

**UNTANGLING THE INTERSECTION OF DISABILITY AND EMPLOYMENT:
Offsets against Damages and Disability Benefits with Respect
to Current and Terminated Disabled Employees
by Arleen Huggins and Danielle Gauer¹**

Work is one of the most fundamental aspects in a person's life, providing the individual with a means of financial support and, as importantly, a contributory role in society. A person's employment is an essential component of his or her sense of identity, self-worth and emotional well-being. For most people, work is one of the defining features of their lives. Accordingly, any change in a person's employment status is bound to have far-reaching repercussions. –Wallace v. United Grain Growers Ltd. [1997] 3 S.C.R. 701

As the Supreme Court of Canada illustrates in the above extract from *Wallace v. United Grain Growers Ltd.*, work continues to be an integral part of our everyday lives. Thus becoming seriously ill or disabled can have a devastating impact upon an individual employee. While a disabled employee can be a significant disruption for the employer and its business, for employees, becoming temporarily or permanently disabled can result in devastating financial hardship and lead to serious emotional stress. Understanding what benefits a disabled employee is entitled to, while employed and even after termination, is extremely important. However, navigating this area of law can be quite challenging.

The following paper will provide a discussion on the availability of income replacement benefits to employees who become temporarily or permanently disabled. In addition, this paper will look at the interplay between employees with disability claims and the offsets against those benefits, before and following a termination.

This paper shall not however discuss the interface between disability benefits and collateral benefits in the context of a motor vehicle accident as that shall be canvassed by another panelist.

I. STD and LTD Benefits

The *Employment Standards Act, 2000* (“ESA”)² provides a “floor of rights” entitling the individual employee to certain inalienable fundamental benefits which must be guaranteed in the workplace. With respect to illness or disability, the *ESA* allows an employee who works for an employer who employs 50 or more employees to take personal emergency leave, without pay, to a maximum of 10 days per year.³ However, the *ESA* does not provide the same entitlement to employees who are or become disabled while working for employers of fewer than 50 employees. In this respect, the *ESA* is narrower in scope than the Ontario *Human Rights Code*

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² *Employment Standards Act, 2000* S.O. 2000, Ch. 41

³ *Employment Standards Act, 2000* S.O. 2000, s.50.

(“the *Code*”) which requires employers to accommodate absences resulting from disability irrespective of how large the workplace is.⁴

However, neither the *ESA* or the *Code* provide a compensation scheme for absences due to disability and the employee must look for compensation through their own private insurance or through an employer’s group disability policy. Such compensation is based upon a contractual agreement between the employee and the insurance benefit provider directly (through a private disability policy) or indirectly (between the employee as beneficiary to an employer’s group disability policy and the insurance benefit provider).

General principles of contract law apply to the interpretation and application of a disability policy, with any ambiguity in respect thereof being interpreted against the policy insurer.⁵

Short term disability (STD) and long-term disability (LTD) benefits provide partial income replacement to an employee who becomes either temporarily or permanently disabled on the job and incapable of working due to illness or injury.

STD and LTD benefits are customarily integrated with one another, in that LTD benefits only begin once STD benefits expire. An injured or disabled employee will generally only be entitled to these benefits after a specified qualifying period. An employee claiming these benefits must demonstrate an inability to perform occupational duties or a loss of earnings by virtue of disability. While most such policies require total disability, there are policies which provide benefits for partial disability under certain conditions.

Not only is it critical for an injured or disabled employee to understand when they will be entitled to disability benefits, but understanding how these benefits relate to other benefits that may be available is essential.

Offsets and STD/LTD Benefits

In order for an insurer to reduce or eliminate the amount of LTD benefits payable to an employee, insurance contracts will incorporate direct or indirect offset provisions or provisions in respect of an integration of benefits. These direct offsets or indirect “all source” provisions are intended to ensure that the disabled employee is not receiving compensation from various sources which amount to more than the employee’s pre disability income. Generally, to ensure that the employee is not overcompensated, the amount of expected disability benefits will be reduced by offsetting other sources of income replacement received by the employee.

The courts have agreed that it is not contrary to public policy to reduce disability benefits by offsetting it with other sources of income support, because otherwise the cost of private insurance would likely increase, making it less affordable.⁶

⁴ *Human Rights Code*, R.S.O. 1990, Ch. H.19.

⁵ *Brisette Estate v. Westbury Life Insurance Company*, [1992] 3 S.C.R. 87 at 92-93

⁶ *Ruffolo v. Sun Life Assurance Co. of Canada* [2007] O.J. No. 4541 per Perell J. at para. 118, leave to appeal to SCC refused, [2009] S.C.C.A. No. 226.

Where a disabled claimant has access to other benefit sources, such as pursuant to the Canada Pension Plan (CPP) and the Workplace Safety and Insurance Board (WSIB), it is important to understand how they interrelate with the claimant's disability benefits. Each of these offsets will be discussed below.

