Salary Continuance from the Employee’s Perspective**

Some of the reasons employees prefer lump sum damages award over continuation proposals are:

- most often, the salary continuance offers do not properly include all claim elements. (e.g. notice periods are not long enough, continuation is based on salary but only some benefits, (e. g. bonuses; pension are not included)
- Even with properly structured offers, the requirement that continuation ceases when the employee finds alternative employment creates a situation where the employee's interests are not finally settled. The employer could cease payments, on the basis that the employee had chosen not to accept available "suitable alternative employment", or failed to take reasonable efforts to locate employment. The employee is asked to depend on the employer's exercise of judgment, in circumstances where the employer has just breached the employment contract;
- employees in receipt of lump sum damage awards are potentially able to obtain new employment during the notice period, and thus be better off than they would have been if the employer had provided actual working notice.<sup>1</sup>
- There may be other unacceptable conditions attached, (e.g. confidentiality clauses; restrictive covenants)

#### **IV. Jurisprudence on Salary Continuance**

In the 1990s, the B.C. courts issued several decisions which rejected claims by employees for lump sum damages while in receipt of salary continuance.

- Spooner v. Ridley Terminals Inc. (1991), 39 C.C.E.L. 65 (B.C.S.C.)
- Marshall v. Artek Group Ltd. (1993), 47 C.C.E.L. 229 (B.C.S.C.)
- Polak v. Surrey Memorial Hospital Society [1996] B.C.J. No. 131 (S.C.)

Since Polak was decided, the judges in several B.C. cases have significantly limited the role of salary continuance.

- Light v. City of Richmond [1998] B.C.J. No. 102 (S.C.)
- Albach v. Vortek Industries [2000] B.C.J. No. 1650
- Moody v. Lafarge Canada Inc., 2000 BCSC 1847
- Leung v. MDSI Mobile Data Solutions Inc., 2002 BCSC 1597

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<sup>1</sup> It is interesting to note that even with an accepted (fully compensatory) salary continuation offer, the employee who obtains employment during the notice period would be better off, after receipt of the 50% lump sum. The typical continuation offer therefore is based on an assumption that it is appropriate for employees to receive something in addition to continuation, even where new employment is obtained.

#### IV. Recent Jurisprudence:

- **Richard Tull v. Norske Skog Canada Ltd.** 2004 BCSC 1098

In Tull, Judge Pitfield undertook a comprehensive review of the decided cases on the subject, summarized the effect of the jurisprudence to that time, and stated in clear language his own view that salary continuance ought not to bar a dismissed employee from obtaining judgement for damages payable on a lump-sum basis.

The plaintiff was a 14 year employee, who at the time of discharge was Mill Manager at Norske Skog's pulp and paper mill in Crofton, BC. He was discharged without cause, and the employer advanced an offer where Tull could choose either:

- (a) **Lump Sum Settlement** - This option would have involved the company paying a lump sum equivalent to 12.8 months of base salary without benefits.
- (b) **Salary Continuance** - The plaintiff would be placed on "Termination Leave" for a period of up to 16 months, or shorter if he found "alternative employment". This scenario involved continuation of base salary and only some benefits. There was a clause ending continuation if the plaintiff found "alternative employment", with a lump sum at that time of 50%

The offer also required Mr. Tull to sign a Release.

Mr. Tull chose not to accept either option, and action was commenced claiming payment of damages on a lump-sum basis.

The plaintiff argued that the court should grant a lump sum damage award, and not require the plaintiff to stand by receiving salary continuance because the offer:

- (a) was not equivalent to what the plaintiff would have received if he had been given working notice as it:
  - (i) was based on continuation for a maximum of 16 months – less than the appropriate notice period;
  - (ii) did not include any payment for bonus, and the bonus was the sort that ought to have been included;
  - (iii) did not include certain benefits. The omitted benefits were excess and family life insurance, short and long term disability Insurance, 24 hour travel accident insurance and automobile fuel reimbursement;

- (b) included a requirement that payments cease if (vaguely defined) “alternative employment” was found;
- (c) involved an arbitrary 50% lump sum on benefits continuance;
- (d) required the plaintiff to execute a Release.

