INDEPENDENT CONTRACTORS

Independent Contractor/Agency Agreements: Is There a Minimum Notice of Termination Requirement?

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Introduction

The traditional workplace is in flux.

Long-term or "permanent" employment is being replaced increasingly by various contingent arrangements including "independent contractor" or "agency" services.

Businesses may seek to retain the services of workers in a capacity other than employment for several reasons:

- core staff can be supplemented on a short-term basis to address fluctuating business needs (e.g., in a pregnancy or other temporary leave of absence);
- specialized skills and expertise not available within the regular workforce can be readily obtained;
- the engagement can be used as a low-risk test period to determine suitability for longer-term employment;
- there is a cost reduction in direct employee benefits (e.g., pension, insurance) as well as related staffing expenses (e.g., payroll taxes).

An independent contractor/agency arrangement is traditionally seen as a commercial bargain, the terms and conditions of which are subject to negotiation between the parties and fully enforceable by the courts. This is in contrast to the status of being employed which is not a straightforward commercial relationship; instead, as the Supreme Court of Canada has reaffirmed: "a person's employment is an essential component of his or her sense of identity, self-worth and emotional well-being."[1]

Employees in Canada cannot be employed on an "at will" basis. In the event that an employer wishes to terminate employment without just cause – a very high standard – the employer is required to provide "reasonable notice" of termination or payment in lieu thereof, commonly known as severance. This is a term legally implied into every employment relationship. This right to reasonable notice can be the subject of an express agreement fixing the appropriate notice or payment; however, the right cannot be waived and must, in every case, comply with certain minimum standards set by legislation. If there is no employment contract, then the appropriate reasonable notice is determined on an individual basis based on what is reasonable in the circumstances. The main factors to consider include years of service, compensation, position, status in the corporate hierarchy, reporting arrangements, age, and opportunity to locate alternative employment.

Traditionally, Canadian law has not afforded independent contractors/agents the same right to severance. An independent contractor/agent may be terminated "at will" unless there is a contractual provision to the contrary. Put another way, the presumption is that no notice is required to terminate such an arrangement whether with or without just cause.

A recent decision of the Ontario Superior Court of Justice, *Aqwa v. Centennial Home Renovations Ltd.*,[2] has now blurred the distinction between employees and independent contractors, at least in the context of termination. In *Aqwa*, the Court disregarded the express commercial contract reached between the parties regarding notice of termination, substituting in its place an implied term of "reasonable dealing" akin to the reasonable notice obligation owed when terminating an employee.

[1] *Reference Re Public Service Employee Relations Act*, [1987] 1 S.C.R. 313.
[2] [2001] O.J. No. 3699.

The Facts

The plaintiff, Ron Aqwa, entered into an independent contractor agreement on May 10, 1995 (the "Agency Agreement") with Centennial Home Renovations Ltd. ("Centennial").

Pursuant to the Agency Agreement, Mr. Aqwa was retained as an "independent sales agent." Mr. Aqwa acted as a sales agent, his services comprised of selling products on behalf of Centennial on a commission basis.

Although there was evidence of significant control by Centennial over certain of Mr. Aqwa's selling activities, the Court did not take issue with the level of control exerted, stating:[3]

> That is the way many manufacturers choose to sell their products to the public. Detailed manuals describing the manufacturer's products are printed and the "sales agent" is required to follow the procedures so described. That does not make the agent an employee. On the other hand, the plaintiff conducted himself throughout as an independent contractor. He declared himself for tax purposes as deriving his income from a business and in computing his profit from his business, he deducted all related expenses. His income was totally dependent on his efforts. He received no commissions advance to be applied against the commissions to be earned. He was on his own: he was on his own to sell Centennial windows whenever and wherever he could. In doing so, he organized himself, advertised and promoted himself, and totally expended his personal efforts towards selling Centennial windows.

The Agency Agreement also included an express termination clause:[4]

> [I]t is agreed that either party may terminate this agreement at any time without notice or penalty. And it is further agreed that both the AGENT and the COMPANY are independent entities who mutually agree to the terms of this agreement.

On or about December 11, 1996, after about a year-and-a-half after the Agency Agreement was signed, Centennial gave notice to Mr. Aqwa that it was terminating the Agency Agreement effective immediately. Although there was some suggestion of wrongdoing on the part of Mr. Aqwa, this was not pursued in the judgment and the termination was treated as being without cause.

Notwithstanding the express termination clause in the Agency Agreement, Mr. Aqwa claimed damages for wrongful dismissal. He asserted that the "true relationship between the parties" was in substance one of employment and not an independent contractor relationship at all. Mr. Aqwa also maintained that the Agency Agreement and its significance (presumably with special reference to the "no notice" termination provision contained in it) were not fully explained to him at the time that the contract was signed.