(i) CPP Disability Benefits

The purpose of CPP disability benefits is to provide replacement income for contributors with prolonged disability. Whether CPP disability benefits should offset a claimant's LTD benefits was considered by the Ontario Superior Court of Justice in *Perreault v. Manufacturers Life Insurance Co.* [2006] O.J. No. 2613 (S.C.J.). The plaintiff, an employee of Abitibi Consolidated Inc., brought an action against his insurer for an order for payment of LTD benefits equal to 55% of his pre-disability income. Pursuant to a Collective Agreement, Manulife agreed to provide group LTD benefits for Abitibi employees to the extent of 55% of pre-disability earnings. The offset provision in the policy stated that, "an insured employee's benefit will be reduced by income payable...from the Canada/Quebec Pension Plan." The language of the provision stipulated that once CPP disability benefits are payable to a disabled employee they are offset against the LTD benefit payable by the insurer. The employee argued that CPP disability benefits are only to be offset against Manulife's LTD benefits if the total of the CPP disability benefits and the LTD benefits is greater than 85% of the employee's pre-disability income; 85% being the amount of the "all source" limitation. The employee submitted that only where the income from all sources exceeds 85% of pre-disability income can Manulife pay less than 55% of pre-disability income. Since the Manulife LTD benefits plus the CPP disability benefits totalled 76% of the employee's pre-disability income, the employee stated that there should be no reduction in the LTD benefits.

Although Shaw J. agreed that the purpose of the policy is that the disabled employee will never receive less than 55% of his or her pre-disability income in the event of disability, he held that the amount is to be reduced by any base CPP disability benefit. The plaintiff was not entitled to a combined LTD and CPP benefit that would total 85% of his pre-disability income. Justice Shaw also concluded that the offset provision provided that if the employee receives income from CPP payable retroactively, the disability benefit payments will be adjusted by the insurer to reflect any overpayment that would have been made.

Another issue is the interplay between LTD benefit payments and CPP dependent benefits payable to an insured's children. The issue of whether an insurer is permitted to deduct CPP disability benefits paid to dependent children of the insured from LTD benefits paid to the insured was clarified by the Court of Appeal in *Ruffolo et al. v. Sun Life Assurance Company of Canada*, [2009] O.J. No. 1322 (C.A.).

In this case, the plaintiffs, who were both totally and permanently disabled, were covered under group insurance policies with Sun Life that provided for LTD benefits. They both had minor children at the time. In addition to receiving LTD benefits under Sun Life's group insurance policy, they also received disability benefits for their dependent children under CPP. The plaintiffs commenced the action asserting that it was improper for Sun Life to off-set their children's CPP benefits from their own LTD benefits. Sun Life responded by contending that it

was entitled by the terms of the policy to deduct the CPP Child Benefit from the amounts payable by it to the plaintiffs under its group insurance policies.

The Court of Appeal agreed with the trial judge that the language of the policy clearly permitted Sun Life to “set-off” CPP Child Benefits from the plaintiffs’ monthly LTD payments, and stated in its reasoning that: “even though the CPP Child Benefits are not ‘disability income to which the disabled member is entitled’ in a proprietary legal sense, the payments are made to the disabled parent in trust. The disabled parent is entitled to receive them in that sense, which is sufficient under the terms of the policy.”⁷

(ii) CPP Early Retirement Benefits

Prior to the amendments to the *Canada Pension Plan*, R.S.C. 1985, c. C-8 in 2009 (the “CPP”), an individual who wanted to take his or her CPP retirement pension before age 65 was required to provide proof that he or she had substantially or wholly ceased working or significantly reduced their earnings (formerly section 68.1). Pursuant to the amended legislation, which became effective in 2012, the CPP (section 67(3.1)) now permits individuals to take a permanently reduced CPP retirement pension as early as age 60 or to take a permanently increased pension after age 65. The goal is to provide more flexibility to individuals to transition to retirement by enabling individuals to receive CPP retirement benefits while continuing to work.

But what happens when an employee, while receiving CPP retirement benefits, subsequently becomes disabled? In light of the recent amendments to the federal legislation, an issue arises as to whether disability benefits should be offset by the CPP retirement benefits received by an individual claimant prior to becoming disabled. There appears to be no case law yet on this issue however arguably, it would be inconsistent with the purpose of the recent changes to the CPP to reduce disability benefits by CPP retirement benefits which commenced prior to becoming disabled and which continued post disability. Further, to do so would inappropriately penalize those individuals who elected to receive CPP retirement benefits early at age 60.

(iii) WSIB

In order to be eligible for loss of earnings pursuant to section 43(1) of the *WSIA* the employer must be covered by the *WSIA* and the employee must have undergone an injury or illness “arising out of and in the course of his or her employment.” This benefit is administered and paid for by the WSIB.

