5 Ways to Get Socked with Wallace Damages for Bad Faith Termination

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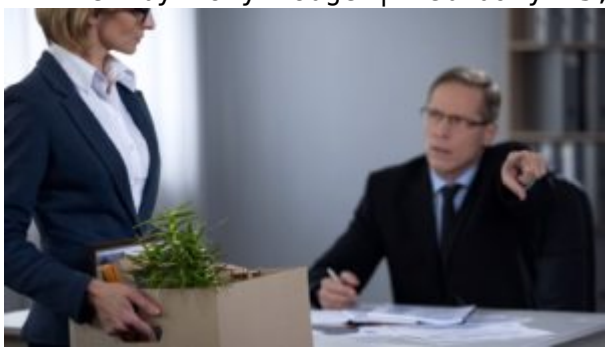

Liability-wise, how you terminate may be just as important as why you terminate

Sometimes, termination isn't just wrongful but downright mean. When terminations fall into the latter category, employers are subject to a special kind of damages on top of notice and other amounts payable for wrongful dismissal. Although they're called "moral damages," people still typically refer to them by their previous name of "Wallace damages." (As will we for purposes of this article.) And they can run into 5, 6 and even 7 figures. Wallace damages are supposed to be reserved for the nastiest employers, i.e., the ones who act in "bad faith." But because courts have historically set the bar so low, employers can engage in bad faith termination without intending to. Here are common termination process pitfalls that can expose your organization to liability for Wallace damages.

The Wallace Case

The Canadian Supreme Court invented Wallace damages in a 1997 case where a Manitoba grain company fired a 45-year-old salesman after 14 years of unblemished and stellar service. When it first hired him, the company had verbally assured the salesman of job security and fair treatment. But the company wasn't true to its word. When the axe fell, it refused even to explain its reasons—other than to say it had good cause to terminate.

The salesman sued and the case eventually reached the Supreme Court, which sided against the company. Every employer has an implied obligation of good faith and fair dealing to its employees, the Court reasoned. Termination doesn't extinguish this obligation. On the contrary, good faith is especially important at termination since this is when employees are at their most vulnerable. According to the Court, employers who cause "humiliation, embarrassment and damage to [an employee's] self-esteem" during the termination process should pay damages. The Court also decided that courts should consider bad faith as a factor in deciding an employee's termination notice. In this case, the Court ordered the grain company to pay a whopping 24 months' notice, or $15,000 in damages [*Wallace v. United Grain Growers*, [1997] 3 S.C.R. 701].

The Honda Case

Wallace spawned a flood of bad faith termination lawsuits and soon courts were extending termination notice almost as a matter of routine. To make matters worse, there was a lot of uncertainty over what employers were supposed to do to avoid

getting socked with damages. “The obligation of good faith and fair dealing is incapable of precise definition,” admitted the *Wallace* Court. “However, at a minimum, in the course of dismissal, employers ought to be candid, reasonable, honest and forthright.”

By 2008, the situation had become so dicey that the Supreme Court felt it necessary to establish some new limits on *Wallace* damages. The opportunity came when Honda fired an employee diagnosed with chronic fatigue syndrome for missing too much time. In addition to being wrongful, the Ontario court found the termination to be in bad faith. In addition to extending his termination notice to 15 months, the court awarded the employee $500,000 in punitive damages for Honda’s “high-handed and outrageous” behaviour. “It goes without saying that Honda is a worldwide corporation, a Leviathan compared to the minnow that [the employee] represents. . . A large whack is required to wake up a wealthy and powerful defendant to its responsibilities.”

After the Ontario Court of Appeal slashed the *Wallace* damage award to $100,000, the Supreme Court eliminated it completely. Although not taking away an employee’s right to collect damages for bad faith termination, the Court drew a new line in the sand. Courts could no longer just extend the termination notice period; from now on, employees would have to prove the actual damages they suffered as a result of the employer’s bad faith. Since the employee couldn’t prove or put a money value on the mental stress he suffered, Honda didn’t have to pay him *Wallace* damages [*Honda Canada Inc. v. Keays,* [2008] 2 S.C.R. 362].

Strategic Pointer: Although the *Honda* Court was thinking of mental stress, subsequent courts have allowed employees to collect Wallace damages to compensate them for economic and professional losses they incurred as a result of the bad faith way they were fired.

The Current State of *Wallace* Damages

Although *Honda* made it harder for employees to qualify for *Wallace* damages, courts are still handing out huge “moral damages” awards for bad faith termination. As a result, employers need to beware of the liability risks and ensure that managers and supervisors charged with terminating employees behave accordingly. But simply telling people involved in the termination process to “act in good faith” won’t do much good. The challenge is to explain what good and bad faith actually mean, not simply as moral concepts but as principles of behaviour for termination. How? **Answer:** By using actual court cases as guideposts for what you should and especially shouldn’t do during the termination process.

5 Bad Faith Termination Pitfalls to Avoid

While innocent and honest mistakes may make termination wrongful, they’re not enough to make it bad faith. As one Ontario court describes it, cases where *Wallace* damages get handed out almost always involve “the presence of something akin to intent, malice or blatant disregard for the employee.” It’s conduct best characterized “as callous and insensitive treatment, or as `playing hardball.’” While each case is different, there are 5 common patterns of “callous and insensitive treatment” to watch out for:

1. Making False Accusations

Good faith covers not just how you handle a termination but how you reach the decision to terminate in the first place. As an HR director, you know all about the limits of “just cause.” You also know that certain forms of misconduct, such as violence, harassment, dishonesty and fraud, constitute just cause for termination.

