

Employment Update: Enforcing Employment Contracts After Substantial Changes

Date: April 17, 2023

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Most employers are aware of the importance and value of employment contracts, particularly for the purpose of setting out and limiting an employee's termination entitlements. However, many employers may not be aware that employment contracts are not always set in stone and risk going stale as roles change, grow and expand. In fact, changes over time to an employee's position, compensation or responsibilities can have an impact on the enforceability of the termination provisions in the original employment contract. This issue was recently addressed by the Ontario Court of Appeal in [Celestini v. Shoplogix Inc., 2023 ONCA 131](#).

Background

In 2002, Mr. Celestini co-founded Shoplogix as a technology start-up company. In 2005, he stepped down from his CEO role to that of a Chief Technology Officer ("CTO"). At the time Mr. Celestini became CTO, he signed an employment contract that limited his entitlements upon termination to a 12-month notice period. This contract remained the only written employment contract signed between the parties at the time of Mr. Celestini's termination.

Twelve years later in 2017, Mr. Celestini's employment was terminated without cause after Shoplogix was acquired by another company. At the time of his termination, Mr. Celestini argued that the employment contract no longer applied because his role had since substantially changed. In 2005 when he started as the CTO, Mr. Celestini was not responsible for any operational programs or anything directly related to sales or research and development. He had no staff, nor any managerial responsibilities. By contrast, by 2017, Mr. Celestini was expected to handle important operational and managerial duties that extended well beyond his role as CTO following the layoff of senior team members and a mass restructuring. While Mr. Celestini's title remained CTO, he was assigned significant new duties and responsibilities, including sales which involved significant international travel. Shoplogix argued that Mr. Celestini was bound by the 12-month notice period in his 2005 employment contract, as his role did not significantly change during his employment.

The Superior Court Decision

The Court applied the doctrine of “changed substratum” and held that the 2005 employment contract did not apply. In the employment law context, the doctrine of changed substratum provides that significant changes in employment may cause the termination provisions in a previous contract of employment to become unenforceable at the time of termination.

The Court found that Mr. Celestini was assigned significant additional responsibilities that led the “substratum” (or foundation) of his written employment contract to disappear. It followed that the 12-month contractual notice period in his employment contract was considered unenforceable and Mr. Celestini was awarded 18 months of pay in lieu of notice in accordance with the common law.

In summarizing the law, the Court referenced a quote from Justice Perrell in [MacGregor v. National Home Services, 2012 ONSC 2042](#): “The idea behind the changed substratum doctrine is that with promotions and greater attendant responsibilities, the substratum of the original contract has changed, and the notice provisions in the original employment contract should be nullified.”

The Court of Appeal's Decision

Shoplogix appealed the decision and argued that the motion judge erred in finding that any changes in Mr. Celestini’s employment duties were sufficient to engage the doctrine of changed substratum.

On February 28, 2023, the Court of Appeal upheld the Superior Court’s decision to set aside the 2005 employment contract. The Court of Appeal agreed that the employee’s responsibilities and compensation had fundamentally and substantially increased over the course of his employment. As such, the Court found that “the substratum of his [2005] contract of employment disappeared and implicated the changed substratum doctrine which left the notice terms in his contract no longer enforceable.”

Notably, the changes in the “substratum” that made the contract unenforceable included:

- Significant changes to the employee’s role under the direction of a new CEO, even though he maintained the same title; and
- A significant increase to the employee’s compensation by way of a new bonus structure, that increased his total remuneration about 173% over the course of his employment.

Regarding the new bonus structure, the Court of Appeal took note that the parties had not mentioned or ratified the 2005 employment contract when the new bonus structure was agreed to.

Key Takeaways for Employers

This case serves as an important reminder to employers to include a clause in every employment contract that states its provisions, (including its termination provisions), continue to apply even if the employee’s position, responsibilities, salary or benefits change. Employers

should also make sure employees ratify their original employment termination provisions each time their responsibilities or compensation change substantially.

The Court of Appeal summarized these key takeaways in paragraph 35:

“The written employment contract may oust the application of the changed substratum doctrine if it expressly provides that its provisions, including its termination provisions, continue to apply even if the employee’s position, responsibilities, salary or benefits change [...] The written employment contract may also have continuing force even if there have been substantial changes in the employee’s duties if the parties ratified its continued applicability when those changes occurred.”

Employers are well advised to review and refresh their contracts anytime there is a significant change to an employee’s position, duties and responsibilities, or compensation, to mitigate against the risk that the termination provisions in their employment contract will not be enforced.

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