

THE TERM CONTRACT TRAP

There are two types of employment contracts, indefinite and limited-term. The misuse of the latter, and the resulting liability, is a trap into which employers routinely stumble.

If used properly, limited-term contracts can be a useful and effective tool for structuring employment relationships. In my experience, however, there are three common outcomes from the use of limited-term employment contracts and two of them are undesirable.

The purpose of a limited-term employment contract is to document a relationship which is truly time-limited. The employer hires an employee for a particular period of time and when the contract expires the employee departs.

Upon the expiry of the term agreement and the cessation of the relationship, the employer has no obligation to provide working notice or any pay in lieu. Correspondingly, the employee has no basis for severance-related claims against the employer.

This use of a limited-term contract is perfectly legitimate and, if properly administered, can be a very effective tool for documenting the relationship with the employee. That's the desirable outcome.

Often, however, limited term contracts are not structured properly, which leads to one of the undesirable outcomes.

If the employer wishes to sever the relationship prior to the expiry of the term of the agreement, it is critical to have an early termination formula built into the contract. This is important because of the common law rules regarding early termination of a limited-term contract.

The common law requires that, in the absence of an early termination formula, the severed employee is entitled to be paid out for the entire balance of the contract period. It seems that employers usually don't realize they've been caught by this rule (or that it even exists) until the relationship has been severed and it's too late to avoid the liability.

In the case of a lengthy term, the resulting payout to the employee can be quite substantial.

In a recent case, the B.C. Provincial Court emphasized the rule applying to early termination of limited-term contracts. Frederic Ntibarimungu was a teacher employed by the Vancouver Career College commencing in 2006. He was signed to a new contract in 2007 stating that his employment would expire in January of 2008.

In the interim, however, the College claimed to have received complaints about his teaching style and to have concluded that he had a poor teaching attitude. As a result, Frederic's employment was terminated.

The Court did not accept the College's position that Frederic was terminated for reasons amounting at law to just cause for summary dismissal. That left the Court with the task of assessing damages owing to Frederic as a result of the termination.

The Court re-stated the "general principle in law ... that wrongfully dismissed employees on fixed-term contracts are not entitled to reasonable notice but rather to the balance due under their fixed-term contract." The College was ordered to pay Frederic damages representing the wages he would have earned during the balance of the term of his agreement.

I'd say that misuse of limited-term contracts definitely falls within the top ten mistakes made by inexperienced employers and human resources staff. Avoiding this trap simply requires some basic knowledge of how the courts view the early termination of limited-term contracts.