But what you also need to realize is that you must have some reasonable basis for believing that the employee engaged in such misconduct. Simply believing an unsubstantiated accusation isn't enough and could be construed as bad faith.

Example: A municipality knew that an inspector had designed the building he was about to inspect but gave him the green light. Later, it claimed it had just cause to fire the inspector for conflict of interest. The Ontario court found bad faith termination and awarded the inspector $200,000 in *Wallace* damages on the basis of the mental stress he suffered and the harm done to his professional reputation [*Johnston v The Corporation of the Municipality of Arran-Elderslie*, 2018 ONSC7616 (CanLII)].

The Moral: Investigate and substantiate allegations of wrongdoing before acting on them, especially if the employee involved has served your company well.

2. Insensitive Timing

Terminated employees arouse great sympathy. And these emotions and sense of "Leviathan v. minnow" are often at the very heart of the bad faith lawsuit. "Employers might have a valid justification for their handling of the termination," according to an Alberta lawyer. "But their explanations might not get serious consideration if they come across as insensitive or indifferent to the plight of the terminated employee." One of the best ways to come off looking like a monster is to choose a sensitive or awkward time to deliver the pink slip. Examples:

- The anniversary of the employee's start with the company;
- Just before the employee is about to go on maternity leave [*Rae v. Attrell Hyundai Subaru*, [2005] O.J. No. 4917]; and
- When the employee is suffering a physical or emotional crisis outside of work [*McNamara v. Alexander Centre Industries Ltd.,* [2001] O.J. No. 1574] (24-year employee fired because and right after he found out he had a disability)].

3. Firing Employees in Front of Co-Workers

Termination is inherently demeaning and it's almost impossible to completely prevent the employee from experiencing at least some degree of humiliation. But if you do it in a way that's likely to embarrass the employee, like breaking the news in public or in front of co-workers, expect to pay a high price:

- **$250,000:** Grabbing an employee by the elbow and making her count to 10 to prove to her colleagues that she was intellectually capable of doing so just before firing her [*Boucher v. Wal-Mart Canada Corp.,* 2014 ONCA 419];
- **$70,000:** Belittling a disabled employee in front of her colleagues at the time of termination [*Strudwick v. Applied Consumer & Clinical Evaluations Inc*., 2016 ONCA 520]; and
- **$10,000:** Unceremoniously escorting a bartender accused of theft off the premise during his shift in front of co-workers and customers [*Schimp v. RCR Catering Ltd*., [2004] N.S.J. No. 57].

Moral: Do everything in your power to keep the delivery of the news to terminate as respectful, unembarrassing and dignified as possible. At a minimum, break the bad news to the employee discreetly and in private:

4. Deliberately Misleading the Employee

Good faith, says the Court in *Wallace*, involves being "candid, honest and forthright" with employees at the time of termination. Think about that for a second. You're not supposed to humiliate employees or rub their noses in it; but you need to be

“candid.” This strongly suggests that you’re not supposed to tell “white lies” to spare an employee’s feelings. Steering a line between candor and the obligation to inflict humiliation isn’t easy. But here’s some help.

First of all, lawyers tell the *Insider* that you don’t have to be brutally honest. “You can and must consider the employee’s feelings,” according to one. “If that involves putting the best spin on the situation, so be it.” What you can’t do is deliberately mislead, lie or blindside the employee. The employee, in other words, should have some inkling of what’s coming.

Example: A general manager with a BC non-profit company gets a mostly positive annual review. You’re going to make an excellent manager, the board tells him. Just keep us apprised of any costs that go over budget. A year later, he gets a letter saying he’s been fired for dishonesty and insubordination. It’s a bolt from the blue. The court finds the company guilty of bad faith termination [*Zadorozniak v. Community Futures Development Corp*., 2005 BCSC 26 (CanLII)].

5. Damaging the Employee’s Prospects of Finding Another Job

One of the most egregious things an employer can do to open the door to *Wallace* damages is to leave the employee damaged goods in the eyes of future employers. Examples:

- BC car dealer publishes negative statements about a former salesman in the trade press [*Hamer-Jackson v. McCall Pontiac Buick*, [2000] B.C.C.A. 416]; and
- Bank blacklists employee and her family members and withdraws previously paid personal loan payments which hurt the employee’s credit rating and damaged her ability to get hired by another employer [*Mastroguiseppe v. Bank of Nova Scotia*, [2005] CarswellOnt 7607 (Ont. S.C.J.)].

Moral: If possible, offer to help terminated employees find another job. That might involve providing outplacement services and/or positive references. However, you should also understand that the failure to give a terminated employee a positive reference can be but isn’t necessarily bad faith justifying *Wallace* damages. As with other forms of conduct, there are no hard and fast rules. Courts will consider the entire context of the dispute. Thus, the BC Supreme Court ruled that an environmental engineering firm didn’t have to pay Wallace damages for refusing to provide a reference, particularly since the company wasn’t satisfied with the terminated employee’s performance [*Ashby v. EPI Environmental*