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TAKING THE RISK OUT OF TERMINATION: AN ENTERPRISE RISK MANAGEMENT ANALYSIS OF THE NORMATIVE SYSTEM OF EMPLOYMENT STANDARDS CHALLENGED BY *HONDA v KEAYS*

Ryan Henry Edmonds*

*“Work is one of the most fundamental aspects in a person's life, providing the individual with a means of financial support and...a contributory role in society. A person's employment is an essential component of his or her sense of identity, self-worth and emotional well-being.”*¹

- Chief Justice Dickson, 1987

INTRODUCTION

Over many years, Canadian courts have crafted a unique body of employment law jurisprudence. The purpose of this paper is to discuss how that jurisprudence was unraveled when the Supreme Court of Canada rendered its decision in *Honda v. Keays*.² That holding, in effect, overturned aspects of *Wallace v. United Grain Growers*;³ a case that transformed how non-unionized employees were thought of and treated in Canadian society. This paper examines the analytical underpinnings of wrongful dismissal law's previous regime on bad faith damages and juxtaposes it to the new regime in *Keays*, concluding that the shift in focus from employer misconduct to employee losses exacerbates the employment relationship's power imbalance and deprives employees of protection when they need it the most. In reaching this conclusion, the paper uses the analytic frameworks of reflexive regulation and enterprise risk management to predict how employers will react to their newfound advantage. The finding is that by taking the risk out of termination, there is now downward pressure to do away with the normative

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¹ *Reference Re Public Service Employee Relations Act (Alta)*, [1987] 1 SCR 313 at 368.

² 2008 SCC 39, [2008] 2 SCR 362 [“*Keays*”].

³ [1997] 3 SCR 701 [“*Wallace*”].

“upwardly ratcheting” system of employment standards that workplaces enjoyed under *Wallace*.

EXPLAINING CORPORATE BEHAVIOUR: RISK AND REGULATION

i. Theories of Regulation: Centralized and Reflexive Regulation

Academic literature posits two kinds of regulatory force: “centralized” (or “command and control”) regulation and “decentered” (or “reflexive”) regulation. In either case, the state’s purpose is to exert influence over how the target entity comports itself. Whether it is centralized or reflexive regulation, this is done by creating a situation where risk management, with respect to that influence, is prioritized vis-à-vis other competing objectives.⁴

With centralized regulation, the state’s intention is to strictly hold the target to a set of rules. If not followed, then the rules are enforced by subjecting the target to sanctions.⁵ Thus, the decision-making process with respect to centralized regulation is for the target to prioritize rule compliance for fear of punishment. Consider employment standards legislation,⁶ which sets out terms of the employment relationship that employers must observe. Typically this includes limiting working hours,⁷ setting a minimum wage,⁸ statutorily protecting leaves of absence,⁹ and requiring that appropriate notice of termination be given.¹⁰ Centralized regulation posits that an employer will comply with employment standards because the risk of sanctions is greater than any profit that could be derived from non-compliance.¹¹

Reflexive regulation, which is the focus of this paper, operates quite differently. With the centralized approach, there are limits in terms of jurisdiction and substance as to what may be regulated.¹² The state may have a preference for certain conduct, but for one reason or another, it may be inappropriate or impossible to enforce this preference with a sanction. In such cases, scholars argue that reflexive regulation holds the answer.¹³ Rather than compelling conduct with sanctions, reflexive regulation operates

⁴ Bridget M. Hutter and Clive J. Jones, “From Government to Governance: External Influences on Business Risk Management” (2007) *Regulation & Governance* 27.

⁵ *Ibid.*

⁶ See e.g. *Employment Standards Act, 2000*, SO 2000, c 41.

⁷ *Ibid.*, s 17.

⁸ *Ibid.*, s 23.

⁹ *Ibid.*, ss 46-53.

¹⁰ *Ibid.*, ss 54-66.

¹¹ *Ibid.*, s 133-139. Also, certain remedies prescribed for certain standards have a normative element as well. See s 53, which permits reinstatement for breaches of statutory leaves. For an empirical analysis of the questionable effectiveness of reinstatement as a remedy for employment disputes in Quebec, see Gilles Trudeau, “Is Reinstatement a Remedy Suitable to At-Will Employees?” (1991) 30 *Indus Rel* 302.

¹² David J. Doorey, “Who Made That?: Influencing Foreign Labour Practices through Reflexive Domestic Disclosure Regulation” (2005) 43 *Osgoode Hall LJ* 353 at 366 [Doorey, “Who Made That?”].

¹³ *Ibid.*

by influencing the target's normative practices by shaping the context in which interaction occurs.¹⁴ A classic example is the American *Home Mortgage Disclosure Act*,¹⁵ which requires lending institutions to disclose a racial breakdown of loan recipients in order to discourage racially preferential lending practices.¹⁶ The logic is that by making a breakdown of loan recipients public record, this information could be used to antagonize malevolent lenders. By creating a risk of public shaming, the intent is to influence lending practices by making the target prioritize compliance vis-à-vis any profit it could derive from the discouraged course of action. In other words, reflexive regulation posits that by injecting risk into the decision making process, a corporation's behaviour will be steered towards the preferred course of conduct.¹⁷

Reflexive regulation's application to labour law is not new, however discussion of it has previously been confined to issues of transnational labour regulation. David Doorey has argued that if disclosure of apparel manufacturers' factory locations were required, employers would improve labour standards for fear of the risks created by NGO groups exposing "sweatshop" conditions.¹⁸ In an alternative vein, Sabel, O'Rourke and Fung propose a "ratcheting" theory of transnational labour standards.¹⁹ This theory is premised on requiring corporations to disclose information on labour standards to transnational monitoring groups, who in turn rank the firms according to certain indicia. The idea is that high profile companies would compete to build their reputation as socially responsible actors, and the competition would result in a transnational "upward ratcheting" of voluntarily adopted labour standards. In what follows, this paper proposes that Canadian workplaces previously enjoyed a hybrid form of normative "ratcheting" labour standards via the risks associated with the ubiquitous threat of *Wallace* damages. However, since *Keays* has taken much of the risk out of termination, it is argued that this system of reflexive regulation is no longer in effect.

ii. Theories of Risk: Enterprise Risk Management

For reflexive regulation to have any normative force, the target must perceive (and prioritize) risk in the situation it is faced with.²⁰ Consequently, this paper will interpret

¹⁴ *Ibid.*

¹⁵ 12 USC 2800.

¹⁶ Doorey, "Who Made That?" at 373.

¹⁷ David J. Doorey, "Can Factory List Disclosure Improve Labor Practices in the Apparel Industry? A Case Study of Nike and Levi-Strauss" (2008) [unpublished], online: CLPE Research Paper Series 1 <http://www.comparativeresearch.net/index.jsp> at 8 [Doorey, "Factory List Disclosure"].

¹⁸ See generally, David J. Doorey, "In Defence of Transnational Domestic Labor Regulation" (2010) *Vanderbilt J of Trans L* 953; Doorey, "Who Made That?"; Doorey, "Factory List Disclosure".

¹⁹ Charles Sabel, Dara O'Rourke and Archon Fung, "Ratcheting Labor Standards: Regulations for Continuous Improvement in the Global Workplace" (2000) KSG Working Paper Number 00-010, Columbia Center for Law and Economic Studies.

²⁰ Ryan Henry Edmonds, "Reflexively Regulating International Labour Practices: Are We There Yet? An Enterprise Risk Management Analysis of Social Disclosure" (2010) [unpublished, submitted in fulfillment of 'International and Comparative Labour Law' (3040.3N) at Osgoode Hall Law School] online: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1737931.

the risk component of reflexive regulation in accordance with the principles of Enterprise Risk Management (“ERM”).

The individual components of ERM have long been functions of sound business management, but ERM as a cohesive discipline and function of senior management emerged only recently.²¹ In response to public pressure from the collapse of Barings Bank and other financial disasters of the 1990s, public-private consortium groups published a number of guidelines on best accounting practices for internal financial risk controls.²² Notably, however, these guidelines also urged companies to go beyond financial risk and to begin accounting for risks posed by law, health and safety, the environment, reputational damage, and so on.²³ As a result, ERM as an independent, cohesive discipline emerged from the amalgamation of financial risk, operational risk, and strategic risk. Although ERM is prescribed for banks and other financial institutions,²⁴ policy makers have strongly recommended that all businesses adopt it as a matter of good corporate governance,²⁵ making it a useful framework for present purposes.

In order to appreciate an employer’s response to the new requirements for *Keays* damages, it must be emphasized that ERM is not merely a discipline aimed at risk mitigation. Rather, ERM’s service to a company lies in its value-creation function because ERM is uniquely positioned to exploit risk-generating events in a way that advances the company’s interests.²⁶ For example, consider risk hedging; once an ERM practitioner identifies a risk to the company, he or she will undertake another risky activity in order to offset that risk. Insurers who hedge mortality risks by selling both life insurance and business annuity insurance to the same customer group are the classic example of this.²⁷ As businesses exist to derive profit for their shareholders, ERM’s propensity for value-creation makes it a useful framework to examine and predict employers’ responses to *Keays*.