The main point advanced on behalf of the plaintiff was that the defendant had breached the employment agreement, and was liable to judgment for damages for breach of contract. Those damages were to be assessed at the time of trial and quantified according to the principle in *Nygaard International v. Robinson* 46 B.C.L.R. (2d) 103 (BCCA) (judgement to be granted for an amount of money sufficient to place the plaintiff in the position he or she would have been in, given proper working notice).

Defendant’s argument that a lump sum damage award might confer a windfall on the plaintiff was met by the submission that:

1. the risk was created by the defendant breaching its contractual obligation to give actual working notice – the defendant had missed its chance to avoid the risk;
2. when damages were assessed, the court could, in an appropriate case, make a reduction for the contingency that the plaintiff would successfully mitigate.

In *Richard Tull v. Norske Skog Canada Ltd.* 2004 BCSC 1098, Mr. Justice Pitfield summarized jurisprudence to date on the subject of salary continuance:

[47] In *Cooper*, supra, reasons released May 29, 1991, Esson C.J.S.C., as he then was considered whether an employer was entitled to continue to pay salary during the period of reasonable notice. As in the present case, a salary continuance arrangement option and lump sum severance option had been offered to the employee who accepted neither. At p. 344 the learned Chief Justice said the following:

In this case, I think it unnecessary to get into the complexities of constructive dismissal. What took place on October 29, 1990, was accurately described by the division manager when he said that Mr. Cooper was "terminated as of right now". The fact that the employer offered, as one of two options, to keep the employee on payroll for 12 months did not affect the reality of the transaction. Any possible doubt about that is removed by the alternative offer of a lump sum payment equal to 10 months salary. Those were two ways of offering to meet the employer's obligation to pay a reasonable amount in lieu of notice. Neither offer having been accepted by Mr. Cooper, he was free then to bring action.

The next question is whether the amount offered was sufficient to meet the company's obligation. I do not think it is correct to describe the offer, as the company now does, as one equivalent to 12 months' notice. The lump sum offer was based on 10 months. The offer to keep Mr. Cooper on payroll was subject to the onerous term that his salary and benefits would cease were he to "commence other employment".

[48] In MacDonald v. Woodward Stores Ltd. (1991), 39 C.C.E.L. 58, reasons released August 27, 1991, Campbell A.C.J. addressed the argument that the Chief Justice, in Cooper, had found nothing wrong with salary continuance arrangements. The learned Associate Chief Justice addressed the claim as follows at p. 61:

The defendant suggests that the Chief Justice, in Cooper, did not find anything objectionable to salary continuance as a means of an employer meeting its severance pay obligations and that he, in effect, confirmed its legitimacy. Thus, it says, that since the options offered the plaintiff here were fair and reasonable considering the plaintiff's position and length of service, the defendant's obligations have been met and the plaintiff has no basis on which to bring this action.

I cannot agree with this submission. At best, the Chief Justice gave equivocal support to the notion that salary continuation does not offend an employee's rights. He said of the options given Cooper "those were two ways of *offering* to meet the employer's obligation ..." [emphasis in original]. He did not say that they were both legitimate means of achieving that result at law. Indeed, later in his reasons he treated salary continuation as the lesser of the two offers due to the "onerous" term dealing with mitigation and the premature loss of coverage upon re-employment, and also found the alternate offer of ten months' salary in lieu of notice inadequate in the particular circumstances.

The Chief Justice makes it clear in Cooper that where an employee is not prepared to accept severance terms or a choice of severance packages offered by an employer, he is "free then to bring [an] action" (p. 5 quoted supra). I find myself in full agreement with him despite the persuasive submissions to the contrary on behalf of the defendant. It makes no difference in this regard whether Cooper is, as the defendant suggests, a dismissal for cause case.

