

Executive employment contracts: What C-suite executives need to know | Frank Portman

By **Frank Portman**

Law360 Canada (September 25, 2024, 11:34 AM EDT) -- One of the most important legal relationships in any Canadian's life is their legal relationship with their employer. This relationship is defined by the employment contract, written or unwritten, between worker and employer about how they will work together. This is especially true for executives and executive employment contracts.

However, the complexity and nuance of executive employment contracts mean that they must be interpreted with particular care and caution. Even for those experienced in dealing with commercial contracts, executive employment contracts have special considerations that can significantly change their impacts in ways that can even be contrary to what their wording actually says.



Frank Portman

1. Executive employment contracts are important but won't cover everything

Executive employment contracts are often complex and lengthy. Given the importance of the position and the stakes involved for all parties, they aim to avoid leaving anything to chance.

Even with this as the goal, however, executive employment contracts cannot predict every circumstance that can arise throughout an employment relationship. This is particularly true for executives, whose responsibilities are wide-ranging and can vary dramatically from day to day.

To account for this, employment law has evolved to fill in gaps in employment contracts. Almost all of these inferences favour the employee. In other words, an ambiguity that is not dealt with in an employment contract will usually be determined in an employee's favour. This applies to executives, too.

2. Executive employment contracts will not always mean what they say

The first step in interpreting an executive employment contract is, of course, to read it to see what it says. In the vast majority of contracts, it is usually enough to interpret the words of the contract to determine what rights the contract provides.

Importantly, executive employment contracts are also subject to an additional consideration that other contracts are not: employment standards legislation. Although the exact requirements vary from province to province, employment standards legislation puts limits on what parties can agree to.

What happens if a part of an employment contract violates these employment standards? That provision becomes unenforceable in every way. As a precedent-setting case, *Machtiger v. HOJ Industries Ltd.*, [1992] 1 S.C.R. 986, established almost 35 years ago, legally, this renders the clause in question as though it never existed. In most cases, this benefits the employees. Severance entitlements can balloon, sometimes from as little as eight weeks to as much as 24 months or more. Extremely restrictive, non-solicitation or non-competition covenants can evaporate.

Executives need independent legal advice to understand exactly what components of their employment contracts may or may not be enforceable and what their rights and responsibilities are

as a result.

3. Executive employment contracts can become stale and obsolete

Executive employment contracts are generally long-term contracts. However, they can become obsolete.

The most common way in which an employment contract can become obsolete is that a court finds that one of its provisions contravenes employment standard legislation. Such a finding does not simply help guide the drafting of future contracts. It applies to all existing employment contracts as well.

This is what occurred in *Waksdale v. Swegon North America Inc.*, [2019] O.J. No. 5021, in which a contractual provision in common use at the time was found to invalidate the termination provision. Overnight, massive amounts of termination provisions across the contract were instantly invalidated, exponentially increasing employee entitlements on termination.

Another less common way in which an employment contract can become obsolete is the doctrine of substratum. This doctrine, as described in *Celestini v. Shoplogix Inc.*, 2023 ONCA 131, applies when, over the course of an employment relationship, an employee's work "fundamentally changes" such that the employment contract governs a position that functionally does not exist anymore. While that could apply in circumstances where a long-time employee rises through the ranks from an entry-level position to a senior executive, it can also apply to fundamental changes where the employee stays in the same position.

Such obsolescence can fundamentally alter the rights of both an executive and the employer, even with a written contract.

4. Executive employment contracts can radically change how disputes are resolved

While the majority of Canadian employment law disputes go through the courts, this is not always true for executives. Executive employment contracts often contain provisions requiring that disputes arising from them go to arbitration, rather than the courts.

Arbitration can provide many advantages to litigants. It is quicker, allows the parties to select an adjudicator they feel is appropriate, can be fully confidential and private and gives the parties significant control over the process they use to resolve a dispute. However, arbitration can be expensive and can fundamentally change how a dispute is addressed and resolved.

5. In executive employment contracts, not all compensation is treated equally

For many executives, salary may not be the only form of compensation. Instead, bonuses, stock options and grants, and other forms of compensation can form a significant, if not majority, component of their compensation. Indeed, many executives prefer this because non-wage compensation can often result in better tax-reduction options.

Many times, these metrics of compensation are dealt with in documents, agreements, or policies different from those of the executive employment contract. Annual bonuses can be subject to a particularized bonus plan. Stock options or grants may be dealt with by their own separate, complex agreements.

Further, termination provisions in executive employment contracts often significantly reduce or eliminate the payment of these non-wage compensation structures during the notice period. This is particularly true in the case of annual bonuses or stock options. While a contract may stipulate a lengthy notice period, it often stipulates that the value of that notice period is restricted to salary.

Needless to say, with the length of most executive termination provisions extending to long periods, this can make a huge difference in an executive's entitlements.

It can also impact whether executives are eligible for performance bonuses for work they do prior to termination but which are paid after termination. In one case that went to the Supreme Court of

Canada, *Matthews v. Ocean Nutrition Canada Ltd.*, 2020 SCC 26, an executive received a liquidity event bonus of over a million dollars, despite the liquidity event only occurring 13 months after he was constructively dismissed. However, a more tightly-drafted employment contract could have eliminated this entitlement completely.

6. Executive employment contracts need legal review

Among complex contracts, executive employment contracts are notable for the number of different legal considerations that apply to their interpretation, and how the entire meaning or effect of a provision can change based on a misplaced or careless word or definition.

Given the enormous stakes for executives and their families, it is always wise to consult with an executive employment lawyer before signing a contract.

Similarly, when dealing with a dismissal, an executive employment lawyer can ensure that executives have a firm understanding of what their legal entitlements are rather than what the contract suggests they might be. To do otherwise could be to leave money on the table.

Frank Portman is an employment lawyer at Massey LLP. His specialty is executive employment law where he assists presidents, vice-presidents and other C-level executives and the organization seeking to hire their talents, to complete the deal through effective executive employment contracts.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the author's firm, its clients, LexisNexis Canada, Law360 Canada or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

Interested in writing for us? To learn more about how you can add your voice to Law360 Canada, contact Analysis Editor Peter Carter at peter.carter@lexisnexis.ca or call 647-776-6740.