The three disciplines within ERM are financial risk, operational risk, and strategic risk. Each is an independent discipline in its own right, but they are joined together under the

²¹ See eg, Casualty Actuarial Society, “Overview of Enterprise Risk Management”, online: <http://www.casact.org/research/erm/overview.pdf> at 3 [ERM, “Overview”]. See also Lisa K. Meulbroeck, “Integrated Risk Management for the Firm: A Senior Manager’s Guide” (2002) [unpublished] online: <http://www.hbs.edu/research/facpubs/workingpapers/papers2/0102/02-046.pdf> and Committee of Sponsoring Organizations of the Treadway Commission, “Enterprise Risk Management – Integrated Framework”, online: http://www.coso.org/Publications/ERM/COSO_ERM_ExecutiveSummary.pdf.

²² See eg, the Turnbull Report in the United Kingdom, online: <http://portal.surrey.ac.uk/pls/portal/docs/PAGE/RISK/BACKGROUND/LEGISLATION/TURNBULL/TURNBULL%20REPORT.PDF>, and the Report of the National Commission on Fraudulent Financial Reporting in North America (the “Treadway Commission”), online: <http://www.coso.org>.

²³ ERM, “Overview” at 3.

²⁴ Basel II is legislated through the Office of the Supervisor of Financial Institutions, online: <http://www.infosource.gc.ca/inst/sif/fed04-eng.asp>.

²⁵ ERM, “Overview” at 35.

²⁶ *Ibid* at 8.

²⁷ *Ibid* at 4.

value-creating principle of ERM. Financial risk is the most traditional form of risk analysis. It is typically concerned with a company's share price, its cost of undertaking business ventures, its purchasing power, and its ability to hedge risk. Operational risk is an inter-disciplinary method of risk assessment that is embedded into functions such as human resources, product development, supply chain management, and information reporting.²⁸ It works by harnessing the diverse skills of internal agents in order to identify risks within their functional expertise. Following this risk assessment, senior management then operationalizes internal controls based on the agents' recommendations.²⁹ Finally, strategic risk is primarily concerned with reputation management and competitive pressures.³⁰ The former speaks to the value that offers "premium product prices, lower costs for capital and labour, [and] improved loyalty from employees",³¹ while the latter considers the business' standing vis-à-vis the public and its competitors.³²

In what follows, an ERM analysis of the financial, operational, and strategic risks associated with bad faith discharges will show that the recent *Keays* reformulation has reduced the risk of employee terminations. While this may seem reasonable on its face, a deeper analysis of the *Wallace* regime and the effect its precedents had on motivating employer best practices will show that the Supreme Court took a serious misstep when rendering its decision in *Keays*.

WHAT WAS ONCE OLD... REVIEW OF DAMAGES IN CANADIAN EMPLOYMENT LAW

The law of non-unionized employment in Canada is fundamentally rooted in the law of contract. While scholars dispute the exact influence or control that traditional contract law doctrines have, or should have, over employment law,³³ it is clear that courts have attached special significance to the contract of employment as compared to other commercial contracts.³⁴ This flows from the judicial recognition that non-unionized employees are a vulnerable group in society in light of their dependence on employers to continually purchase their labour power without any mechanism for future job security.³⁵ Consequently, courts have held that traditional contract law doctrines must be re-thought

²⁸ *Ibid* at 10. Michael Power, "The Invention of Operational Risk" (2005) Review of International Political Economy 577 at 584 [Power, "Operational Risk"].

²⁹ Power, *supra* note 28 at 585.

³⁰ ERM, "Overview" at 10.

³¹ Jan Bebbington, Carlos Larrinaga & Jose M. Moneva, "Corporate Social Reporting and Reputation Risk Management" (2007) Corporate Social Reporting 337 at 339 [Bebbington, "Reputation Risk Management"].

³² *Ibid* at 346.

³³ See Don Jack and Jane Southren, "The Problem with Wrongful Dismissal Law" 5 CLELJ 45 at 47 [Jack, "Problem with Wrongful Dismissal"], and John Swan, "Damages for Wrongful Dismissal: Lessons from *Wallace v. United Grain Growers*" 6 CLELJ 313 [Swan, "Lessons from *Wallace*"].

³⁴ See *Slaight Communications Inc v Davidson*, [1989] 1 SCR 1038 at 1051-52.

³⁵ See *Wallace* at paras 72-73.

in order to account for this inherent unfairness in non-unionized employment.³⁶ While this has caused much frustration for commercial litigators,³⁷ scholars have generally applauded courts' progressive thinking.³⁸ However, none of this has changed the fact that an employment relationship can still be terminated for any reason,³⁹ provided adequate notice is given. In this regard, the judiciary's most significant innovation has been the remedy crafted to protect employees from acts of bad faith when they are at their most vulnerable; namely at the time of termination.

i. The Early Years: *Hadley* and *Addis/Peso*'s Strict Limits on Wrongful Dismissal Recovery

Canadian courts did not arrive at this progressive position overnight. At first, contracts of employment were considered no different than any other commercial contract. This meant that wrongful dismissal actions were subject to the cap on foreseeability imposed by *Hadley v Baxendale*,⁴⁰ which limited recovery to only that which was in the contemplation of the parties at the time of contract formation. Under the 19th century *Hadley* regime, the only damages plaintiffs could recover were compensation for pay in lieu of reasonable notice.⁴¹ This was premised on the artificial notion courts imputed that it was always in the contemplation of the parties that the contract may end at any time, provided adequate notice was given.⁴² Consequently, under the *Hadley* regime, the loss of employment and everything associated with it was not *per se* compensable; rather, only damages representing the proper length of notice that ought to have been given could be recovered.⁴³ For many years to come, this doctrine had the effect of significantly restricting the scope of what was recoverable in a wrongful dismissal action.

In *Addis v Gramophone Co.*,⁴⁴ a case nearly a hundred years ahead of its time, the House of Lords considered whether an employee could recover losses in a wrongful dismissal action for harm occasioned by the manner of termination. Relying on the analytical rubric of *Hadley*, the Law Lords rejected the claim. Lord Loreburn noted that the employer could not be liable for "the injured feelings of the servant, or for the loss he

³⁶ Such progressive thinking has led courts to adopt different rules about: employment contract formation, see *Adams v Comark Inc* (1992), 81 Man R (2d) 119 (CA) regarding imputing terms of employment by conduct over time; interpretation, see *Ceccol v Ontario Gymnastic Federation* (2001), 55 OR (3d) 614 (CA) regarding the interpretation of employment contracts commensurate with the protection of employees; and modification, see *Hobbs v TDI Canada Ltd* (2004), 246 DLR (4th) 43 (Ont CA), regarding the insufficiency of continued employment as valid consideration to sustain change to an employment contract.

³⁷ Jack, "Problem with Wrongful Dismissal" at 50-63.

³⁸ Geoffrey England, "Recent Developments in Individual Employment Law: Tell Me the Old, Old Story" 9 CLELJ 44 [England, "Tell Me the Old Story"].

³⁹ Provided the reason does not run afoul of prohibited grounds set out by employment standards, labour relations, or human rights legislation.

⁴⁰ (1854) 9 Ex 341, 156 ER 145, 23 LJ Ex 179.

⁴¹ Jack, "Problem with Wrongful Dismissal" at 48.

⁴² *Ibid.* See also *Morrison v Abernathy School Board* (1876), 3 SC (4th) 945 (HL).

⁴³ Jack, "Problem with Wrongful Dismissal" at 48.

