

'Doctrine of frustration' implications for executive employment contracts | Frank Portman

By **Frank Portman**

Law360 Canada (January 20, 2025, 11:23 AM EST) -- In Ontario, the "doctrine of frustration" of contract has significant implications for c-suite executives who have executive employment contracts. A good executive employment lawyer should be familiar with this legal principle, but it is not well understood by c-suite executives.

This legal principle applies when unforeseen events render the performance of contractual obligations impossible, thereby terminating the contract without liability for either party.

Historically, frustration has most often arisen in the context of long-term medical conditions that have permanent impacts on an employee's ability to perform the job.



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However, recent case law has emphasized its application in non-medical contexts, with important lessons for executives.

The easiest way to think of the "doctrine of frustration" is the "unknown unknowns" that were unforeseen circumstances and therefore did not get included in the executive employment contract. The phrase "unknown unknowns" was popularized by United States Secretary of Defense Donald Rumsfeld, who served under the administration of George W. Bush (2001-2006).

What is 'frustration of contract?'

"Frustration of contract" occurs when an unforeseen event, beyond the control of either party, fundamentally changes the nature of the contractual obligations, making it impossible to fulfill the contract. In such cases, the contract is automatically terminated, and neither party is liable to the other.

Importantly, in Ontario, if an employment contract is frustrated for non-medical reasons, the employer is relieved of their obligation to provide statutory termination and (if applicable) severance pay.

A critical element of frustration is that the underlying event could not and was not contemplated by the parties at the time of the contract. The parties are free to contract for any possible eventuality, and if a contract covers the subject matter of the alleged frustration, it will govern the parties' rights and frustration will have no application.

There are three categories of usual circumstances in which non-medical "frustration of contract" can arise.

1. Unforeseen circumstances, 'Acts of God'

The first, was dealt with in the Ontario Court of Appeal's recent decision in *Croke v. VuPoint Systems Ltd.*, 2024 ONCA 354.

In this landmark case, the Ontario Court of Appeal upheld the Superior Court's decision that an

employee's refusal to comply with a mandatory COVID-19 vaccination policy constituted frustration of the employment contract. VuPoint Systems Ltd. implemented the policy following a directive from Bell Canada, a major client for whom the employee performed essentially all of his work, and which prohibited unvaccinated employees from working for Bell.

The employee's non-compliance rendered him unable to perform his duties, leading to the frustration of the contract, since it rendered him fundamentally unable to do his job, which was to provide services to Bell.

As such, since the vaccine requirement was not imposed by either party, it was deemed to have frustrated the contract.

It should be noted that the decision in *Croke* is limited, and is likely to only apply in cases where employment is tied very closely to a particular client, such that not being able to work for the client functionally means the employee can no longer work. This is unlikely to arise in executive employment circumstances.

2. Disaster, outside event destroys business

The second, which was canvassed in *Clarion Lakeside Inn v. UFCW Local 175*, 2022 ONSC 3850, is where some disaster or event caused by an event outside of the parties' control destroys the business and effectively ends it.

That case involved the closure of a business due to a fire. However, the owners intended to reopen the business, albeit after significant downtime.

In determining that the fire did not frustrate the employment relationships of the staff, the court emphasized that frustration does not apply if the employer's operations are only paused and not permanently ceased.

Had the business closed permanently, it is probable that the frustration doctrine would have applied to at least some of the employees' circumstances.

3. Employee can no longer meet legal requirement for the position

The third category occurs when an employee is no longer able to meet a necessary legal requirement for the job. This occurred in the case of *Cowie v Great Blue Heron Charity Casino*, 2011 ONSC 6357 (Div. Ct.)

In that case, with the passage of the *Private Security and Investigative Services Act*, the employee became subject to a licensing requirement that required a clean criminal record. The employee did not have such a record and their employment was ended. The Divisional Court found that the passage of the Act was an unforeseen event out of the control of the parties, which rendered it impossible (and indeed illegal) for the employee to continue in their position, and was therefore frustrated.

Implications of 'frustration of contract' for c-suite executives

While non-medical frustration of executive employment contracts is rare, there are certain distinct circumstances where it can arise.

First, frustration might arise where external factors render the continued business impossible. This could be the destruction of physical premises, such as what occurred in *Clarion Lakeside Inn*. However, it could also occur in the case of legal requirements. For example, in 2018, changes to the *Consumer Protection Act* rendered many types of door-to-door sales of home appliances illegal. It is arguable that such changes, rendering a business illegal, would constitute frustration of contract.

Second, frustration could occur when an executive loses a certification necessary for their position, such as a chief legal officer losing their law licence, or a chief accounting officer losing their accounting license. It could also occur in industries requiring security or other clearance.

Frustration of an executive's contract could be disastrous, with the executive not only losing their position but also their accrued termination entitlements. The only way to avoid this outcome is the effective use of executive employment contracts with proper 'frustration' clauses.

How executives can prevent 'frustration' in executive employment contracts

First, executives should seek guaranteed severance payouts that are paid even in the event of a frustration of contract. It is open to the parties to provide severance payments that apply even in cases that could, in the absence of such a contract, be frustration, but this requires precise and explicit drafting by an experienced executive employment lawyer.

Second, executives should ensure that the contract does not expand the list of "requirements" on the executive beyond what is actually necessary to perform the work. Expanded requirements carry a greater risk of frustration, since they create more grounds upon which an employer can assert that frustration occurs.

Both of these protective measures require detailed, written executive employment contracts, reviewed by experienced an executive employment lawyer. Failing to do so could lead to a loss of significant entitlements. And leaving 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.

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