

# Constructive Dismissal: The Perils of Unilaterally Changing Pay Formulas



While few employers would be brazen or foolish enough to unilaterally cut salary levels expressly agreed to in an employment contract or collective agreement, it may be more tempting to try this approach when the agreed to pay isn't a specific dollar amount but a variable pay formula. But don't kid yourself. In addition to violating the contract, unilateral changes to compensation formulas can lead to liability for "constructive dismissal"—a form of wrongful dismissal where an employer doesn't actually tell an employee that he's fired but changes his job terms so substantially and unfavourably that it forces him to leave. Because it goes to the very heart of the employment relationship, changing the terms of compensation arrangement is exactly the kind of action that rises to the level of constructive dismissal—even if the change affects only the variable part of the pay arrangement.

## **Replacing Cash Bonus with Stock Shares = Constructive Dismissal**

An Alberta case is an illustration of the risks of unilateral changes to variable pay arrangements. The case involved a galvanizing company that paid a portion of company profits to employees, in addition to regular wages. One year, without warning, the company decided to issue company shares instead of cash bonuses. The company claimed it could make unilateral changes because the profit-sharing plan was a company policy rather than a term of an employment contract. But the court disagreed and ordered the employer to pay profits in cash to each employee. Switching from cash bonuses to stock shares substantially changed the essential terms of employment and amounted to constructive dismissal, the court ruled [Carabine v. Daam Galvanizing, 2000 ABPC 56].

## **What You Can Do**

In finding the company liable for constructive dismissal, the Carabine court said the employer should have communicated the changes to employees and gotten their input in restructuring the plan. In other words, making unfavourable changes to variable pay arrangements isn't necessarily illegal; what is illegal is making those changes unilaterally. General Rule: Pay cuts and other contractual changes in compensation that are unfavourable to employees aren't legally valid unless the affected employee:

- Expressly agrees to them; and
- Receives consideration, i.e., something of value in return for that agreement.

Also recognize that, absent specific collective agreement contractual language to the contrary, you generally don't have to offer new employees who haven't yet signed an agreement the same exact terms that apply to current employees who are under contract. New employees start with a clean slate and you're free to negotiate any variable pay arrangement you want.