In general, pursuant to the terms of the LTD policy, any LTD benefits received by the insured will be reduced by any payment received from the WSIB representing loss of income benefits.

The Courts have determined that this is the case even when the employee could have received WSIB loss of income benefits but elects to forego them in favour of a civil suit.

⁷ *Ruffolo et al. v. Sun Life Assurance Company of Canada*, [2009] O.J. No. 1322 (C.A.) at para. 16.

Specifically, in *Richer v. Manulife Financial et al.* (2007), 85 O.R. (3d) 598 (C.A.) the Court of Appeal considered whether after electing to proceed with a civil tort action pursuant to sections 30(2), (4) and (5) of the *WSIA*, the plaintiff was still eligible to receive the LTD benefit payable under the Manulife policy; and if so, would the LTD benefit be subject to an offset for the amount of the WSIB benefits he would have received had he not elected to proceed with a civil tort action.

In this case, during the course of his employment, the plaintiff sustained injuries as a result of a motor vehicle accident. A provision in the disability insurance plan stipulated that in order to be eligible to receive benefits pursuant to the plan, the insured was required to apply for workers' compensation disability benefits. The amount of the monthly LTD benefits was to be reduced by any payment received under the WSIB scheme. After filing an application with the WSIB for benefits, he was advised that he could elect to proceed with a civil tort action against the third party responsible for his injuries pursuant to sections 30(2), (4) and (5) of the *WSIA*. The employee elected to proceed with the civil action against the third party.

The motions judge decided that the plaintiff was not entitled to receive any LTD benefits and that the question of offset did not need to be answered. The Court of Appeal reversed the motions judge, holding that the plaintiff was still entitled to receive LTD benefits under the policy after electing to proceed with the civil action. However, the LTD insurer was entitled to reduce the insured's monthly LTD benefits payable under the policy by the amount of WSIB benefits to which the employee would have been entitled to receive had he not elected to proceed with the civil action against the third party.

The Court of Appeal's decision in *Richer* contradicts *Abdulrahim v. Manufacturers Life Insurance Co.* [2003] O.J. No. 2592 (S.C.J.), an earlier decision of the Ontario Superior Court of Justice. In that case, Himel J. held that once the insured elected to proceed with a civil tort action the insurer could not offset the WSIB benefits that would have been received had the employee elected to proceed under the statutory regime against LTD benefits that the employee was entitled to receive under the group policy.

A question also arises as to what happens to the insured's LTD benefits when he or she is initially denied benefits by WSIB, but later successfully appeals that decision. This issue was recently addressed in *RBC Life Insurance Co. v. Janson*, 2013 ONSC 3154 (S.C.J.), where the Ontario Superior Court of Justice confirmed that where an employee's statutory WSIB claims are initially denied but the appeal is later accepted, the insurer is entitled to recover any overpayments, on a gross basis, and can require the insured to reimburse the insurer for that amount.

(iv) Employment termination income

As mentioned above, it is important to look at the direct offset or all source limitation provision under an insurance benefit provider's policy to understand which sources of income replacement received by the employee will be offset against LTD benefits. Whether termination pay, severance pay, or amounts in lieu of notice paid by the employer will be deducted from LTD benefits depends on the wording in the policy.

The case law has signaled that absent specific wording in the policy language, statutory severance payments and statutory termination payments will not be deducted from disability benefits as they are treated as compensation for past service. In other words, it is argued that both statutory severance pay and statutory termination pay are not synonymous to salary continuation.

The Court of Appeal has considered this issue in a number of cases and has consistently rejected the argument that statutory severance pay should be deductible from LTD benefits.

In *Sills v. Children's Aid Society of Belleville* [2001] O.J. No. 1577 (C.A.), the plaintiff was given 14.5 months working notice of termination due to an organizational restructuring. She was promised an additional 3.4 months of statutory severance pay on termination for a total of 17.9 months. Within two months of receiving notice, she suffered a disabling depression and as a result was unable to work during the balance of the working notice period. The employer did not pay her any salary from when she stopped working, but she did receive STD payments from the employer's group insurance provider equivalent to 66 percent of her salary. She applied for LTD, but her claim was not processed immediately. At trial, she was awarded 16 months in wrongful dismissal damages and statutory severance pay of 3.4 months, totalling 19.4 months.

In dismissing the employer's appeal and upholding the trial decision, the Court of Appeal disagreed that *Sylvester*⁸ stands for the proposition that "an employer is relieved of its obligation to pay damages for wrongful dismissal by virtue of the existence of a disability plan"⁹. The Court of Appeal stated that *Sylvester* "merely provides that disability benefits are deductible from the damages payable in certain circumstances."¹⁰ The Court held that there was no evidence that the parties did not intend employees to be entitled to both damages and disability benefits and that the plaintiff had contributed to the benefits indirectly as "part of a trade-off in arriving at benefits and salary."¹¹ Justice Simmons stated the following:

I consider it reasonable to assume that an employee would not willingly negotiate and pay for a benefit that would allow her employer to avoid responsibility for a wrongful act. I consider it reasonable to infer that parties would agree that an employee would retain disability benefits in addition to damages for wrongful dismissal where the employee has effectively paid for the benefits in question.¹²

In the Court of Appeal decision of *O.N.A. v. Mount Sinai Hospital*, [2005] O.J. No. 1739 (C.A.), the hospital was ordered to pay statutory severance pay under the former *ESA*, despite the employee receiving disability benefits under the group policy.