⁴⁴ [1909] AC 488.

may sustain from the fact that his having been dismissed of itself makes it more difficult for him to obtain fresh employment.”⁴⁵ In his concurring reasons, Lord Atkinson noted that a tort claim for malice, fraud, or defamation was the proper domain for such recovery, and that it had no place in an action for breach of contract.⁴⁶ *Addis* remained the law in Canada for some time, and its holding was echoed nearly verbatim by the Supreme Court in 1966’s *Peso Silver Mines Ltd v Cropper*,⁴⁷ when it ruled that “damages [in a wrongful dismissal action] cannot be increased by reason of the circumstances of dismissal whether in respect of the respondent’s wounded feelings or the prejudicial effect upon his reputation and chances of finding other employment [emphasis added].”⁴⁸ *Addis* and *Peso* governed the law of recovery in wrongful dismissal actions until the Supreme Court undertook its modernization of non-unionized employment law, beginning in 1989 with *Vorvis v Insurance Corp of British Columbia*.⁴⁹

ii. A Precursor of Things to Come: *Vorvis* and *Machtiger’s* New Direction

Vorvis concerned the termination of an in-house lawyer, Eonis J. Vorvis, who was described as “conscientious to a fault” and produced “Cadillac[s] when Ford[s] would suffice”.⁵⁰ He was subject to belittling and humiliating workload meetings each week that eventually necessitated medical attention, and later precipitated his termination. Although the Supreme Court rejected his appeal for aggravated and punitive damages, the majority broke new ground by holding that damages for mental distress occasioned by the manner of termination could be awarded in a wrongful dismissal action if the conduct complained of was an independently actionable wrong (e.g. a tort or separate breach of contract). This was a huge step forward from *Addis*, which required discharged plaintiffs to decide whether to frame their action in tort or contract. In dissent, Wilson J. urged the Court to collapse recovery for mental distress into the rubric of *Hadley*, noting that the second branch of the *Hadley* test permitted extended damages if there were special circumstances or particular plaintiff vulnerabilities that the defendant was aware of at the time of contract formation.⁵¹ This, she reasoned, was more appropriate than requiring another independently actionable wrong.

For a case that broke new ground for the rights of terminated employees, it is important to note that the tone of *Vorvis* is remarkably sterile. In particular, the only reference to employee vulnerability was made in passing by Wilson J.’s dissent. Three years later, however, the Supreme Court unveiled its new policy with respect to non-unionized employees in *Machtiger v. HOJ Industries*.⁵² In that case, Iacobucci J. opened the Court’s ruling by acknowledging that “the law governing the termination of employment significantly affects the economic and psychological welfare of employees.” He went on to describe employment as being of “central importance to our society”, “fundamental to an individual’s identity” and that non-unionized employees are “in an unequal

⁴⁵ *Ibid* at 491.

⁴⁶ *Ibid* at 496.

⁴⁷ [1966] 1 SCR 673.

⁴⁸ *Ibid*.

⁴⁹ [1989] 1 SCR 1085.

⁵⁰ *Ibid*.

⁵¹ *Ibid* at 1123.

⁵² [1992] 1 SCR 986.

bargaining position” and their interests must be “protected” by remedially interpreting minimum standards legislation whenever possible.⁵³ As a sign of things to come, Iacobucci J. also noted that “the manner in which employment can be terminated is equally important” to other policy considerations. These values set the stage for *Wallace v. United Grain Growers*, the Supreme Court’s employment law opus that transformed the way termination of employment was thought of, managed, and litigated in Canada.

iii. The Wallace Era: Wrongful Dismissal’s “Market Correction”

If the Supreme Court embarked on a course correction in 1989 with *Vorvis* and made a pit stop in 1992 with *Machtiger*, then it truly arrived in 1997 with *Wallace v. United Grain Growers*.

Jack Wallace was a sales person who was induced away from lengthy and secure employment to join the defendant at the age of 45. Despite being the top sales person in the company and being told he was doing a great job and could work until retirement, Wallace was inexplicably fired without notice at the age of 59. The employer maintained egregious just cause allegations that damaged Wallace’s reputation in the industry until just before trial when they were withdrawn. A lawyer whose academic publications had vigorously argued the need for a judicial remedy to address bad faith terminations represented Wallace at the Supreme Court.⁵⁴ In his own words, Wallace’s lawyer thought “Canada’s existing law reflected the antiquated values of the United Kingdom, and that it was wrong to impose these values on Canadian employees”.⁵⁵ In light of the direction *Vorvis* and *Machtiger* had gone in, he thought the time had finally come for Canadian wrongful dismissal law to receive a significant and comprehensive “market correction”.

Wallace presented three arguments to the Supreme Court: first, that because of its special significance, the contract of employment was a “peace of mind” contract, the breach of which could give rise to aggravated damages; second, that the Court ought to recognize a freestanding tort of bad faith discharge; and third, in the alternative to tort, that the law should impose a contractual term of good faith and fair dealing, the breach of which could give rise to additional damages. The Court rejected all three of Wallace’s proposals.⁵⁶ However, instead of leaving him without recourse, it crafted a truly unique remedy that became known as “*Wallace* damages”. Rather than create a tort or impose a contractual term up front, which could significantly interfere with an employer’s right to manage its workforce, the Court imposed, though the back door, a *sui generis* standard of good faith and fair dealing at the time of termination. This preserved employers’ management rights during the life of the employment relationship, while still giving employees protection from acts of bad faith at the time of termination, which is when they are most vulnerable. Notably, the Court’s remedy did not take the form of lump

⁵³ *Ibid.*

⁵⁴ See eg, Stacey Reginald Ball, “Bad Faith Discharge” (1994) 39 McGill LJ 568 [Ball, “Bad Faith Discharge”].

⁵⁵ Author’s notes of Stacey Reginald Ball’s lecture to ‘Individual Employment Law’ (2550.03) at Osgoode Hall Law School, dated March 16, 2010.

⁵⁶ *Wallace* at para 88.

sum damages, but rather was fashioned in the form of an extension to the reasonable notice period.

Similar to *Machtiger*, the Court's starting premise was that the relationship between an employer and non-unionized employee is not one of equal power; a condition assumed in most other contractual relationships.⁵⁷ This allowed the Court to declare that the contract of employment was distinct from other commercial contracts, thus giving it a special status in Canadian law.⁵⁸ This flowed from the recognition that a power imbalance permeates all aspects of an employment contract, and that "compliance" with its terms is like an act of "submission".⁵⁹ Further, the Court noted that work is one of the most fundamental aspects of a person's life, which provides not only a livelihood, but also a sense of identity and self-worth. As such, the Court concluded that the loss of employment has a profound effect on a person's emotional well being, and if that loss was occasioned by acts of bad faith, then the effect will be even greater.⁶⁰ As a result, *Wallace* damages were fashioned in the form of a lengthened notice period because a victim of bad faith will take longer to obtain alternative work.⁶¹

It is important to note that while taking longer to find alternative work is a tangible result of bad faith, the Court turned its back on *Hadley, Addis/Peso*, and to an extent, *Vorvis*, by deciding that the intangible injuries flowing from termination, in and of themselves, could also be compensable.⁶² Recall that past jurisprudence allowed recovery in a wrongful dismissal action only for the failure to provide reasonable notice, or later on, for an act that was already itself independently actionable. To justify this paradigm shift, the Court analogized from libel law, where the act of defamation allows recovery for intangible injuries to one's state of mind.⁶³ The Court reasoned this was appropriate given the damage to Wallace's professional reputation on account of his employer's egregious (and groundless) accusations. This analogy underlies the Court's other examples of wrongdoing that, occurring in the course of termination, could also be compensable by *Wallace* damages. Examples include: humiliation, embarrassment, and damage to self-worth or self-esteem.⁶⁴

NO EVIDENCE, NO PROBLEM: ANALYZING WALLACE DAMAGES' IMPACT ON EMPLOYER CONDUCT

i. Wrongful Dismissal Policy: Lessons Learned from Defamation Law

It is crucial to note that since defamation law provides the justification for recovering intangible losses, *Wallace* damages, like libel, did not require the plaintiff to lead evidence of intent or harm suffered. Defamation law justifies this on two grounds. The

⁵⁷ *Ibid* at para 90.

⁵⁸ *Ibid* at para 91.

⁵⁹ *Ibid* at para 92.

⁶⁰ *Ibid* at para 94.

⁶¹ *Ibid* at para 95.

⁶² *Ibid* at para 104.

⁶³ *Ibid* at para 105.

⁶⁴ *Ibid* at para 103.

first is that, as a tort, damages in defamation are calculated on a compensatory, rather than expectation, basis; the intention is to put the plaintiff back in the position had the tortious act not occurred. However, due to the difficulty of exhaustively approximating loss from harm to reputation, for policy reasons tort law recognizes the concept of damages-at-large, which is designed to compensate for such intangible injury.⁶⁵ As a result, no evidence is required to establish proof of loss.

Note that in employment-related tort actions, damages-at-large for reputational injury have awarded compensation for past and future income loss.⁶⁶ The logic is that the tortious act may have not only resulted in the loss of a job, but also in the loss of a career.⁶⁷ Further, in defamation cases, the plaintiff is not required to prove that the defendant intended to undertake the tortious action. This is because Canadian and English common law has long held that a finding of recklessness will constitute “constructive malice”, satisfying a tort’s requirement for intent.⁶⁸ In light of the *Keays* reformulation which burdens the plaintiff with having to prove actual loss from the alleged bad faith discharge, it is important to be mindful of the reasons why this was originally not the case.