The Judgment

The Court rejected Mr. Aqwa's contention that the Agency Agreement was not properly explained to him. On the contrary, the Court determined that Mr. Aqwa "well understood that he was not being hired as an 'employee'."[5] As a result of the express terms of the Agency Agreement, the acknowledgment of Mr. Aqwa and the manner in which he carried on his sales agency services, the Court concluded that Mr. Aqwa was not an employee but rather an independent contractor/ agent as set out in the Agency Agreement.

This conclusion, coupled with the express termination provision in the Agency Agreement, should have resulted in a dismissal of the action. As acknowledged by the Court itself, "[b]ased on that finding the plaintiff's claim for damages for wrongful dismissal would necessarily have to be dismissed."[6]

Mr. Aqwa's claim for wrongful dismissal damages was not, however, dismissed. Instead, Mr. Justice Sheppard of the Ontario Superior Court of Justice reached a novel and somewhat extraordinary conclusion.

The Court first reviewed a trilogy of employment cases decided by the Supreme Court of Canada: *Machtinger v. HOJ Industries Ltd.*,[7] *Wallace v. United Grain Growers Ltd.*,[8] and *McKinley v. B.C. Tel.*[9]

[3] Ibid. at paragraph 14.
[4] Ibid. at paragraph 5.
[5] Ibid. at paragraph 5.
[6] Ibid. at paragraph 2.
[7] [1992] 1 S.C.R. 986.
[8] [1997] 3 S.C.R. 701.
[9] [2001] S.C.R. 38.

Acknowledging that the Supreme Court of Canada's judgments were rendered in the context of a traditional employer/employee rather than the independent contractor/agency relationship, Mr. Justice Sheppard in *Aqwa* detected an inherent "judicial attitude." This judicial attitude assumes that all employment-like relationships are premised on unequal bargaining power, with employees or contractors being a particularly "vulnerable group in society" requiring protection especially at the time of termination.[10] After all, as he noted, the effect on Mr. Aqwa of a termination was likely the same as on any terminated employee; that is, he was "instantly cut-off from earning income."[11]

As a guiding principle, Mr. Justice Sheppard adopted this statement from the Supreme Court of Canada in *Wallace*:

> I fail to see how it can be onerous to treat people fairly, reasonably, and decently at a time of trauma and despair. In my view, the reasonable person would expect such treatment. So should the law.[12]

From this starting point and notwithstanding that Mr. Aqwa was an independent contractor working under an Agency Agreement with an express termination provision (which he fully understood), the Court concluded that the relationship between the parties was so "closely connected to or akin to an employment relationship" that Mr. Aqwa "was entitled to an award of damages to reflect the special nature of the contractual relationship between the parties and the breach of that relationship."[13] As a result, reasonable notice of any termination must be "read into" every such independent contractor/agency contract as a matter of "fairness." Accordingly, the Agency Agreement's express termination clause would have to be ignored as inherently unfair, unreasonable and legally unenforceable.

The Court determined that its role was:

> to read into [the] contract the provision which the parties, had they been in an equally informed bargaining position, would likely have included themselves in order to bring a degree of fairness to the relationship.[14]

As a result, "the law [would] imply a term of reasonable notice or, in this case, reasonable dealing."[15]

In determining the appropriate severance, Mr. Justice Sheppard reviewed various factors including: Mr. Aqwa had not invested significant capital; Mr. Aqwa worked on his own with no employees; Mr. Aqwa was likely to become engaged as a sales agent with another manufacturer in due course; the parties had agreed to an independent contractor relationship from the outset and not an employer-employee relationship and (ironically) "the court should accept what parties to an agreement have agreed to."[16]

In the end, the Court purported to award damages lower than what an employee would have received, fixing damages at five months compensation.

Analysis

The Court's reasoning in *Aqwa* is highly suspect and the decision will not likely be followed. Some points to consider:

- If the rationale of the Court was that Mr. Aqwa's relationship with Centennial was more like an employer-employee relationship than a true independent contractor/agency arrangement, then that should have been the Court's determination. If so, the "no notice" termination provision in the Agency Agreement would be unenforceable as falling below the minimum requirements set by the *Employment Standards Act* (Ontario) with the result that reasonable notice should have been provided in accordance with the Supreme Court of Canada's *Machtinger* decision.
- The Supreme Court of Canada trilogy relied on by the Court expressly recognized that employment contracts are enforceable so long as they comply with minimum statutory requirements for notice of termination/severance. Unlike the case with employees, there is no statutory