The employee worked as a neonatal intensive care nurse with the hospital for 13 years before being dismissed due to innocent absenteeism. Since her employment contract had been frustrated as a result of her disability, the employer did not pay her notice of termination or severance pay

⁸ *Sylvester v. British Columbia* [1997] S.C.J. No. 58 (S.C.C.).

⁹ *Sills v. Children's Aid Society of Belleville* [2001] O.J. No. 1577 (C.A.) at para. 26.

¹⁰ *Sills v. Children's Aid Society of Belleville* [2001] O.J. No. 1577 (C.A.) at para. 26.

¹¹ *Sills v. Children's Aid Society of Belleville* [2001] O.J. No. 1577 (C.A.) at para. 41.

¹² *Sills v. Children's Aid Society of Belleville* [2001] O.J. No. 1577 (C.A.) at para. 45.

upon termination. The Court of Appeal considered the issue of whether former section 58(5)(c) of the *ESA*, which created an exception to an employer's obligation to provide statutory severance pay to employees whose employment had been frustrated, was constitutional.¹³

Both parties made arguments with respect to the dominant purpose of severance pay. The hospital's argument hinged on the purpose of severance pay being "directed toward compensating employees for capital losses going forward as they find new employment."¹⁴ The hospital further argued that it was due to the fact that those employees whose contracts have been frustrated due to disability are "unlikely to re-enter the workforce that denying them severance pay was not discriminatory."¹⁵ By contrast, the O.N.A. contended that severance pay is retrospective and is therefore "intended to compensate long-serving employees for their years of service and investment in the employer's business."¹⁶

In its analysis the Divisional Court looked at the legislative background of the section. When subsection 58(5)(c) was originally enacted, it made clear that those employees who were temporarily absent due to illness or injury at the time of plant closure were entitled to severance pay. It was only when the section was broadened in 1987 to include frustration generally that employees whose contracts were terminated by reason of disability were disentitled from receiving a benefit to which they otherwise would be entitled. The Court found the subsection to be unconstitutional. It stated the following:

Legislative history, together with relevant jurisprudence, make it clear that severance pay (in contrast to termination pay in lieu of notice) is an earned benefit that compensates long-serving employees for their past services and for their investment in the employer's business. It is properly payable for any non-culpable cessation of employment.¹⁷

The Divisional Court also held that the distinction drawn by subsection former 58(5)(c) of the *ESA* imposed a disadvantage on a disabled person in a manner that constitutes discrimination under section 15(1) of the Charter.

In dismissing the appeal, the Court of Appeal held that severance payments serve to compensate employees for years of service, unless terminated for cause, and to assist terminated employees with re-entrance to the workforce. The Court of Appeal made the following comment:

To the extent that severance pay is intended to ease the transition of terminated employees to other employment, the need of disabled employees for support in retraining and the acquisition of new skills may be even more pressing than that of other terminated employees. Denying them the benefit of severance pay

¹³ The former Act was repealed effective September 4, 2001, and replaced with the *Employment Standards Act*, 2000. Severance pay is now provided for in section 64 of the new statute and the exclusions and exceptions to termination pay and severance pay are found in O.Reg. 288/01.

¹⁴ *O.N.A. v. Mount Sinai Hospital*, [2005] O.J. No. 1739 (C.A.) at para. 12

¹⁵ *Ibid.*

¹⁶ *O.N.A. v. Mount Sinai Hospital*, [2005] O.J. No. 1739 (C.A.) at para. 13.

¹⁷ *O.N.A. v. Mount Sinai Hospital*, [2005] O.J. No. 1739 (C.A.) at para. 14.

therefore does not further the objective of severance pay identified by Attorney General. To the contrary, it frustrates it.¹⁸

Pursuant to sections 2(1)(4) and 9(1)(2) of the current *ESA*, O.Reg 288/01, employees are not entitled to statutory notice of termination or termination pay or statutory severance pay where the employment contract has been frustrated or impossible to perform by a fortuitous or unforeseeable event or circumstance. However, there is now a specific exception in *ESA* O. Reg. 288/01 with respect to an employee whose contract is frustrated due to disability or serious illness. Pursuant to sections 2(3) and 9(2)(b), an employee whose contract is frustrated as a result of an unforeseen event are still entitled to receive termination pay and severance pay under the *ESA*. This change was made as a result of the *O.N.A. v. Mount Sinai Hospital* decision.