With respect to why plaintiffs ought not to bear a heavy evidentiary burden, the reasons why the Supreme Court rejected the “actual malice” rule from US defamation law are exemplary. As mentioned, Canadian and English common law does not require the plaintiff to prove loss or intent in a defamation action. In *Hill v Church of Scientology*,⁶⁹ the Church of Scientology urged the Supreme Court to adopt the US’s “actual malice” rule. This rule eliminated the common law’s presumption of falsity and intent, instead requiring the plaintiff to prove that, at the time made, the defendant knew the defamatory

⁶⁵ *McCarey v Associated Newspapers Ltd*, [1965] 2 QB 86 (CA). Consider the following passage from the speech of Lord Pearson:

“Compensatory damages, in a case in which they are at large, may include...not only actual pecuniary loss and anticipated pecuniary loss or any social disadvantages which result, or may be thought likely to result, from the wrong which has been done. They may also include the natural injury to his feelings -- the natural grief and distress which he may have felt at having been spoken of in defamatory terms, and if there has been any kind of **high-handed, oppressive, insulting or contumelious behaviour by the defendant which increases the mental pain and suffering caused by the defamation and may constitute injury to the plaintiff’s pride and self-confidence, those are proper elements to be taken into account in a case where the damages are at large.**” [Emphasis added]

⁶⁶ See eg, *Drouillard v Cogeco Cable Inc*, 2007 ONCA 322, 86 OR (3d) 431.

⁶⁷ *Ibid* at para 42.

⁶⁸ *Fedele v Windsor Teachers Credit Union Ltd*, 2001 CLLC 210-001 (Ont SCJ), aff’d 10 CCEL (3d) 254 (Ont CA). See also *Cogeco*, *supra* note 68 paras 39-40, where the rule was applied in the context of the tort of interference with contractual relations. Note that the application to employment may have limits on the grounds of policy considerations: see *Piresferreira v Ayotte*, 2010 ONCA 384, 263 OAC 347 [“*Piresferreira*”] for a discussion of the tort of negligent infliction of mental suffering.

⁶⁹ [1995] 2 SCR 1130 [“*Hill v Church of Scientology*”].

statements were false, or acted recklessly in not doing so.⁷⁰ As such, the “actual malice” rule resembles the *Keays* formulation of bad faith damages in a number of ways. Most significantly, both encumber plaintiffs with an evidentiary burden; with “actual malice” it is to prove falsity, and with *Keays* it is to prove harm.

In *Hill*, the Supreme Court rejected “actual malice” based on the US’s troubled experience with the doctrine. For one, the emphasis on proving falsity in defamation was said to result in overly detailed inquiries into matters of media procedure.⁷¹ This, in turn, significantly increased the length of the trial and discoveries, which often obfuscated the claim’s purpose and had the effect of coercing settlement.⁷² Consequently, the burden of proving “actual malice” was said to actually increase, rather than decrease, the threat to freedom of expression.⁷³ Similarly, the elongated inquiry was said to dramatically increase the cost of litigation, leaving many resource-strapped plaintiffs without access to justice.⁷⁴ Finally, and perhaps most importantly, in light of these obstacles, many thought that the purpose of the “actual malice” rule had become perverted by effectively protecting the dissemination of falsehoods, rather than thwarting them.⁷⁵ Scholars argue the totality of this has exacted a major cost on American society.⁷⁶ In concluding that the “actual malice” rule was not appropriate for Canadian jurisprudence, the Court noted:⁷⁷

[The law of defamation] is the means by which the individual may protect his or her reputation which may well be the most distinguishing feature of his or her character, personality and, perhaps, identity. **I simply cannot see that the [current] law of defamation is unduly restrictive or inhibiting.** Surely it is not requiring too much of individuals that they ascertain the truth of the allegations they publish. ... Those who publish statements should assume a reasonable level of responsibility. [Emphasis added]

With respect to the current defamation law’s presumption of falsity, the Court’s comment about it not being a burden on publishers in light of the significance of one’s reputation is telling. Consider the following statement from *Wallace* regarding the effect a presumption of injury might have on employers:⁷⁸

The law should be mindful of the acute vulnerability of terminated employees and ensure their protection by encouraging proper conduct and preventing all injurious losses which might flow from acts of bad faith or unfair dealing on dismissal, both tangible and intangible. I

⁷⁰ *Ibid* at para 122.

⁷¹ *Hill v Church of Scientology* at para 129.

⁷² *Ibid* at para 130.

⁷³ *Ibid* at para 129.

⁷⁴ *Ibid* at para 130.

⁷⁵ *Ibid* at para 128.

⁷⁶ *Ibid* at para 131.

⁷⁷ *Ibid* at para 137.

⁷⁸ *Wallace* at para 107.

note that there may be those who would say that this approach imposes an onerous obligation on employers. I would respond simply by saying that I fail to see how it can be onerous to treat people fairly, reasonably, and decently at a time of trauma and despair. In my view, the reasonable person would expect such treatment. So should the law. [Emphasis added]

In both situations, the Supreme Court held that the interests of the individual, in terms of equity and access to justice, were best served by burdening the more powerful entity (employers and publishers) with presumptions and duties that would otherwise be unfair, but-for the unequal relationship and resource disparity. In other words, the Court recognized that defamation litigants might not be able to recover damages to their reputation if they were saddled with onerous evidentiary requirements; as a result, publishers are burdened with risks caused by the law's presumption of falsity for defamatory statements they publish. The assumption is that, in response, publishers will undertake more diligent publishing practices. Similarly in *Wallace*, the Court realized terminations conducted in bad faith could cause far more injury to employees than pay in lieu of notice encompasses; consequently, the law imposes risks of employers having to compensate for invisible injuries caused by their termination process. Again, the assumption is that employers will address this risk with more dignified and polished termination procedures.

ii. **The ERM-Reflexive Regulation Analysis: Connecting *Wallace's* Uncertainty to Termination Best Practices**

So what happened in *Wallace* and *Hill*? Simply put, the Supreme Court exercised an ingenious form of reflexive regulation. In both cases, the law imposed a significant measure of uncertainty; in terms of the risk of defending litigation that assumes published statements are false and damaging, and the risk of defending litigation that assumes injury was caused by an egregious termination.

From an ERM perspective, there are tremendous risks associated with such level of uncertainty. First, there are obvious financial risks in terms of having to pay additional damages. Further, because company auditors assess risks posed by ongoing litigation and their conclusions are a matter of public record, lawsuits for dismissals made in bad faith could theoretically affect a company's share price as well. A corporate reputation tarnished by allegations of bad faith also poses many problems in terms of strategic risk. Not only are court documents containing the allegations available to the public, but when the plaintiff was a former colleague, employment litigation has a tendency to polarize the workforce as well. Depending on the nature of the *Wallace* claim, the damage to a

company's reputation may also impair its ability to compete for top talent.⁷⁹ Finally, in certain competitive industries, this damage can reverberate further and potentially erode price premiums that had previously been maintained by consumer loyalty.⁸⁰

In light of the foregoing, while operational procedures are the greatest source of *Wallace* liability, revising them also presents the greatest opportunity for risk mitigation and value creation; this is where the practice of operational risk comes in. For example, human resources personnel and lawyers are frequently the “lightning rod” for employment disputes. As part of a risk assessment that draws on their workplace expertise, these agents are uniquely positioned to enhance their roles in the eyes of senior management by identifying termination-related risks in company policies and procedures, which could be susceptible to *Wallace* damages' ubiquitous uncertainty. In response, management will operationalize new measures aimed at mitigating those risks.⁸¹ While it is outside the scope of this paper to attempt a thorough human resources analysis of the organizational value that can be derived from this, it would certainly be an area ripe for further research. That said, the net result of tying the risk of uncertainty posed by *Wallace* damages' presumption of injury to the self-correcting theory of reflexive regulation and ERM is that workplaces will function better as employers strive to isolate and eliminate possible liability for bad faith discharges.

iii. Arbitrary by Prolific: Precedents Set by *Wallace* Damages

In light of *Wallace* damages' notorious uncertainty, ERM practitioners relied on case law to identify what conduct, practices, or procedures left employers vulnerable to allegations of bad faith. In the years following *Wallace*, one lawyer noted that “the novel ways some employers exhibit their insensitivity to their dismissed workers, combined with an imaginative and diligent plaintiff's bar, provide[s] endless fact scenarios.”⁸² In the ten years following this statement, plaintiffs' lawyers have lived up to that expectation. Without attempting to be exhaustive, courts have awarded *Wallace* damages for the following employer conduct:

- Making serious but unsubstantiated allegations of just cause;⁸³
- Making express or implicitly derogatory remarks about the plaintiff to his or her former colleagues after dismissal;⁸⁴

⁷⁹ See Kelly Pullen, “The Problem With Women” *Toronto Life* (10 May 2010), online: <http://www.torontolife.com/daily/informer/from-print-edition-informer/2010/05/10/the-problem-with-women/>, which discusses Diane LaCalamita's lawsuit against McCarthy Tetrault LLP for systemic gender discrimination. Similarly, see Michelle Henry, “Woman alleges sexual discrimination in lawsuit against Toronto-based firm” *Toronto Star* (15 Feb 2011), regarding Jaime Laskis' lawsuit against Osler Hoskin & Harcourt LLP for sex discrimination. Anecdotally, the author has found that law students quickly become aware of these stories, especially during recruitment seasons.