[49] With respect to the reasonableness of either offer made to the employee in the case before him, the learned Associate Chief Justice wrote as follows at p. 62:

The options offered, as noted earlier, were a maximum 54 weeks salary continuance, payable bi-weekly with conditions similar to those

characterized as "onerous" in Cooper, or a lump sum equal to six months salary.

Do either of these options fall within the range of a reasonable notice or salary in lieu thereof? Clearly, the six month offer does not. In terms of dollars alone, the 54 week offer is roughly equivalent provided the payment continued for that entire period. While it also includes various benefits, there are "onerous" conditions, including the cessation of the payments and benefits upon obtaining new employment. In addition, bi-weekly written reports from the plaintiff of his efforts to obtain employment are required.

Given these factors, it is difficult to determine the true value to the plaintiff of the salary and benefit continuation option. However, an exact determination is not necessary in these circumstances since whatever that value is, it is, in my opinion, significantly less than the 12 months which I have determined to be reasonable notice the plaintiff was entitled to receive.

The defendant suggests that if it has given adequate notice regardless of how payment in lieu thereof is made, there is no breach for which it can be held liable. This argument overlooks the fact that, as stated earlier, the conditions attached to the salary continuance option reduce its effective term to significantly less than 12 months.

[50] Neither the Cooper nor the MacDonald decision denies the employer use of a salary continuance arrangement, but neither looks favourably upon such an arrangement.

[51] The issue was next considered by MacDonald J. in Spooner v. Ridley Terminals Inc. (1991), 62 B.C.L.R. (2d) 132, reasons released December 2, 1991. The learned trial judge wrote as follows at pp. 137-138:

I see no reason in principle to reject salary continuance as a proper means of paying the damages which flow from the termination of employment without reasonable notice. No reason, that is, so long as the salary continuance is equivalent to the damages which would be fixed by a court for such a breach.

By doing so, an employer can avoid the accumulation of pre-judgment interest on the amounts so paid. There is even an attractive argument that the periodic nature of salary payments during employment suggest salary (and benefit) continuance as the most appropriate means of paying such damages. Salary continuance also avoids such questions as present value (see below) and future possible mitigation arising from alternate employment.

The defendant urges upon me the proposition that "termination of employment alone is not a breach of contract". It argues that if an employer correctly estimates the reasonable notice period and pays the salary and benefits due for that period, no breach has occurred. That argument is designed to provide a foundation for the "reasonable offer" doctrine discussed below since it avoids the need to characterize post-termination payments as damages.

Even though I accept that the law does not in most cases require an employer to provide work during the notice period (See Park v. Parsons Brown (1989), 39 B.C.L.R. (2d) 107 (C.A.)), I prefer the plaintiff's characterization of what occurs when employment is terminated on less than reasonable notice. Termination in such circumstances is a breach of the employment contract. Even where the employer elects to pay in lieu of notice and pays more than the court awards, there has been a breach. But in that case, the employee's action will be unsuccessful because he has already received adequate damages for the breach.

While Cooper and Macdonald [cites omitted] do not embrace the salary continuance alternative with much enthusiasm, I do not read either of those decisions as rejecting that alternative. I agree with the plaintiff's submission that the issue is not whether there has been a breach of the employment contract (assuming termination on less than reasonable notice) but rather what damages flow as a consequence of that breach.

In both Cooper and Macdonald the court found that the conditions attached to salary continuance in those cases (cessation on re-employment) rendered such offers less valuable than a lump sum payment calculated on an equivalent period. I do not have that difficulty with the form of the salary continuance offered here. Had the initial offer been for a 12 rather than an 8 month term, the 50% reduction and cessation of health benefits on reemployment would not have prevented me from accepting such payments as adequate compensation (subject, of course, to the "productivity award" discussed below). And I am assuming that any contributions by the defendant to the plaintiff's pension would continue in proportion to the amounts she was entitled to receive monthly under salary continuance, both before and after re-employment.

[52] In Spooner, the learned trial judge modified the salary continuance arrangement by increasing its duration to coincide with his determination of the reasonable notice period. At the same time, he awarded damages in relation to the 'productivity bonus' payable forthwith.