(v) Other Offsets

Although WSIB and CPP are the typical income replacement benefits that will be included in the offset provision of an LTD policy, it is critical to pay close attention to the language of the insurance policy to know what other sources of income will offset the amount of disability benefits. Other offsets can include proceeds from third party claims which typically means any claim against a third party for past and future wage loss arising from events that caused the disability.

II. Wrongful Dismissal Damages

Where an employer wishes to terminate an employee without cause, the employer is required to give reasonable notice of termination to the employee. When the employer fails to provide notice or compensation in lieu of notice, the employee can bring a claim for wrongful dismissal claiming compensation. The idea is that wrongful dismissal damages will put the employee in the same financial position he or she would have been in had they been allowed to continue working over the reasonable notice period. Reasonable notice is an implied term and the amount of wrongful dismissal damages will be determined on a case by case basis in accordance with a number of factors, including but not limited to the length of service, the age of the employee, the employee's level of compensation and the employee's character of employment. At a minimum, an employer must provide statutory notice or termination pay and statutory severance pay as per the *ESA*.

It is important for both employees and employers to understand the relationship between wrongful dismissal damages and other income replacement benefits. In particular, it is critical to consider whether these benefits will be offset against the amount of wrongful dismissal damages.

¹⁸ *O.N.A. v. Mount Sinai Hospital*, [2005] O.J. No. 1739 (C.A.) at para. 38.

Offsets and Wrongful Dismissal Damages

(i) STD and LTD Benefits

It is clear that while an employee is employed and subject to the employer's group disability policy, the employee is entitled to the compensation provided for in the disability policy as long as eligibility and other threshold requirements are met. It is also clear that pursuant to section 60(1)(a) and (c) of the *ESA*, an employer of a terminated employee under the jurisdiction of the *ESA* is entitled to the same policy protection during the statutory notice period by virtue of the employer's obligation to maintain all terms and conditions of employment, including all policies, through to the end of the statutory notice period provided for in the *ESA*.

However, the interplay between disability benefits and wrongful dismissal damages becomes quite complex when an employee becomes disabled *after* the statutory notice period when the disability policy coverage comes to an end.

Until *Egan v. Alcatel*, [2006] O.J. No. 34 (C.A.), the issue of whether an employer should be responsible for disability payments during the common law notice period was never fully canvassed by the Court of Appeal. In *Pioro v. Calian Technology Services Ltd.* (2000) 48 O.R. (3d) 275 (S.C.J.), the Ontario Superior Court of Justice considered what an employer was obliged to do when an employee becomes disabled during the notice period. In this case the plaintiff's benefits package had LTD insurance coverage and group life insurance coverage. Pursuant to the terms of the policy, both the LTD coverage and group life insurance coverage ended when the insured's employment was terminated. Shortly after his termination, the plaintiff experienced chest pains and was diagnosed as having myocardial ischemia and unstable angina. According to his physician, his prognosis was poor and it was highly unlikely that he would be able to maintain any employment. The employee sued for wrongful dismissal and claimed an entitlement to LTD benefits on the basis that he became totally disabled during the reasonable notice period.

The Court found that the reasonable notice period was 22 months. The court stated that there was no obligation for the employer to provide *actual* work to the employee. It could instead keep the employee on the payroll for the purpose of being employed. However, due to a plant closure, even the latter would not have been possible and as a result, under the terms of the disability policy, the employee would not have been entitled to LTD coverage. This case is unique because of the fact that the plant closed and therefore there was no work to be given to keep the LTD coverage intact. As per the language of the policy, the employee therefore had no claim against the employer for disability benefits.

In *Egan*, after a period of employment of less than 21 months, the plaintiff was dismissed and given 12 weeks' salary in accordance with the *ESA*. The employer advised that the plaintiff would be covered for group insurance benefits, including STD and LTD benefits, until the end of the statutory notice period. The employer discontinued the plaintiff's insurance coverage at the end of the 2 week *ESA* period. The plaintiff became ill 12 weeks after the termination.

The plaintiff sued the employer for wrongful dismissal and claimed losses incurred as a result of its failure to maintain her disability insurance throughout the reasonable common law notice period. At trial she was awarded 9 months' notice, but was not awarded any damages for loss of disability benefits.