⁸⁰ Bebbington, “Reputation Risk Management” at 339.

⁸¹ Power, “Operational Risk” at 585.

⁸² Joe Conforti, “Bad Faith Discharge and the *Wallace* Factor” (Paper presented to the Law Society of Upper Canada's Second Annual Six Minute Employment Lawyer Conference, 29 April 1999) [unpublished].

⁸³ *Rady v Canadian Medical Laboratories Ltd.*, [1999] OJ No 5858 (QL) (SCJ).

- Threatening to rescind a severance package and allege just cause if the employer's offer was not accepted;⁸⁵
- Terminating a dissenting employee that refused to accept changes to the terms of employment in order to secure agreement from other employees;⁸⁶
- Refusing to provide a letter of reference;⁸⁷
- Failing to allow an employee to respond to allegations of wrongdoing prior to termination;⁸⁸
- Withholding statutory severance/termination pay in order to coerce settlement;⁸⁹
- Firing without first investigating the surrounding circumstances;⁹⁰
- Failing to inform a sick employee who resigned because of illness about the availability of disability benefits;⁹¹
- Preventing an employee from qualifying for disability benefits by making unsubstantiated allegations of malingering to the insurance company;⁹²
- Firing employees returning to work from disability leave;⁹³
- Failing to cooperate in a timely manner with the discovery process;⁹⁴
- Engaging in abusive treatment that culminated in constructive dismissal (regardless of intent to humiliate or embarrass);⁹⁵
- Firing a "whistle blowing" employee;⁹⁶ and
- Conducting a termination by telephone message.⁹⁷

Although courts also frequently declined to award *Wallace* damages, the remedy quickly gained a reputation for being notoriously arbitrary. In light of this, a cottage industry dedicated to educating employers about termination practices and how to minimize

⁸⁴ *Cassady v Wyeth-Ayerst Canada Ltd* (1997), 163 DLR (4th) 1 (BCCA).

⁸⁵ *Squires v Corner Brook Pulp & Paper Ltd* (1999), 175 Nfld & PEIR 202 (Nfld CA).

⁸⁶ *Slepenkova v Ivanov* (2008), 60 CCEL (3d) 303 (Ont SCJ).

⁸⁷ *Barakett v Levesque Beaubien Geoffrion Inc*, 2001 NSCA 157, 198 NSR (2d) 135.

⁸⁸ *Hampton v Thirty-Five Charlotte Ltd* (1999), 218 NBR (2d) 109 (QB).

⁸⁹ *Stolle v Daishinpan (Canada) Inc* (1998), 37 CCEL (2d) 18 (BCSC).

⁹⁰ *Rady v Canadian Medical Laboratories Ltd*, *supra* note 86.

⁹¹ *Mernard v Royal Insurance Co of Canada* (2000), 1 CCEL (3d) 305 (NBQB).

⁹² *Youkhanna v Spina's Steel Workers Co* (2001), 15 CCEL (3d) 99 (Ont SCJ).

⁹³ *Skopitz v Intercorp Excellence Foods Inc* (1999), 43 CCEL (2d) 253 (Ont Ct (Gen Div)).

⁹⁴ *Antidormi v Blue Pumpkin Software Inc* (2004), 35 CCEL (3d) 247 (Ont SCJ).

⁹⁵ *Saunders v Chateau des Charmes Wines Ltd* (2002), 20 CCEL (3d) 220 (Ont SCJ).

⁹⁶ *Mark v Westend Development Corp* (2002), 18 CCEL (3d) 90 (Ont SCJ).

⁹⁷ *Carter v Packall Packaging Inc* (2004), 128 ACWS (3d) 516 (Ont SCJ).

liability quickly developed.⁹⁸ This created a healthy eco-system of normative employment standards in the following way: The ubiquity of *Wallace* “bumps” enticed plaintiffs’ lawyers to risk carrying a wrongful dismissal action on contingency, resulting in more theories of bad faith being tested by courts, which led to more reported decisions on examples of bad faith that were fed back into the employment bar for dissemination to employers, who incorporated them into revised operational procedures. The net result was an “upwardly ratcheting” system of normative employment standards for non-unionized employees, functioning entirely under the purview of reflexive regulation.

As the saying goes, however, “all good things must come to an end”. While management-side employment lawyers loudly bemoaned advising on, and litigating against, *Wallace* damage claims,⁹⁹ the judiciary soon began to sympathize with their cause. Notably, the Honourable Justice Randall Scott Echlin of the Ontario Superior Court of Justice, a prominent employment law jurist and former management-side employment lawyer,¹⁰⁰ lashed out at the plaintiff bar’s propensity to test novel theories of bad faith in *Yanez v Canac Kitchens*.¹⁰¹ Echlin J. described the plaintiff’s lawyer as “throw[ing] in the kitchen sink” in terms of ancillary claims, which resulted in “more than half of the total trial time [being] dedicated to the plaintiff’s claim for ‘*Wallace* damages’”. The conduct in question concerned the employer’s failure to offer the statutory minimum level of notice for an employee with 16 years of service, and its insistence that he sign a Release, characterizing the offer as “more than fair”. The employer led evidence that this was a mere mistake that was quickly rectified, but the plaintiff nonetheless pursued his claim for *Wallace* damages. Echlin J. allowed the claim for wrongful dismissal, flatly denied a *Wallace* “bump”, and then fired a shot across the bow of plaintiff lawyers everywhere across Canada by suggesting unmeritorious *Wallace* claims might warrant sanctions involving reduced cost or damage awards.¹⁰²

⁹⁸ In previous years, advising on how to avoid *Wallace* liability was a large function of the employment bar’s continuing legal education. See eg, Canadian Institute’s 6th Annual Advanced Forum on Employment Law (2006), online: http://www.lerners.ca/content/documents/employment_law.pdf; McCarthy Tetrault LLP, “The Break-Up: Termination of Employment” (2006), online: http://www.advisor.ca/images/other/t/Termination_McCarthy.pdf; Law Society of Upper Canada’s 8th Annual Six-Minute Employment Lawyer (2005), online: <http://ecom.lsuc.on.ca/pdf/flyers/2005/sixminuteemployment.pdf>.

⁹⁹ See eg, Jack, “Problem with Wrongful Dismissal”.

¹⁰⁰ “Honourable Randall Scott Echlin”, Canada Law Book Biography, online:

<http://www.canadalawbook.ca/honourable-justice-randall-scott-echlin.html>.

¹⁰¹ (2004), 45 CCEL (3d) 7 (Ont SCJ).

¹⁰² *Ibid* at paras 34-43. Consider the reprimand given by Echlin J.:

“Wallace damages” ought not to be asserted in every case. Only in the appropriate case. This lawsuit involved an employer who, while being less than generous, did attempt to do it right...when it was notified that it had made a mistake, rather than to stonewall, it immediately remedied the situation...

... The time has now come to express this Court’s disapproval of routine assertions of “Wallace damage” claims which are not justified by the facts.

Echlin J.'s concerns about *Wallace* claims not grounded in fact are reasonable; indeed, in *Wallace* Iacobucci J. noted the remedy was not "anything akin to an automatic claim for damages...in every case of dismissal."¹⁰³ However, Echlin J.'s contention that such claims have no value and waste court time is not accurate; in addition to knowing what makes them liable, employers also need to know what conduct will not attract *Wallace* liability. For example, the Ontario Court of Appeal's decision that rejected *Wallace* damages for firing an employee on sick leave provided important clarification on how to conduct risky terminations with dignity and respect.¹⁰⁴

Despite the benefits of *Wallace* that this paper has advocated, it is no longer the law in Canada. The new law that governs terminations conducted in bad faith is *Honda v Keays*. As will be explained, the focus is no longer on what the employer has (or has not) done, but rather on the proof of injury the plaintiff must produce. This paper's position is that *Keays*' approach removes the disciplining effect on employer conduct that *Wallace* had, and in effect, destroys the eco-system of precedent and education that reflexively created the normative system of ever-improving employment standards that Canadian workplaces used to enjoy.