[10] *Aqwa v. Centennial Home Renovations*, supra note 2 at paragraph 10.
[11] Ibid. at paragraph 14.
[12] *Wallace v. United Grain Growers*, supra note 8 at 746.
[13] Supra note 2 at paragraph 2.
[14] Ibid. at paragraph 6.
[15] Ibid.
[16] Ibid. at paragraph 3.

minimum termination requirement for independent contractors/agents; rather, severance (if any) is a matter solely for negotiation between the parties. Absent factors such as unconscionability, duress, lack of consideration, etc., an agreement regarding termination will be enforced. The Supreme Court of Canada has never authorized wholesale revisions of employment (or other) contracts so as to achieve what courts might consider to be objectively "fair."

- *Aqwa* implies that an employer can never terminate a relationship other than by providing reasonable notice. This principle is not absolute. As stated by the Supreme Court of Canada in *Machtinger*, reasonable notice is only a presumption which is "rebuttable if the contract of employment clearly specifies some other period of notice, whether expressly or impliedly."[17] Put another way, reasonable notice is required unless there is "express contractual language to the contrary "given that the goal is "to ascertain the intention of the parties"."[18] This is so whether the relationship is one of employment, independent contract/agency, or some "intermediate" status. In *Aqwa*, there was such an express contractual provision. The effect of the Court's decision in *Aqwa* is to deprive the parties of the right to negotiate and agree on a contractual notice provision regarding severance – a matter expressly permitted by the Supreme Court of Canada.
- Termination provisions have economic consequences. In the context of a freely negotiated commercial agreement as a whole, a clause providing less (or more) severance may have an impact on other components of the agreement (compensation, restrictive covenants, etc.). Notwithstanding the supposed objective of "fairness," judicial intermeddling into completed commercial transactions creates significant uncertainty and potential unfairness.
- The references to the Supreme Court of Canada's decisions in *Wallace* and *McKinley* are misplaced. Neither of those cases involved contractual severance provisions, but rather employers' rather harsh conduct to their long-standing workers in denying the severance to which those employees were legally entitled. In contrast, there does not appear to be any indication of "bad faith" termination by Centennial of Mr. Aqwa. The worst that could be said of Centennial was that it sought to rely on a contractual term freely negotiated and well-understood by the parties to the agreement (and which, until *Aqwa*, should have been fully enforceable in accordance with Canadian legal principles).
- As previously explained, the Supreme Court of Canada trilogy is premised on a certain power dynamic:[19]

> The terms of the employment contract rarely result from an exercise in free bargaining power in the way that the paradigm commercial exchange between two traders does.

That is, there is an inherent imbalance of power justifying judicial and legislative intervention in order to protect employees. Even if this assumption were true in all employment situations (which is doubtful), there appears to have been no evidence put before the Court in *Aqwa* to justify its application to a more independent arrangement. *Aqwa* is significant in that it implies that independent contractor arrangements are, like employment relationships, not ordinarily a result of free bargaining power and do not reflect true "commercial exchanges."

Conclusion

Even though *Aqwa* is probably wrong, there are important lessons to be learned from the decision.

Firstly, there are significant risks associated with attempting to characterize what is, in essence, an employment relationship, as that of an "independent contractor/agent." In addition to the wrongful dismissal damages at issue in *Aqwa*, there are myriad other employment-related obligations which could arise including: statutory termination pay/ severance pay; reinstatement rights subsequent to maternity/parental leave; workers' compensation/occupational health and safety liabilities; tax withholding obligations. Courts will

[17] *Machtinger v. HOJ*, supra note 7 at 998.
[18] *Carter v. Bell & Sons (Canada) Ltd.*, [1936] O.R. 290 (C.A.), at 297-98.
[19] See, e.g., *Wallace*, supra note 8 at 740-41.

scrutinize any arrangement which may have the effect of depriving individuals (or society) of protections taken for granted by employees.

Secondly, courts tend to view as patently unfair the traditional Canadian legal principles that an independent contractor/agency agreement can be terminated "at will" without notice. Even express and unambiguous contracts to this effect will be viewed with skepticism. In order to avoid this appearance of unfairness, some advance notice of termination/"severance" should be incorporated even in a true independent contractor/agency agreement. Absent just cause, a minimum 30- or 60-day notice termination provision would be recommended.

Finally, regardless of the nature of the relationship of the status of the parties – employee or independent contractor/agent – a business must treat its workers honestly and with decency throughout the relationship and continuing even through the termination process. If there is some evidence of a lack of "good faith" or "fair dealing," courts will be inclined to intervene with a view to remedying any perceived imbalance.