On appeal, the Court of Appeal found ample support for the trial judge's finding of fact, stating that reasonable notice and disability payments cannot be awarded at the same time because doing so would amount to double recovery. However, the Court of Appeal held that the employee was entitled to receive notice and then thereafter, damages for loss of disability benefits commencing from the date of disability. Thus the employer was ordered to pay the plaintiff's salary in lieu of notice for 13 weeks, damages in lieu of STD benefits for the next four months, and damages in lieu of LTD benefits for the remainder of the period that the plaintiff was disabled. In this case the employee recovered within the 9 month notice period. The damages were to be "grossed-up" to ensure that the plaintiff would receive the damages in lieu of the LTD and STD payments tax free.¹⁹

The Court stated that "where an employee would otherwise have qualified for disability benefits during the reasonable notice period, but the application is denied on the basis that coverage was wrongfully discontinued by the employer, the employer must be liable for the value of the disability benefits that would otherwise have been payable."²⁰

There is no real discussion in the decision, but query whether the employer could have continued the disability coverage even if it had wanted to do so as the plaintiff was no longer actively employed at the time and customarily, LTD policies require active employment to be eligible for policy coverage. Given that generally insurers will refuse to provide such coverage, at least unless special underwriting arrangements are specifically made, it would appear that the only way an employer can protect against the *Egan* decision, short of a Full and Final Release being obtained, is to clearly specify in the initial employment contract that the employee agrees that disability coverage shall end after the statutory notice period, following termination of employment and that the employer is not liable for any disability benefits or any payment or damages in lieu of such benefits.

More recently, the Court of Appeal in *Brito v. Canac Kitchens* [2012] O.J. No. 376 (C.A.) shed further light on this issue by revisiting the question as to what an employer's obligation is when a terminated employee becomes disabled beyond the statutory notice period but during the common law notice period. In this case, the plaintiff was terminated as a result of business restructuring. After the eight week statutory notice period, the plaintiff's disability coverage was terminated. Sixteen months after his dismissal from the employer, the plaintiff was diagnosed with cancer for which he underwent a number of surgeries. The plaintiff brought an action against the employer for damages for wrongful dismissal and associated benefits, including STD and LTD benefits.

¹⁹ Payments from an insurance company are not taxable when the employee pays the premiums for coverage whereas damages for wrongful dismissal paid by the employer to an employee are taxable.

²⁰ *Egan v. Alcatel*, [2006] O.J. No. 34 (C.A.) at para. 26.

The Court of Appeal agreed with the trial judge that the employer was obligated to compensate the plaintiff for the loss of benefits for the duration of the reasonable common law notice period and found that the plaintiff was “totally disabled” within the meaning of the disability plan. Arguably, had the plaintiff actually been employed with the employer during the reasonable notice period, he would have received benefits until his 65th birthday. As such, the Court upheld the trial judge’s award, with the exception of the punitive damages award. The plaintiff was awarded salary for a notice period of 22 months, \$9,078 in STD benefits, \$2,096 in monthly LTD for two years; being a total of \$146,723 for pre-trial LTD benefits and \$47,941 for post-trial LTD benefits to age 65. In doing so, the Court stated that “[the employer] consciously chose not to make alternative arrangements to provide its loyal, long-service employee with replacement disability coverage. Rather, it chose to go the bare minimum route. It provided only the statutory minimums in pay and benefits and then gambled that he would get another job and stay well.” The employer’s appeal was dismissed.

Employers are cautioned that failure to maintain disability coverage for their employees following expiry of the statutory notice period will put them at risk. In the event of employee disability they will be deemed to step into the shoes of the insurer, and therefore potentially be responsible for disability payments for the duration of the notice period and potentially beyond, until the employee recovers.

In both *Canac* and *Egan* the employee became disabled after the statutory notice period when the disability policy was at an end. But what is an employer’s obligation when an employee is terminated while receiving disability benefit payments?

STD benefits are self-insured benefits generally funded solely by the employer. As such, the employer pays the benefits either through a self-insured plan usually administered by a third party. Therefore, a disabled employee will not be entitled to double recovery by receiving both STD benefits and wrongful dismissal damages. STD benefits are therefore virtually always an offset against wrongful dismissal damages.

The case law is divergent as to when LTD disability benefits paid to disabled employees during the reasonable notice period are deductible from wrongful dismissal damages. The interplay between LTD benefits and wrongful dismissal damages is largely contingent on whether the premiums are paid by the employee rather than the employer.

The Supreme Court of Canada in *Sylvester v. British Columbia* [1997] S.C.J. No. 58 (S.C.C.) held that disability benefits paid to disabled employees during the reasonable notice period are deductible from damages in lieu of notice, provided they are paid pursuant to disability insurance schemes established and paid by employers. The Court’s reasoning was as follows:

If disability benefits are paid in addition to damages for wrongful dismissal, the employee collecting disability benefits receives more compensation than the employee who is dismissed while working. Deducting disability benefits ensures that all affected employees receive equal damages, i.e., the salary the employee would have earned had the employee worked during the notice period. If benefits are not deductible, employers who set up disability plans will be required to pay more to employees upon termination than employers who do not

set up plans. This deterrent to establishing disability benefits plans is not desirable.²¹

The distinguishing feature in this case is the fact that STD and LTD benefits were funded by the employer. The non-contributory disability benefits were to be deducted as the benefits were intended to be an indemnity for lost wages while Mr. Sylvester was unable to work.

