

# When Do Cuts in Employee Benefits Cross the Constructive Dismissal Line?



✖ Termination comes in different varieties. The most common form is to make a deliberate decision to terminate. But there's also a more subtle way to accomplish the same purpose: Change the terms of employment so unfavourably that the employee feels compelled to leave. Termination without the pink slip is called constructive dismissal and it's considered wrongful. And what makes it so dangerous is that you can be liable for constructive dismissal even if it didn't actually intend to force the employee out. One way to accidentally commit constructive dismissal is to cut an employee's benefits. Here are 4 traps to avoid.

## 1. Cutting Salary or Wages

The most obvious form of a compensation-related constructive dismissal offence is a direct cut in wages and salary. The deeper the cut, the greater the risk. But there's no bright line of how deep you can cut before crossing the line.

**10% or less isn't enough:** We found courts were generally unwilling to find constructive dismissal when compensation changes resulted in a less than 10% change in an employee's income. However, 10% or less could be enough when coupled with unfavourable changes in the other terms of employment. Thus, for example, an Ontario court ruled that a pharmacy that cut an employee's salary from \$40 to \$36 per hour, a 10% cut, and also changed her position was liable for constructive dismissal [*Ontario Chemists Rx Inc. v. Ibrahim*].

**20% or more is enough:** By contrast, changes that result in at least a 20% reduction in income generally did result in a finding of constructive dismissal. For example, a BC court ruled that reducing an employee's monthly salary from \$3,600 to \$2,400—a 30% cut—breached a fundamental term of the employment relationship and was constructive dismissal [*Farquhar v. Butler Brothers Supplies Ltd.*].

## 2. Cutting Bonuses and Commissions

Unilaterally cutting employees' bonuses and commissions can be just as bad as cutting their salary, depending on the amount of the cut and how much of the employee's income comes from bonuses and commissions.

**Example:** As part of a change in the employee's job responsibilities and title, an employer removed a bonus of five percent of company revenues. The court said the

employee had been constructively dismissed because the revenue bonus was a critical part of his compensation package. Eliminating the bonus would likely cut his compensation 25%—a substantial change [*MacLean v. CrossOff, Inc.*].

That's not to say that you can never reduce bonuses and commissions. If the reduction doesn't have a significant dollar impact, it won't by itself amount to constructive dismissal.

**Example:** As a result of corporate restructuring, a company cut an employee's bonus from 15% to 10% of salary—a net income loss of \$4,500. The court ruled that the cut was too insignificant to amount to constructive dismissal [*Poole v. Tomenson Saunders Whitehead Ltd.*].

### 3. Restructuring the Compensation Package

Although it's more subtle than a wage or bonus cut, unilaterally changing the structure of an employee's compensation package can achieve the same effect. If the restructured package is substantially less favourable than what the employee agreed to at the start of employment, it could be constructive dismissal. One way to restructure your way into constructive dismissal is to convert guaranteed salary to contingent payments such as commissions and bonuses.

**Example:** An employee had a guaranteed base salary with commissions and benefits and managed 21 branches of a real estate company that produced more than \$16 million in gross income. The company demoted him to manager of a poorly performing branch. At the new position, the employee received commissions rather than a guaranteed base salary. Adding insult to injury, his commissions were based on the sales of the poorly performing branch. True, the commission was 3% higher than what other branch managers got. The company also threw in a "reorientation allowance." But the Canadian Supreme Court ruled that the company had constructively dismissed the employee because the new package didn't compare to the previous one due to its failure to include a guaranteed base salary [*Farber v. Royal Trust Co.*].

Of course, shifting from guaranteed to contingent isn't the only way to adversely re-engineer a compensation package. The reverse change can also rise to the level of constructive dismissal. In other words, there are no pre-determined formulas. Courts will look at the overall impact of the changes, including the amount and nature of the cuts made.

**Example:** A store manager earns \$92,000, including \$33,000 in base salary plus a personal bonus and a bonus tied to the store's profitability. The employer decides to merge salaries with personal bonuses. To make up for the lost bonus opportunity, the store adjusts the manager's base salary to \$64,000. The manager claims that this is really a pay cut and resigns. The BC court rules that the manager was constructively dismissed because the store bonus was a fundamental term of the employment contract and eliminating it resulted in a significant salary reduction [*Wood v. Owen De Bathe Ltd.*].

### 4. Cutting and Restructuring Benefits

Significant changes in benefits can also result in constructive dismissal, especially when combined with cuts in direct compensation. As with direct compensation, the most obvious form of an adverse change is a direct cut in benefits. This could include eliminating or reducing contributions to pension, health and other employer-sponsored benefits plans.

Of course, the size of the cut is a key factor in determining if benefit reductions

amount to constructive dismissal. Although there's no pre-determined cutoff point, courts do look at the value of the benefits cut and the percentage by which it decreases the employee's earnings in determining if constructive dismissal occurred.

**Example:** In addition to cutting her salary and removing a wellness bonus, a BC employer stopped paying Medical Service Plan premiums on an employee's behalf. The total impact of those changes was an approximately 20% reduction in compensation. The court found this to be "material" and found the employer liable for constructive dismissal [*Streight v. Dean*].

**Example:** A SK employer failed to make \$1,218 in pension contributions for an employee. This represented 3% of her salary. The court dismissed the employee's constructive dismissal claim, ruling that this wasn't significant enough to amount to a fundamental breach of the employment contract [*Hlewka v. Moosomin Education*].

**Example:** As a result of hard economic times, an Alberta employer suspended matching contributions to an RRSP plan and cut vacation benefits from six to four weeks. Two employees claimed constructive dismissal. The cuts represented between six and eight percent of the employees' total compensation, not enough to make the employer liable for constructive dismissal, according to the court [*Otto v. Hamilton & Olsen Surveys Ltd.*].