[53] In Marshall v. Artek Group Ltd. (1993), 47 C.C.E.L. 229, Meredith J. followed Spooner, supra, and held that a salary continuance arrangement was a

proper means of paying damages “which flow from the termination of employment without reasonable notice”. It removed “most, if not all, of the speculation implicit in a lump sum award”. Having so found, the learned trial judge said the following at p. 233:

I am not sure that the court has jurisdiction to make an order for future payments short of enforcement of a judgment. So in the present case, insofar as salary continuance is concerned, I order that the application for lump sum judgment be *adjourned* generally with liberty to the plaintiff to apply if, as, and when, the defendant discontinues the payment of salary and benefits before the expiration of the notice period. I do not carry the terms of the offer of the defendant to the plaintiff into this part of the order.

[54] In Polak v. Surrey Memorial Hospital Society (1996), 17 C.C.E.L. (2d) 283, Cohen J. endorsed a salary continuance arrangement that was to extend for a period of 17 months which was the reasonable notice period stipulated by the employer. The learned judge ordered the employer to continue to pay the amounts stipulated in the salary continuance arrangement and adjourned the application for lump sum judgment generally with liberty to the plaintiff to apply if the employer discontinued the payments contemplated by it.

[55] In Albach v. Vortek Industries Ltd. (2000), 79 B.C.L.R. (3d) 353, reasons released August 14, 2000, Brooke J. concluded that “salary continuance with the condition of the reduction of the payments during the notice period if new employment is obtained requires the employer, and may permit the court, to look to the higher end of the appropriate range [of the period of reasonable notice]”. On the facts before him, the learned judge determine that the notice provided to the employee was unreasonable, the dismissal was therefore wrongful and he saw no reason to depart from the principle that damages are awarded in a lump sum once and for all.

[56] Finally, in Moody v. Lafarge Canada Inc., [2000] B.C.J. No. 2678, 2000 BCSC 1847, reasons released December 21, 2000, Hunter J. dealt with the employer’s claim that it should be entitled to continue to pay salary on a monthly basis over whatever term the court considered appropriate as follows at paras. 25-26:

I am not satisfied that a salary continuance is appropriate. Lafarge terminated the plaintiffs’ employment which it was entitled to do. It did not however provide reasonable notice of that. Instead Lafarge advised the plaintiffs that they would no longer be employees as of April 28, 2000. The breach by Lafarge is in failing to give reasonable notice. The plaintiffs’ claim for damages is based on a calculation of the notice period multiplied by their monthly salary. There is no agreement to accept payment of a salary continuance in the event of dismissal nor an acceptance by the plaintiffs,

upon their employment termination, of payment on a monthly basis for the appropriate notice period.

In the circumstances I have concluded that the plaintiffs are entitled to judgment in a lump sum and should not have to wait for payment of that judgment amount spread over a period of months following the judgment.

After this comprehensive review of BC cases on the subject of salary continuation, a review which clearly shows that different judges have had different approaches to the issue, Judge Pitfield clearly set out his own perspective (reformatted for emphasis) at para. 60:

“In my opinion,

- the principle that damages must be assessed on a once and for all, one-time basis,
- the requirement that the court resort to a kind of mandatory injunction or adjourn judgment to a point following expiry of the notice period if the effectiveness of a salary continuance arrangement is to be assured, and
- the fact that a salary continuance arrangement to which the employee does not agree reflects the employer’s attempt to unilaterally amend the employment contract,

suggest that such arrangements should not be endorsed as a means of compensating an employee for damages in a wrongful dismissal action.”