Although *Sylvester* is often regarded as the leading case on the issue of deductibility of disability benefits from wrongful dismissal damages, a number of cases have since distinguished it.

In *McNamara v. Alexander Centre Industries Ltd.* [2001] O.J. No. 1574 (C.A.), the Court of Appeal considered the issue of whether an employee who is wrongfully dismissed can retain both damages and disability payments, or if the latter should be deducted from damages for the wrongful dismissal. The Court stated that the resolution of the appeal turned on the application of the principles enunciated by the Supreme Court of Canada in *Sylvester*.

In *McNamara*, the plaintiff was a long-standing employee and had worked for the company for 24 years. He started his employment as the company's controller but was later promoted to Vice-President of Finance, and eventually to President. Due to work related stress, the employee was advised by his doctor to take medical leave. He was terminated shortly after he advised his employer that he required time off work. At no time did the company's CEO ask the plaintiff about his expected return date to work. Although the plaintiff indicated that he was able to return to work after a few weeks, his employer sent him a letter indicating that he understood that for medical reasons he would not be returning to work. The plaintiff sued for wrongful dismissal. At trial, the plaintiff was awarded 24 months' notice. With respect to the disability payments received by the employee during the relevant notice period, the trial judge held that they were not deductible from the damages award. In distinguishing this case and *Sylvester*, the Court of Appeal upheld the trial judge's decision disallowing a deduction. Here, since the employer purchased the plan from a private third party, when the employee was in receipt of benefits, it was not the employer who was paying the employee. Further, the employee was held to have provided consideration for the LTD benefit in that he would not have accepted the salary but for the benefit package as part of the overall compensation scheme.

This issue was further considered by the Ontario Superior Court of Justice in *Dowling v. TNT Logistics North America* [2005] O.J. No. 2091 (S.C.J.) where Speigel J. held that there should be no deduction in the damages for wrongful dismissal as a result of the STD or LTD benefits received. Justice Speigel stated:

There is nothing in the employment contract that would indicate that Dowling cannot receive both employment benefits and LTD benefits...the provisions in the Plan are contractual provisions with the insurer, not with TNT...They are the usual provisions that state that an employee on LTD has his or her benefits reduced if the employee is earning money elsewhere. I do not interpret these provisions to apply to an employee receiving damages for wrongful dismissal;

²¹ *Sylvester v. British Columbia* [1997] S.C.J. No. 58 (S.C.C.) at para. 21.

an insurer under an LTD policy would be hardpressed to deduct these damages.²²

In *Atlman v. Steve's Music Store Inc.*, [2011] O.J. No. 1136 (S.C.J.), Corrick J. held that the LTD benefits received were not to be deducted from the wrongful dismissal damages award since the plaintiff paid the premiums for the LTD insurance and the benefits were paid by Standard Life, not the employer, as was the case in *Sylvester*. Justice Corrick instead followed the reasoning in *Piresferreira v. Ayotte*, [2008] O.J. No. 5187 (S.C.J.), *McNamara v. Alexander Centre Industries Ltd.* [2001] O.J. No. 1574 (C.A.), and the Court of Appeal in *Sills v. Children's Aid Society of the City of Belleville* [2001] O.J. No. 1577 (C.A.). These cases take a different approach to that of *Sylvester* in that disability benefits were not deducted from the damages award.

The jurisprudence appears to illustrate that whether disability benefits will be deducted from a wrongful dismissal damages award will be determined based upon the unique set of facts of each case. Disability payments will not be deductible from a damages award if doing so conflicts with the express terms of the employment contract or if the disability benefit plan is akin to benefits from a private insurance plan. In other words, where an employee has provided consideration in exchange for benefits from a private insurance plan, they may seek LTD disability benefits in addition to damages for wrongful dismissal.

The cases suggest that there will be three particular circumstances wherein *Sylvester* will not apply: 1) if there was evidence that the employee provided consideration for the disability benefits; 2) if it went against the express language of the employment contract; or 3) if the contract was silent and it was determined that the true intentions of the parties would not have been to deduct disability benefits from damages awards. Justice Simmons in *Sills*²³ commented as follows at paras. 45 and 46:

Absent an express provision precluding double recovery, in my view, the principles enunciated in *Cunningham v. Wheeler*, [1994] 1 S.C.R. 359 assist in determining whether an intention that there would be double recovery in the event of a wrongful dismissal can be inferred. I consider it reasonable to assume that an employee would not willingly negotiate and pay for a benefit that would allow her employer to avoid responsibility for a wrongful act. I consider it reasonable to infer that parties would agree that an employee should retain disability benefits in addition to damages for wrongful dismissal where the employee has effectively paid for the benefits in question.

(ii) Retirement Pension Benefits

Unlike disability benefits, the Supreme Court of Canada recently confirmed that the nature and purpose of a retirement pension benefit is distinct from a disability benefit and therefore should not be deducted from a damages award for wrongful dismissal.