...IS NOW NEW AGAIN: THE SUPREME COURT'S DECISION IN *HONDA V KEAYS*

i. Extreme Facts Lead to Extreme Law

Similar to *Wallace*, extreme facts lead to extreme law, and *Honda v Keays* had no shortage of either. Kevin Keays was a dedicated, "conscientious", but disabled, employee of Honda Canada who was terminated for just cause after fourteen years of service. Eleven years after he began working, Keays was diagnosed with chronic fatigue syndrome and went on disability leave. He returned to work a year later after his insurer determined he was fit to do so and was placed in Honda's disability management program. Even with light data entry work, Keays' absences continued. While the program permitted this to some extent, Honda became concerned once the medical notes

... Such claims seriously impede the potential consensual resolution of disputes which could otherwise be settled well short of trial. Additionally, the assertion and defence of specious "Wallace claims" can consume large amounts of valuable court time; can increase the costs to all concerned; and can generally drive the parties apart.

[T]hought must be given in future cases to appropriate deterrents against plaintiffs who assert "Wallace claims" which are clearly without merit and should not have been advanced. Sanctions could include a diminution of either the costs award or the amount awarded for such dismissal claims.

I make no reduction in the amount awarded to this plaintiff in this instance, nor do I reduce the amount granted for costs. However, in future cases, clearly unmeritorious claims for "Wallace damages", having little or no foundation on the evidence, may well face sanctions. [Emphasis added]

¹⁰³ *Wallace* at para. 101.

¹⁰⁴ See *Mulvihill v Ottawa (City)*, 2008 ONCA 201, 235 OAC 113.

he was required to obtain stopped being evaluative and instead became vague and self-reporting. The requirement to obtain notes for each absence led to a showdown, with Honda asking Keays to submit to an examination by their in-house doctor and Keays refusing to do so until he knew the exact purpose of the meeting. Exacerbating this was Honda's cancellation of Keays' limited accommodation, allegedly as reprisal for Keays' decision to retain counsel. Honda sent Keays a letter stating that if he did not meet with their doctor, he would be fired. As no explanation was provided, Keays refused and was fired for just cause. He then sued for wrongful dismissal.

The trial judge found that Honda's conduct was egregious, reprehensible, and evidenced a "conspiracy" against Keays, who was awarded fifteen months notice, an additional nine months of *Wallace* damages, a costs premium fixed at \$610,000, and a punitive damages award of \$500,000, the largest in Canadian employment law history. Honda appealed, and at the Court of Appeal for Ontario was successful only in reducing the punitive damages award and costs premium. The majority found the award "generous, but fair", with Goudge J.A. noting in dissent that the entire punitive damages award ought to have remained intact in light of Honda's misconduct. Honda appealed again, this time to the Supreme Court of Canada.

Writing for the majority, Bastarache J. did not offer the expected guidance on how employers should lawfully terminate disabled employees. Nor did he elaborate on how employers should accommodate employees with invisible disabilities, such as chronic fatigue syndrome, chronic pain, and fibromyalgia. Rather, he side-stepped these issues completely and took the opportunity instead to reformulate how damages for bad faith were to be awarded in wrongful dismissal actions. In doing so, the Court divested itself entirely from *Wallace* and arguably reunified the contract of employment with its commercial brethren under the principles of *Hadley v Baxendale*.

ii. **Back to *Baxendale* For The Damages Formerly Known as *Wallace***

In *Keays*, the Court spent a great amount of time retracing damages in wrongful dismissal law before attempting to shoe-horn them all in under the auspice of *Hadley v Baxendale*, a case that had nothing to do with employment law.

Rather than overturn *Wallace*, *Vorvis*, and other case law that espoused the Supreme Court's modern policy on non-unionized employment, Bastarache J. attempted to pay homage to their principles by acknowledging that termination will always cause employees to suffer some degree of emotional harm, and that an employer's acts of bad faith at this time can exacerbate this harm. In doing so, Bastarache J. invoked *Hadley*'s stipulation that only that which was in the reasonable contemplation of the parties at the time of contract formation could be compensable. Bastarache J. reasoned that when the employment contract is formed, both the employer and employee would have contemplated the debilitating impact of bad faith conduct at termination. Thus, in the event an employer's behaviour was particularly egregious and the employee can prove that it caused more harm than what was contemplated to be "normal", then Bastarache J. held this difference could be compensable. In other words, the Supreme Court took the values espoused by *Wallace*, made them foreseeable under the *Hadley* test, but as a purely compensatory remedy, now requires strict proof of actual losses. In practice, this

has the effect of barring recover for many of the intangible injuries *Wallace* stood to protect against, such as embarrassment, humiliation, and loss of reputation. As stated by Bastarache J.:¹⁰⁵

“Damages attributable to conduct in the manner of dismissal are always to be awarded under the *Hadley* principle. Moreover, in cases where damages are awarded, no extension of the notice period is to be used to determine the proper amount to be paid. The amount is to be fixed according to the same principles and in the same way as in all other cases dealing with moral damages. Thus, **if the employee can prove that the manner of dismissal caused mental distress that was in the contemplation of the parties, those damages will be awarded not through an arbitrary extension of the notice period, but through an award that reflects the actual damages.**” [emphasis added]

As a result of this, and in particular because Keays had not led evidence at trial of the termination’s impact on him, Kevin Keays’ nine-month *Wallace* extension was extinguished, as was his punitive damages award and cost premium, leaving him with only his original fifteen-month notice period and Honda’s bill of legal fees. In dissent, LeBel and Fish JJ. expressed concern that the Court was turning its back on the progressive position it had taken with respect to non-unionized employees.¹⁰⁶

“[A]ny revision [of wrongful dismissal damages] must reflect the view accepted by this Court that the contract of employment is a good faith contract that is informed by the values protected by and recognized in the human rights codes and the Canadian Charter of Rights and Freedoms, particularly in respect of discrimination. **As the Court found in *Wallace v. United Grain Growers Ltd.*, the contract of employment often reflects substantial power imbalances. As a result, it must be performed and terminated in good faith, and fairly.**

...

With respect, I believe that on the facts of this case, **the award of additional damages for manner of dismissal (formerly “Wallace damages”) should stand.** The trial judge committed no overriding errors in this respect. Although his review of the facts may not have been flawless, **there was a sufficient basis for the findings of bad faith and discrimination** in the manner in which the employment of the respondent, Kevin Keays, was terminated by Honda. [Emphasis added]

¹⁰⁵ *Wallace* at para 59.

¹⁰⁶ *Ibid* at paras 81-82.

These statements suggest that plaintiffs need not to be held to such strict proof of actual injury, and that a trial judge's imputed findings of fact may instead suffice. For the reasons that follow, this ought to be the preferred interpretation of *Keays* going forward.

ANALYZING KEAYS/HADLEY'S IMPACT ON EMPLOYER CONDUCT

i. No Evidence, No Recovery: Bad Faith Damages Post-Keays

In the wake of *Keays*, practitioners and scholars debated the actual impact the case would have.¹⁰⁷ Some speculated that *Keays* was merely a superficial restatement of existing law that simply changed the form the damage award took in terms of extended notice vis-à-vis monetary lump sum.¹⁰⁸ For example, shortly after *Keays* was released, a dismissed employee in *Simmons v. Webb*¹⁰⁹ was awarded \$20,000 in "moral damages" on account of his employer's bad faith, despite the fact that the plaintiff led no evidence with respect to actual damages caused by the employer's conduct at termination.

Notwithstanding initial confusion, in the two years since *Keays* was released, appellate courts across Canada have begun to strictly enforce plaintiffs' evidentiary burden with respect to proving loss caused by the manner of dismissal.¹¹⁰ For example, in *Brien v Niagara Motors*,¹¹¹ the Ontario Court of Appeal overturned a bad faith damage award on account of conduct that had typically been a "lock" under *Wallace*: recklessly advancing unfounded just cause allegations. In particular, the employer asserted it had just cause to terminate an employee with 23 years of service for, among other things, refusing to work weekends. The trial judge found that the employer was simply trying to avoid paying out a lengthy notice period. The Court of Appeal did not disagree, even noting that the employer's misconduct could have sustained a damage award under *Keays*, however:¹¹²

"...the mental distress that the respondent suffered upon her termination and the manner of that termination was not of the nature and scope to qualify for compensatory damages in accordance with that decision, **as the respondent did not seek any medical attention, professional assistance or undergo any therapy for her mental distress.**"

[Emphasis added]

¹⁰⁷ See eg, Geoffrey England, "Evaluating the Implications of *Honda Canada v. Keays*" 14 CLEJ 330; Daniel A. Lublin, "Wrongful Dismissal – Bad Faith Damages in Canadian Employment Law: *Honda Canada Inc. v. Keays*" (2009) 59 UNBLJ 153.

¹⁰⁸ Michael P. Fitzgibbon, "Different Doesn't Necessarily Mean Different: A Discussion of *Honda Canada Inc. v. Keays*" (2009) 59 UNBLJ 166.

¹⁰⁹ (2008), 84 CCEL (3d) 196 (Ont SCJ).

¹¹⁰ See eg, Jeffrey Goodman and Christopher Pigott, "Bad Faith Damages post-Honda" (Paper presented to the Law Society of Upper Canada's 2010 Six Minute Employment Lawyer Conference, 15 June 2010) [unpublished].