Then, mindful of the need to dispose of the case in accordance with guiding precedent, Mr. Justice Pitfield distilled the “relevant principles” at para. 61:

1. A contract of employment, otherwise silent on the manner of termination, may be terminated by providing reasonable working notice, or upon payment of a lump sum in lieu of reasonable notice: Ansari, *supra*.
2. The amount payable in lieu of working notice must include all compensation that would have been received in, or in respect of, the reasonable period of working notice and an amount that will permit replacement of employment benefits that would have been enjoyed in the period of working notice had such benefits not been terminated: Ansari, *supra*.
3. The employer’s failure to properly determine the amount payable as a lump sum in lieu of working notice will permit the terminated employee to commence an action for wrongful dismissal. In that action, damages will ordinarily be assessed as a lump sum in satisfaction of all claims. The amount assessed in relation to lost benefits from employment will normally be

determined by reference to the cost incurred by the employee to replace the benefit or, where the lost benefit has not been replaced but the court is persuaded on the balance of probabilities that they will be replaced, the reasonable cost that will be incurred to procure the replacement: Cooper, supra; Wilks, supra; MacDonald, supra.

4. The court may, in its discretion, endorse the use of an employer- imposed salary continuance arrangement as a means of providing the employee with payment in lieu of notice provided the amount determined by the employer to be payable on its terms is a reasonable reflection of that which the employee has lost as a result of not being provided with working notice: Spooner, supra; Polak, supra.

The specific disposition of the Tull case is found at paras 62 and 63:

“In my opinion, discretion should only be exercised in favour of a salary continuance arrangement if the amount to be paid to the employee in accordance with its terms is equivalent to that which the employee would have received had he or she been dismissed with working notice: Spooner, supra.

In the circumstances of this case, I would not exercise discretion to permit continuation of the salary continuance arrangement because (format restructured for emphasis) of:

- of the substantial departure in the notice period as determined by the employer from that which was reasonable,
- the failure to properly compute lost income by omitting short term incentive plan compensation,
- the omission to appropriately compensate for certain of the lost employment benefits,
- the omission to compensate for lost pension benefits,
- the omission to adequately define ‘alternative employment’ that would result in a reduction in the monthly payments stipulated in the salary continuance arrangement, and
- the arbitrary nature of the 50% reduction in the event alternative employment were obtained.”

And then, the learned judge made general comments which, if consistently applied by other judges, will likely mean the end of salary continuance in any circumstances other than where the employee agrees (para. 64 and 65):

“The reduction in the event that ‘alternate employment’ is found does not properly reflect the employee’s obligation to mitigate and, in any event, invites disagreement on the meaning of ‘alternate employment’. An employee who has been terminated should not be discouraged from undertaking any work he is prepared to pursue in the notice period. Acceptance of employment that provides less than one-half the employee’s base salary would result in an excessive reduction to overall compensation in the notice period. It is no answer to say that this, or any other reduction, provides certainty in relation to mitigation while a one-time assessment of damages does not. I prefer the approach adopted by Bouck J. in *Smith*, supra. The adjustment for the contingency of mitigation is a matter of assessment by the court just as contingencies are the matter of assessment in various aspects of personal injury awards.

Acceptance of salary continuance arrangements, whether in the exercise of discretion or otherwise, represents a modification of the established principle that damages for wrongful dismissal are to be assessed as a lump sum, once and for all. Whether the law can and should be revised in that manner is a topic that should be addressed by the Court of Appeal.”

The logical extension of this thinking is that the only way an employer could impose salary continuation on an unwilling employee is if there was no “clawback” clause”; where the offer is such that the employee is promised continued payments for the full notice period.

#### **IV. Conclusion:**

Although Judge Pitfield in *Tull v. Norske Skog* clearly expressed his view that the normal rule for assessment of damages for breach of contract requiring a once and for all lump sum damage award was preferable, there remains in BC support for the existence of a discretion for a court to permit salary continuance.

However, the discretion is to be exercised in accordance with judicial principles developed in the cases, and those principles are such that it is unlikely that the employer would be able to achieve any benefit by advancing a suitable salary continuance offer.

Nevertheless, voluntary salary and benefit continuation agreements may still suit the needs of employers and employees in individual instances, particularly for employees near the end of their working life, as this may permit more efficient benefits continuation.

Dan Gleadle, CLE Employment Law Conference, April 2005