²² *Dowling v. TNT Logistics North America* [2005] O.J. No. 2091 (S.C.J.) at para. 13.

²³ *Sills v. Children's Aid Society of the City of Belleville* [2001] O.J. No. 1577 (C.A.)

In *IBM Canada Limited v. Waterman* [2013] S.C.J. No. 70 (S.C.C.), the employee was dismissed without cause at 65 years of age. Upon termination, the employer informed the employee that he would be treated as a retiree and that he must begin receiving monthly pension payments as of that date. The employee sued for wrongful dismissal and was awarded 20 months' notice at trial.

The trial judge and the Court of Appeal rejected the employer's position that the employee's retiree pension benefits should be deducted from the salary and benefits otherwise payable during this period. Justice Cromwell, speaking for the Supreme Court of Canada, explained that *Sylvester* was distinguishable and therefore that the employee's retiree pension benefits should not be deducted.

Justice Cromwell noted that first, the employee's receipt of retiree pension benefits and wrongful dismissal damages was held to not be incompatible with the employment contract, which contemplated that the employee could receive both retiree pension benefits and employment income. There was no general bar found against an employee receiving both retirement pension income and employment income. Second, disability benefits are income replacement where an employee becomes disabled and unable to work. Retiree pension benefits accrue over time and are based on rewarding an employee's past service. This rationale is consistent with the notion that vested pension entitlements are akin to property rights which over time accrue to the benefit the employee.²⁴ Retirement pension benefits are not considered "income replacement" in the same way as disability benefits. Further, disability benefits and wrongful dismissal damages are also based on opposite assumptions about the ability to work. From a policy perspective, the Court in *Sylvester* was concerned that employers would be reluctant to fund wage replacement benefits if an employee already receiving disability benefits before being terminated would also receive in addition a full damages award. This was not seen as a concern in this case.

(iii) WSIB

The SCC's decision in *Sylvester* clarified that if the maintenance of a disability insurance scheme is established and paid for by the employer, those benefits can be offset against wrongful dismissal damages. WSIB income replacement benefits are treated in the same manner in this province in that in Ontario, loss of earnings benefits ("LOE") received from the WSIB are deductible from wrongful dismissal damages.

The issue of the deductibility of WSIB income replacement benefits received by an injured or disabled employee from wrongful dismissal damages evoked much debate amongst practitioners. The argument was that for employers, it would be unfair to be required to pay a disabled employee wrongful dismissal damages and WSIB income replacement benefits, especially since the employer is the sole contributor to this statutory scheme.

In *Jensen v. Schaeffler*, [2011] O.J. No. 1133 (S.C.J.) the plaintiff was terminated after almost 28 years of service. Three years prior to her termination she was injured at work after

²⁴ *IBM Canada Limited v. Waterman* [2013] S.C.J. No. 70 (S.C.C.) at para. 90.

being struck and knocked to the floor by a swinging automated door. As a result, she was unable to work for a period of time. Ms. Jensen was eventually enrolled in the WSIB Labour Market Re-entry Program where she received bi-weekly loss of earnings payments from WSIB.

Ms. Jensen sued for wrongful dismissal and was subsequently awarded 18 months' notice. In considering the treatment of WSIB payments received by the plaintiff during the notice period, Haines J. agreed with the analysis of the Alberta court of Appeal in *Salmi v. Greyfriar Developments Ltd.*, [1985] A.J. No. 1089:

... in determining the actual award in a wrongful dismissal case the court must take into account the earnings of the plaintiff over the period of the award in mitigation of damages. Therefore if the respondent had been fit for work and had earned \$2,400.00 in wages from the Workers' Compensation Board it would have been deducted. The reason the respondent did not attempt to locate other work was his medical condition. In lieu of wages for the period he received workers' compensation provided by assessments paid by his employer and others in like kinds of industry. The fund is set up by legislation. The employer is the only contributor. The payment is in lieu of wages and takes away the right to sue the employer for injury resulting in his present medical condition which makes him unfit for employment for the period involved or for death.

If the money came from earnings from a complete stranger the appellant would have the advantage of it in mitigation of the loss. As a matter of policy I am quite unable to see why it ought not to be deducted where it is paid from a fund contributed to by the employer by force of law particularly where the payment is in lieu of earnings and to compensate for their loss while unable to work because of injury sustained during the course of the respondent's employment.²⁵

The WSIB income replacement benefits were held to be deductible from common law wrongful dismissal damages.

III. Conclusion

As employment law landscape continues to develop and evolve so will the interplay between disability benefits and wrongful dismissal damages payable to disabled employees and the offsets against those payments. As a result it is important to have a comprehensive understanding of how these different benefits and/or entitlements relate to one another while a disabled employee is working and after the disabled employee has been terminated.

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²⁵ *Jensen v. Schaeffler* [2011] O.J. No. 1133 (S.C.J.) at para. 3.