¹¹¹ 2009 ONCA 887, 78 CCEL (3d) 10.

¹¹² *Ibid* at para 3.

With respect, the employee had to endure the cost and stress of taking her employer all the way to trial in order to realize her lawful entitlement of 24 months notice. While *Wallace*'s uncertainty and presumption of injury may have facilitated settlement from the onset, *Keays*' requirement that a plaintiff establish proof of intangible losses allows an employer to be far, far more bullish, as shown in *Brien*, when litigating wrongful dismissal claims.¹¹³

A case from Saskatchewan, *Fox v Silver Sage Housing Corporation*,¹¹⁴ similarly illustrates the troubling turn wrongful dismissal law has taken. In *Fox*, the trial judge made findings of fact against the employer on account of the following: that Fox was terminated based on management's intense personal dislike for him, that Fox was lied to at the time of termination, that the employer orchestrated a "phony" corporate reorganization simply to "get rid" of Fox, and that the employer engaged in "vindictive and thoroughly unprofessional" behaviour by contacting the employer of Fox's wife after his termination. While the foregoing were previously clear indicia of bad faith, the court held that Fox "[had] not proven that the stress and depression he suffered is related to the manner in which he was treated." As such, Fox received no damages for his mistreatment.

If it is not enough, as in *Fox*, for a court to clearly accept that the employer acted egregiously and that the employee suffered stress and depression as a result, what deterrents are there to make sure that employers treat discharged employees with dignity and respect? While there is a reported case where the plaintiff called an expert witnesses to testify as to the impact the manner of termination had on her psyche,¹¹⁵ it is submitted that by having to proceed all the way to trial to do so, *Keays* is not doing terminated employees—previously recognized as a vulnerable group in society—any favours whatsoever.

ii. The Danger of Subsuming Tort into Contract: *Piresferreira* and *Soost*

While *Keays* has made it more difficult for employees to recover for intangible injuries, more dangerous is the very recent pronouncement that all claims related to the manner of termination, including freestanding causes of action in tort, must be subsumed into the *Keays/Hadley* framework. Because damages in tort are calculated differently than in contract—based on making the plaintiff "whole" versus performance of the contract—this has the potential to reduce damage awards for tortious conduct by an order of magnitude.

The Ontario Court of Appeal's decision in *Piresferreira v Ayotte* stands for this troubling precedent. In *Piresferreira*, the plaintiff's claims arose from an altercation with her supervisor, which the court accepted was assault. The supervisor was subject to minor discipline, and as reprisal, tried to place the plaintiff on a performance improvement

¹¹³ See also *Slepenkova v Ivanov*, 2009 ONCA 526 at para 6, 74 CCEL (3d) 163, where the Ontario Court of Appeal overturned another bad faith award on account that the plaintiff had not led any evidence of "harm, mental distress or actual damage."

¹¹⁴ 2008 SKQB 321, 70 CCEL (3d) 99.

¹¹⁵ *Bru v AGM Enterprises Ltd*, 2008 BCSC 1680, 173 ACWS (3d) 495.

plan. After being presented with the plan, the plaintiff went on sick leave and then long-term disability, which represented the end of her active employment with Bell. She then sued her supervisor for a variety of torts and, with respect to Bell, constructive dismissal. The trial judge found the supervisor personally liable for battery and intentional and negligent infliction of mental suffering, while Bell was held vicariously liable for the supervisor's torts and directly liable for negligent infliction of mental suffering and constructive dismissal. Due to tort's measure of damages that allowed for past and future income loss, the plaintiff received over \$500,000 in compensation.

The Ontario Court of Appeal reversed the trial judge's decision almost entirely. In particular, it held that the tort of negligent infliction of mental suffering was not available in workplace disputes because the *Keays/Hadley* framework was intended to deal comprehensively with all mental distress claims arising from employer conduct coinciding with termination of employment.¹¹⁶

In a case in which the employer's allegedly tortious behaviour includes the termination of the employee, compensation for mental distress is available under the framework the Supreme Court has set out in *Honda*. In a case in which the employer does not terminate the employee, the employee who is caused mental distress by the employer's abusive conduct can claim constructive dismissal and still have recourse to damages under the *Honda* framework. Recognizing the tort in the employment relationship would overtake and supplant that framework and all of the employment law jurisprudence from which it evolved. In other words, in the dismissal context, the law already provides a remedy in respect of the loss complained of here. [emphasis added]

Notwithstanding the fact that the plaintiff had been diagnosed with depression, anxiety, and post-traumatic stress disorder, all caused by the supervisor's assault, the Court of Appeal rolled all her losses into the *Keays/Hadley* framework, which produced a mental distress award of merely \$45,000.

Piresferreira's holding that tortious actions coinciding with the end of employment must be subsumed into a *Hadley/Keays* claim sets a dangerous precedent that withholds the tort measure of relief from those who need it the most. That is, it makes no sense to permit actions in tort, or a tort scale of recovery, at other times during the relationship but not at the end, when an employee is—or at least previously was thought to be—most vulnerable. Further, subsuming tort into the *Keays/Hadley* framework also conflates different heads of damages' differing analytic purposes. First, *Hadley*, which underlies *Keays*, is, and always has been, a limit on damages; it is not a ground for awarding them.¹¹⁷ Further, remedies in contract are compensatory to the extent that they reflect performance of the contract but-for the breach, which is why wrongful dismissal compensates with reasonable notice. If an injury prevents a plaintiff from ever

¹¹⁶ *Piresferreira* at para 61.

¹¹⁷ *Merrill Lynch Canada Inc v Soost*, 2010 ABCA 251 at para 40, 487 AR 389 ["Soost"].

performing another contract, then tort is, and always has been, the appropriate realm for recovery, even in employment law.¹¹⁸ Surely a mental distress award representing the loss of Piresferreira's working life ought to be worth more than \$45,000?¹¹⁹

With respect to denying the tort of intentional infliction of mental suffering, the Court of Appeal also divested itself from a long line of cases, if not a common law principle, that, as discussed, intent can be imputed from a finding of recklessness. Indeed, McLachlin J. (as she was then) espoused this principle in *Rahemtulla v. Vanfred Credit Union*¹²⁰ when she allowed recklessness in lieu of intent to sustain the tort of intentional infliction of mental suffering in a workplace dispute involving allegations of theft.¹²¹ Rather than address this principle head on in *Piresferreira*, the Court of Appeal simply distinguished *Rahemtulla* and suggested that workplace disputes require a higher level of "recklessness" to order to ever sustain an intentional tort. The reasons for this, as one might suspect, flow from *Keays*:¹²²

"Recklessness" is a flexible term capable of different meanings in different contexts. ... The test stated in *Prinzo* and reaffirmed in *Correia* maintains the distinction between intentional torts and negligence. As noted Weiler J.A. said in *Prinzo* that the "consequences must be known by the actor to be substantially certain to follow" (emphasis added [in original]).

...

I have already rejected the recognition of the tort of negligent infliction of mental suffering in an employment relationship. **Accepting an objective sense of "recklessness" dependent on whether the harm ultimately suffered was foreseeable or likely to result should be**

¹¹⁸ See eg, *Sulz v Attorney General et al*, 2006 BCSC 99, 263 DLR (4th) 58 involving recovery of \$950,000 for intentional infliction of mental suffering.

¹¹⁹ The award of \$87,855 for pay in lieu of notice is excluded as it serves a different analytic purpose.

¹²⁰ (1984), 51 BCLR 200 (SC).

¹²¹ *Ibid* at paras 54-55. Consider the following reasoning by McLachlin J.:

Allegations of theft should not be made recklessly, without proper care for whether they are true or not.

...

A further requirement of the tort of willful infliction of mental distress is that the defendant's conduct be "plainly calculated to produce some effect of the kind which was produced". In the case at Bar this element is established. **It was clearly foreseeable that the accusations of theft which the defendant made against the plaintiff would cause her profound distress. That distress could only be exacerbated by the defendant's failure to conduct a proper investigation or allow the plaintiff to defend herself. It was equally foreseeable that the accusations would continue to cause distress into the future, when, in seeking employment, she would be queried by prospective employers as to the reasons for her dismissal from the defendant's employ.** [Emphasis added]

¹²² *Piresferreira* at para 76.

rejected for the same reasons. Essentially, permitting liability on such a reduced standard would unduly interfere with the settled principles of employment law. [Emphasis added]

It is submitted that “settled principles of employment law” is more accurately read as, “new era of employment law under *Keays*”. In this way, the Court of Appeal’s apparent hesitation to permit tort recovery to overlap or, more likely in their minds supplant, the *Keays/Hadley* framework is a very troubling proposition. As discussed, these torts exist for a reason, and it is artificial and prejudicial to deny employees, but perhaps not other individuals, access to tort’s measure of relief simply on account of the presence of an employment relationship. Such a policy invokes memories of past injustices rendered under the doctrine of common employment.¹²³

Similar to *Piresferreira*, the Alberta Court of Appeal recently held that pure economic loss—a tortious head of damage—caused by an alleged bad faith dismissal was not compensable under the *Keays/Hadley* framework.¹²⁴ The plaintiff was an investment banker who was terminated without notice for a variety of reasons. While the trial judge agreed with many of these reasons, he held that none were sufficient to sustain a finding of just cause. Although the plaintiff found new employment within three weeks, many of his former clients did not follow him. In light of this and the damage caused to the plaintiff’s reputation, the trial judge awarded \$1.6 million in *Keays* damages for the economic loss resulting from the lost clients. The Alberta Court of Appeal quashed the award, noting that the allegations of cause, notwithstanding actual harm suffered, did not constitute bad faith:¹²⁵

What if courts imposed heavy and almost automatic penalties on any defendant who alleged cause in good faith, but then failed to convince a judge or jury that it was bad enough? That would be most unfair to employers. It would deter alleging cause, so that employers with cause would instead have to give pay in lieu of notice (to avoid a second set of damages). This would be the slacker’s charter. It would significantly increase the expenses of hiring staff, and hence increase prices charged to innocent customers. I wish to stress that policy consideration. [Emphasis added]

With respect to the Alberta Court of Appeal, just cause is the “capital punishment of employment law”,¹²⁶ it is a high standard, and as such, there ought to be risks associated with invoking it. Further, the court is obfuscating the issue; in this case, just cause was likely pursued because, in light of the plaintiff’s extremely high salary, it was cheaper to

¹²³ See eg, *Priestly v Fowler* (1837), 1 M&W 1 (Ex Ch) and Michael A. Stein, “*Priestly v. Fowler* and the Emerging Tort of Negligence” 44 BC L Rev 689, concerning the prejudicial policy considerations underlying the now-defunct doctrine of common employment, which precluded recovery in tort for workplace injuries precisely because of the presence of an employment relationship.

¹²⁴ *Soost*, *supra* note 120.

¹²⁵ *Ibid* at para 24.

¹²⁶ *Peter Tong v Home Depot of Canada Inc* (2004), 39 CCEL (3d) 59 (Ont SCJ) at para 1.

litigate than to settle. Previously such exploitation of the employee's position at termination would have engendered a finding of bad faith,¹²⁷ but under *Keays* it was not made out. Note, however, that even if it had been, the Alberta Court of Appeal was clear that economic loss flowing from dismissal is not compensable under the *Keays/Hadley* framework.¹²⁸

Based on the foregoing, it should be clear that, as a result of *Keays*, courts are now more hesitant than ever to allow full-fledged tort claims to coincide with actions for wrongful dismissal. If aggrieved plaintiffs must now pick and chose a mutually exclusive cause of action, then isn't it fair to say that Canadian employment law has simply come full circle and is now back to where it started over a hundred years ago under *Addis/Peso*'s strict limits on wrongful dismissal recovery?

iii. **The Reflexive Regulation-Erm Analysis: Reduced Termination Risks Bolster Operational Flexibility, But at What Cost?**

From an ERM perspective, the limits placed on recovery under the *Keays/Hadley* framework have significantly reduced the risks associated with termination. Whereas *Wallace*'s presumption of injury focused the inquiry on the conduct of the employer, *Keays*' evidence-based formula shifts the focus to what loss the employee actually suffered. In many respects, this takes the risk out of termination.

While a number of the financial risks from *Wallace* remain, others have been substantially reduced. In particular, shareholders no longer have to worry about \$950,000 damage awards under the tort measure of recovery;¹²⁹ rather, having been collapsed into the *Keays/Hadley* rubric, bad faith damage awards, like other awards for mental distress, will be consistently modest.¹³⁰ Similarly, since *Keays* damages are paid out in a lump sum, rather than as an extension to the notice period, an employer's financial liability will be more predictable. That is, not only will awards fall in line between the usual \$20,000 - \$75,000, irrespective of whether the employee is at the highest or lowest level of the company, but there will also be no uncertainty about the length of the notice period extension. Under *Wallace*, the variance between a three to six month extension (or more) had dramatically different financial implications depending on the employee's level of remuneration.

The operational risks associated with bad faith terminations under *Keays* have also received a major adjustment. Most significantly, employers' operational procedures are now subject to far less scrutiny, which permits much more flexibility with respect to termination. For example, while it was previously considered bad faith to fire someone without a face-to-face meeting,¹³¹ employees must now lead evidence that this caused

¹²⁷ See eg, *Wallace* note 3.

¹²⁸ *Soost* at para 28; see also *Mathieson v Scotia Capital Inc* (2010), 78 CCEL (3d) 76 (Ont SCJ) at paras 82-83.

¹²⁹ See *Sulz v Attorney General et al*, *supra* note 121.

¹³⁰ See eg, *Ditchburn v Landis & Gyr Powers Ltd* (1997), 34 OR (3d) 578 (CA), where the Ontario Court of Appeal upheld a \$15,000 mental distress damage award for a 59 year old employee with 27 years of service, who had been subject to particularly egregious treatment by his employer.

¹³¹ See eg, *Carter v Packall Packaging Inc*, *supra* note 100.

them injury. Given the difficulty of recovering for far more egregious conduct,¹³² engendering liability for this seems quite improbable. As a result, employers might, for example, now explore methods of mass terminations via electronic means. A further benefit of *Keays* is that it eliminates the risk of aggressively litigating wrongful dismissal claims. Employers previously faced sanctions for playing litigation “hardball”, in light of the parties’ drastic resource imbalance, but that is no longer the case. Consequently, operational resources previously dedicated to preventative measures can now be cut or shifted to funding litigation. Think of it this way: is it still necessary to pay for training on best termination practices if the liability now flows from the plaintiff’s actual injury and not the termination conduct itself?

Perhaps the most disappointing aspect of *Keays* is the impact it will have on the reflexively regulated normative system of “upwardly ratcheting” employment standards. If *Wallace* created a healthy eco-system for ever-improving workplace norms, then it has been thoroughly deforested by *Keays*. Consider this: Given the prospect of suing employers that are willing, and now able, to play “hardball” under a framework that discourages awarding additional damages, plaintiffs’ lawyers will be disincentivized from bearing the risk of litigating on contingency. As a result, less wrongful dismissal cases will be heard by the courts, leading to fewer reported decisions, which already have diminished relevance in light of the focus on plaintiff injury and not employer conduct. Consequently, training on best practices will be deemphasized, meaning that operating procedures will stagnate, or worse, erode. In other words, rather than having an incentive under *Wallace* to constantly improve, the net result under *Keays* will be a “ratcheting down” of normative employment standards.

Recall that reflexive regulation operates by influencing actors’ normative practices so that a preferred course of conduct is prioritized in light of the risks associated with discouraged conduct; by taking the risk out of termination, the Supreme Court has stripped away an important layer of reflexive regulation that protected employees and improved norms for all workplaces across Canada. Some have suggested the net effect of *Keays* will make employers more competitive in the face of international competition,¹³³ but time will tell whether this was, in fact, the right trade-off to make.

CONCLUSION: REVIVING THE TORT OF BAD FAITH DISCHARGE

This paper has argued the critical importance of injecting risk into employers’ decision-making process. If the *Keays/Hadley* framework is going to stand, then thought must be given to reviving the tort of bad faith discharge that was urged on the Supreme Court

¹³² See eg, *Keays*, *supra* note 2, *Brien v Niagara Motors*, *supra* note 114, and *Fox v Silver Sage Housing Corporation*, *supra* note 117.

¹³³ See Ryan Henry Edmonds, “All Hands to Starboard! Situating Wrongful Dismissal’s Recent Course Correction into Broader Labour Market Policy” (2010) [unpublished, submitted in fulfillment of ‘Labour and Employment Policy Colloquium’ (5550.03) at Osgoode Hall Law School] online: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1737944, for a discussion of the interplay between the judiciary’s role in using legal doctrine to set quantum of termination costs and broader labour market policy.

during the hearing in *Wallace*.¹³⁴ Not only should the tort measure of recovery be available to employees in the most egregious of circumstances, but in order to positively influence normative employment standards, employers also need to know that their workplace practices are under judicial scrutiny. As it stands, for this the *Keays/Hadley* framework is insufficient. Although a tort of bad faith discharge would undoubtedly face judicial resistance for overlapping in purpose with *Keays/Hadley*, following a thorough understanding of this paper, and for the sake of protecting the standards of dignity and decency still enjoyed by workplaces across Canada, it is hoped the reader will realize such a remedy is nonetheless necessary.

¹³⁴ See *Wallace* at paras 75-78 and Ball, “Bad Faith Discharge”.